

# IADF BULLETIN



## *FINANCING LOCAL GOVERNMENT*

Volume 1, Issue 2

April, 2004

### **Many Happenings at IADF**

This has certainly been a busy time of year at the IADF. Apart from our normal monthly activities- the newsletter, database research and construction, incorporating suggestions on our website, shaping the organization for next year when we move to being a membership association- we have been hard at work assembling the agenda and logistics for our Second International Conference on Financing Municipalities and Sub-National Governments. Take the time to visit our website, [www.developmentfunds.org](http://www.developmentfunds.org), and sign up for our conference and become an IADF member. We look forward to hearing from you.

Steven G. Thomas  
Manager, IADF  
Editor, IADF Bulletin

### **NEWS DESK**

**--Compiled by Laura Robinson**

#### **BNG reacts to intentions of Minister of Finance**

March 31, 2004  
The Hague  
**Bank Nederlandse Gemeenten**  
[www.bng.nl](http://www.bng.nl)

BNG has been notified of the intention by the Minister of Finance to propose the Dutch Cabinet to discontinue the Corporate Tax exempt status for Bank Nederlandse Gemeenten as from January 1, 2005.

The Minister has indicated that this proposal fits into the general policy of creating a level playing field for government participations after the decision of January 30, 2004 to withdraw the bill "Markt & Overheid" (regulating the commercial market activities by public entities).

In case a bill will be adopted, this will not change BNG's market strategy and BNG's mission as being a bank of and

*Sign Up Now!!!!*

## **SECOND INTERNATIONAL CONFERENCE ON FINANCING MUNICIPALITIES & SUB- NATIONAL GOVERNMENTS**

*September 30 and October 1, 2004*

*The Andres Bello Auditorium of the  
Inter-American Development Bank*

*Washington, DC*

[www.developmentfunds.org/programs.htm](http://www.developmentfunds.org/programs.htm)

for local authorities and public sector institutions. The policy of, on the one hand, competitive pricing and, on the other hand, achieving a reasonable return for the shareholders remains leading. The continuity and the creditworthiness of BNG will not be affected.

## Unemployment rate remains in single digits for second month in a row

April 8, 2004

New Brunswick, Canada

www.gnb.ca

FREDERICTON (CNB) - The unemployment rate remained in single digits for the second month in a row in the province to stand at 9.9 per cent, Training and Employment Development Minister Margaret-Ann Blaney reported today.

Figures released today by Statistics Canada show the New Brunswick seasonally adjusted unemployment rate for March stood at 9.9 per cent, which was the same as the figure reported at the same month last year. The survey also reported that there were 350,200 employed in March which was up slightly from 350,000 at the same time last year. The labor force was 388,800 last month which was also up 300 from when it stood at 388,500 last March.

"We will monitor these figures and our department will continue with its philosophy of providing long-term employment solutions for New Brunswickers," the minister said. "Although we expect some peaks and valleys with these numbers, over the last five years the figures consistently show that we have the fundamentals in place to spark long-term employment growth."

## February deficit of P18.45B better than expected

3/24/2004

Department of Finance, Philippines

www.dof.gov.ph

The budget deficit was better than expected in February, amounting to P18.45 billion or 31.3 percent of the first quarter deficit target of P58.9 billion. Figures from the Department of Finance (DOF) show that a surge in revenues helped cover an 8.4-percent increase in expenditures. With the January deficit recorded at only P16.12 billion, the government can afford a P24.33-billion shortfall in March and still remain within its first quarter target.

The DOF reported that there was an increase in infrastructure spending ahead of the May elections, on top of the increase in debt servicing that pushed spending to a total of P63.1 billion. According to the DOF, the January-February spending was almost two-thirds of the first quarter budget of P210.15 billion, equivalent to a cumulative growth of 7.7 percent.

## INA 's 250 million dollar syndicated "multi-currency" revolving loan

April 9, 2004

Croatia

www.pbz.hr

Industrija nafte, d.d. (INA) has mandated Citibank N.A., ING Bank N.V., Mizuho Corporate Bank, Ltd. and Privredna banka Zagreb d.d. (PBZ) to arrange a \$250 million dollar syndicated "multi-currency" revolving loan.

The loan, which is entirely subscribed by the foreign mandated arrangers, has a repayment period of five years, and is paid half-yearly, beginning from the third anniversary of signing the contract. The loan will be used to finance the general needs of INA. PBZ is the only domestic bank that has been given the mandate to arrange this loan and together with Citigroup it will draw up a document with the relevant data on INA and the Republic of Croatia (Information Memorandum), which will be distributed to potential creditors. INA is currently collaborating

with the mandated arrangers on preparing the syndication of the loan, which should be launched onto the market in the course of this month. The cost of the loan is so balanced that it is favorable for INA, but also brings an attractive yield for potential investors.

INA is owned by the Republic of Croatia (75 percent minus one share) and MOL, the Hungarian integrated oil company, which owns 25 percent plus one share. MOL obtained its share in INA in 2003 and is INA's strategic partner. The synergy of the strategic alliance between INA and MOL creates a platform for strengthening the position of both partners and their expansion on the fast growing market of southeast Europe.

## Rio de Janeiro Government Plans to Wall Off Slums

4/12/04

Brasil

FT.com; VOA News

The government of Rio de Janeiro stated on April 11, that it proposed to build a wall around its sprawling favelas in an effort to help control rampant crime in the city. The government is planning to finance infrastructure projects including water and sewage services in order to prevent favela residents from being segregated.

This announcement came in light of heated violence in an urban drug war that has killed at least 10 people and shut down commerce in the area. The violence broke out over Easter weekend when a rival gang sought to invade and occupy Rocinha, Latin America's largest shantytown, in an attempt to control the drug trade and steal cars. Drug gangs armed with grenades and machine guns, fired relentlessly and local residents were caught in the crossfire. Areas of Rocinha were reported to have resembled a battlefield. Drug gangs, selling mostly cocaine and marijuana, control most of Rio's shantytowns.

"The wall won't put an end to violence [in the slums] but if we don't contain it, it will destroy the [surrounding] forest, the economy of Rio de Janeiro and the lives of the city's residents," Luiz Paulo Conde, deputy governor, said on Monday.

Following the violence, more than 1,200 police officials occupied Rocinha and Vidigal, two slums in southern Rio de Janeiro, in close proximity to the city's beaches. Their patrols sought to re-establish public order.

The situation illustrates the power of drug traffickers in Rio and also the ineffectiveness of the police. Hidden TV cameras have repeatedly filmed police officials and prison guards turning a blind eye on drug traffickers and even taking bribes from them. The military police, subordinate to the state governor, defended its performance, saying violence would have been much worse had it not intervened.

## Low Levels of Aid for poor "Unacceptable"

FT.com

April 25, 2004

James Wolfensohn, the president of the World Bank, on Sunday said the low levels of aid from rich countries contributed to international instability and was unacceptable at a time of unprecedented military spending. "We spend \$900bn on defense globally . . . and we spend between \$50bn and \$60bn on development," he said.

Speaking at the spring meeting of the World Bank and International Monetary Fund, he conceded that progress in stepping up aid to the world's poorest countries remained too slow. He said underdevelopment and a lack of education were among the causes of political instability. Charities said meetings over the weekend had taken only small steps towards achieving the Millennium Development Goals on poverty, education and health. Only five countries have so far hit the target of spending 0.7 per cent of national income in development aid: Denmark, Luxembourg, the Netherlands, Norway and Sweden.

## **G7 Ministers Welcome 'Favorable' Prospects**

FT.com  
April 25, 2004

Finance ministers and central bankers from the Group of Seven high-income countries (G7) on Saturday welcomed the improved outlook for the global economy - but warned of the effects of higher oil prices on economic growth and on the need for emerging market countries to institute policies to reduce external vulnerabilities.

"Prospects are favorable, and although risks remain, such as energy prices, overall the balance of risks to the outlook has improved," the G7 said in a statement following its meeting. "Economic fundamentals have improved in many emerging market countries," it said, "yet, sustained and sound policies are essential to support lasting growth and reduce external vulnerabilities."

Following indicators of a strengthening recovery in the US - including significant employment growth in March - and a decline of the euro against the dollar from its February high, the discussion of foreign exchange markets was less vexed than at recent meetings of the rich country club.

The G7 meeting singled out Argentina in its statement: "In the case of Argentina, progress has been made, but further progress is required." The IMF's supervisory International Monetary and Financial Committee in a communiqué following its meeting called upon Argentina "to continue to push ahead with full implementation of the policies and provisions of its economic recovery program aimed at strengthening growth, including negotiations aimed at reaching a sustainable debt restructuring through a collaborative agreement with creditors."

## **Emerging Debt to Focus on Brazil, Rates**

Reuters  
April 25, 2004

With one eye on the U.S. interest-rate outlook, emerging market bonds are expected to take their cues from Brazil this week, as the government tries to ease poverty while maintaining fiscal discipline.

Emerging market debt has lost 3.6 percent in total returns so far this month, wiping out the gains seen earlier in the year, as investors speculate the likely timing of a widely expected U.S. interest-rate hike.

If rates go up, investors who have financed their purchases of emerging market assets with cheap short-term borrowings in the United States may reduce their leveraged positions.

Hit by the rate fears, Brazil total returns have sunk 5.7 percent so far in 2004 after a 69 percent rally in 2003, according to JP Morgan's Emerging Markets Bond Index Plus. On a positive note, Brazil on Friday easily complied with an International Monetary Fund first-quarter fiscal target and soothed investors' fears that

President Luiz Inacio Lula da Silva might try to spend his way out of recent political troubles. The government, meanwhile, is negotiating with unions and other interest groups to arrive at a plan for increasing Brazil's minimum wage.

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## **Interview with Eduardo Rojas**

Urban Development Specialist, Sustainable  
Development Department  
Inter-American Development Bank

**IADF:** *Can you give us a brief history of the work of the IADB with municipal development funds?*

**ER:** There have been three cycles of support for municipal financing since the early 1970's. Originally, in the 1970's, we followed up with USAID-supported institutions, providing 2<sup>nd</sup> tier financing mostly to institutions in Central America. In the second phase, beginning in the late 1980's, there was a move toward more sustainable institutions in order to leverage more private sector funding. This phase also incorporated transfer funds, which transferred money from the central government to local governments for infrastructure and social development. Examples of this phase include FNDR (National Fund for Regional Development) in Chile and Bolivia, FIS (Social Investment Fund) in a variety of locations. Finally, the third phase has focused primarily on hard-credit discipline and a move towards the private sector. Examples of these institutions include FINDETER in Colombia and PARANACIDADE in Brazil.

**IADF:** *Which municipal funding institutions has the IADB supported?*

**ER:** The IADB has supported institutions in many Central American countries including Guatemala, Honduras, and El Salvador (ISDEM and FISDEL), and also in Costa Rica and Mexico (BANOBAS). In South America, the Bank has lent to institutions in Brazil, Colombia, Chile, and Bolivia with varying levels of success.

**IADF:** *Are there different models in different Latin American countries?*

**ER:** There is a variety of distinct models for development financing institutions in Latin America. The major distinctions involve ownership (state or private) and the extent to which these institutions are self-sufficient and able to leverage funds from the private sector. Others, as mentioned above, still operate as transfer funds, with the source of funding coming directly from the central government.

**IADF:** *Which are some of the better-performing institutions in Latin America?*

**ER:** In terms of their success in becoming self-sustaining and mobilizing private-sector funding, FINDETER in Colombia and PARANACIDADE in the state of Paraná, Brazil have both been very successful. These funds have been able to build hard-credit discipline and have management that is less political than some other institutions.

**IADF:** *How does the future look for local development financing?*

**ER:** The future of sub-national lending looks very promising. This type of lending is critical to the improvement of capital markets and has a very tangible impact on the lives of citizens. The IADB is also trying to improve our capacity to lend directly to municipalities in order to improve efficiency and the availability of funds.

**IADF:** *What is happening in domestic capital markets in Latin America?*

**ER:** A variety of crises over the past decade have prevented the establishment of strong capital markets in Latin America, meaning that municipalities are not allowed to borrow from the private sector. Thus, the proper functioning of these institutions is essential to urban development.

**IADF:** *Are any municipalities issuing domestic bonds? What are the constraints?*

**ER:** A number of municipalities and/or water and sewage companies have issued bonds that are guaranteed by the IADB. This is taking place in Colombia, Brazil (Sao Paulo, Rio de Janeiro), Argentina (Medellin), and Chile. These bonds must meet certain obligations to be backed by the bank, but they are an effective way to secure financing for municipal governments.

**IADF:** *How will these municipal financing institutions eventually fit into a market structure?*

**ER:** Municipal financing institutions currently serve as springboards for further participation of the private sector in lending to local governments. Those that are still dependent on state or IADB/World Bank funding are essentially interim arrangements that are designed to be phased out once capital markets are developed to the point where municipalities can secure funding through the private sector.

## **SPOTLIGHT**



### **- Preston Winter**

**The Kommuninvest Corporation is an interesting and important case of how a cooperative association of municipalities can come together for the purpose of lowering the cost of financing for local development.**

#### **Historical Background to the fund**

Kommuninvest was established in 1986 by a charter signed by the Örebro County Council and 10 municipalities in the county of Örebro, Sweden. Its establishment was a reaction against the unreasonably high cost of financing key investments in the social structure at the local level.

|                                      |  |
|--------------------------------------|--|
| <b>Location</b>                      | <b>Örebro, Sweden</b>  |
| <b>Date Founded</b>                  | <b>1986</b>  |
| <b>Initial Financing</b>             | <b>Municipalities – subscription capital</b>                     |
| <b>Legal Status</b>                  | <b>Owned by a cooperative society with 148 municipal members</b> |
| <b>Total Current Lending</b>         | <b>49.4 billion Swedish kronor (US \$6.5B)</b>                   |
| <b>Credit Rating (Moody's)</b>       | <b>Aaa</b>   |
| <b>Staff (approx.)</b>               | <b>30</b>  |
| <b>President &amp; CEO</b>           | <b>Thomas Åkelius</b>  |
| <b>Chairman, Cooperative Society</b> | <b>Alf Egnerfors</b>   |

#### **Fund Objectives**

To provide the most favorable opportunities possible for raising the finance that is necessary to fund the investment activities of the municipal members. In this way, the company serves the mutual interest of all Swedish municipalities by contributing to reducing

the costs incurred by the public sector when raising the loans it needs.

#### **Primary Activities**

- Kommuninvest lends to its member entities for a variety of projects including infrastructure and educational improvements.
- In order to obtain the necessary equity, Kommuninvest intentionally diversifies its borrowing via different capital markets and currencies.
- Kommuninvest has recently begun providing a number of new services and methods in the area of Finance Support. This largely involves changing the IT-based model for analyzing, optimizing and following up the municipality's own loan portfolio so as to improve the ability to analyze the whole municipal group's financial liabilities.

#### **Ownership, Structure and Operation**

- Kommuninvest is wholly owned by its shareholders, the member municipalities of Sweden.
- The board of the Kommuninvest Cooperative Society composed of representatives from the municipal governments and an executive management team that oversees day-to-day operations.
- By working in a cooperative fashion, overheads are kept to a minimum, especially as Kommuninvest itself works only to cover its costs. The price of loans and all the other conditions concerning the loans are the same for all member municipalities regardless of the size of the loan.

#### **Borrowing**

- Borrowing (for future lending) is divided among the European, Swedish and Japanese capital markets. To achieve the kind of borrowing that is cost-effective over the long term, Kommuninvest takes an active role in providing information about the excellent creditworthiness of the Swedish municipalities.
- Bond issues are made in structured or straight loans with maturities generally of between 2 and 25 years.
- Kommuninvest often participates in buy-backs to re-acquire all or parts of previous bond issues in order to support its book-runners.

#### **Bond-holder Benefits & Security**

- The members of Kommuninvest Cooperative Society are required to sign joint and several guarantees to cover all of the credit market company's obligations.
- The strong financial status of the members and the fact that the municipalities' right to levy taxes is enshrined in the Swedish constitution have contributed to Moody's Investors Service assigning Kommuninvest an Aaa rating for borrowing in foreign currencies.

#### **Performance**

- In 2000, Kommuninvest was able to issue their largest single public bond issue to date, at a value of €500 million.
- The average rate of interest on loans granted in 2003 was 4.2% (2002 4.84%), representing additional benefits for the municipalities.

#### **Credit Criteria**

- At present the members have chosen to adopt a rather restrictive policy towards new investments, which means that most of the current lending is used to refinance old loans.

- Typically, credit is available to any member project. Membership, however, is conditioned by the municipalities' ability to demonstrate that their finances are satisfactory. The analysis covers five different parameters: liquidity preparedness, financial flexibility, financial capacity, commitments and external factors.

**In Case of Default by a borrower**

Although it is very unlikely that there will be a loan default, Kommuninvest is covered in its charter by the cooperative society, which guarantees all of its obligations.

**Project Examples**

Municipalities in Sweden are responsible for the following:

- o social services
- o childcare and care of elderly
- o public utilities (energy, water and sewage, refuse collection)
- o education up to university level
- o road maintenance
- o housing development
- o rescue service
- o protection of the environment.

The financing provided by Kommuninvest helps local governments to provide these services. Kommuninvest is the largest individual lender to the member municipalities, lending, on average, 35% of the total loan portfolios of the member municipalities.

More information from the website [www.kommuninvest.org](http://www.kommuninvest.org)

**SPOTLIGHT**

**Paranacidade**

**- Tridivesh Singh Maini, Laura Robinson, and Yesenia Armijo**

Paranacidade is a non-profit autonomous social service agency, which adheres to private sector rules of regulation. Paranacidade's private sector legal status allows it to operate in a flexible operational environment and provide its services efficiently. It manages and monitors the activities of the Paraná State Urban Development Fund (FDU) which provides financing for municipal investment through State of Paraná funding.

Paranacidade also provides technical assistance for the Institutional Development (ID) of the municipalities of Paraná. Technical Assistance is generally financed by state grants supported by MDB loans. Specific areas of assistance include administrative management, human resource management, tax and financial management, urban planning and information systems.

Paranacidade has a commitment to international outreach. Activities have included the establishment of an international advisory board, publication program, establishment and maintenance of a homepage website, acceptance of foreign delegations, and an English language training program for its staff.

|                         |  |
|-------------------------|--|
| Location                | Paraná, Brazil   |
| Date founded            | June 1996  |
| Initial Financing       | World Bank, IADB, Government of Paraná   |
| Legal Status            | Non-profit social service entity of collective interest with technical, managerial and financial autonomy. |
| Total Fund Assets       | US \$ 4.5 Million (As of 30 December 1999)   |
| Municipalities served   | 399  |
| Urban population        | 9,563,000 (as of 2000)   |
| Projects approved       | 2,547 implemented from 1996-1999   |
| Main sectors of lending | Social Services and Infrastructure   |
| Staff (approximately)   | 104  |
| Chief Executive         | Mr. Renato Guimaraes Adur  |

**Historical Background**

Paranacidade was created in June 1996 as a non-profit autonomous social service agency to take over the functions of FAMEPAR (Paraná State Municipal Assistance Foundation), a state agency which was not able to efficiently service the municipalities.

**Fund Objectives**

The mission of Paranacidade is to lend institutional and technical assistance to the municipalities, to develop activities directed to technological, social and scientific development, and to attract and apply financial resources toward the process of urban development and regional development in the state of Paraná. Objectives include:

- Promote urban, regional, and institutional development.
- Provide technical assistance and institutional capacity building.
- Bring about a qualitative change in the lifestyles.
- Help municipalities improve their provision of social services; and
- Help municipalities raise their own resources for social services and infrastructure.

Through the development of many projects, Paranacidade has created its own project design and development and appraisal capacity. Paranacidade has developed prototype project designs, tender documents and contracts to be used for various community facilities. This feature effectively limits project development costs and implementation time. Additionally, Paranacidade is publishing a report of best practices undertaken by its client municipalities to distribute to the other municipalities.

**Ownership**

The Urban Development Fund (FDU) is owned by the state of Parana. Paranacidade, the management company, is supervised under contract by the State Secretariat of Urban Development, and is accountable to the State Legislator Power. The Executive Board consists of:

Superintendent: Renato Guimaraes Adur

Executive Superintendent: Luiz Forte Netto

Director of Operations: Miryan Kravchychyn

Director of Administration and Finance: Jorge Gomes Rosa Filho

The full Board of Directors consists of the Secretariat of State for Urban Development for the State of Paraná; the Federation of Associations of Municipalities of Paraná; the Secretariat of State for Finance of Paraná; the Secretariat of State for Planning and General Coordination of Paraná; the Institute of Architects of Brazil; the Federation of Industries of the State of Paraná; the Federation of Commerce of Paraná; and the Institute of Engineering of Paraná.

## Operations

Paranacidade's operation is highly decentralized with approximately 120 employees total and five regional offices. An interesting innovation is the close working relationship that Paranacidade has formed with 18 regional municipal associations. The municipal associations have a few in-house technical staff and these are used by Paranacidade to assist in the implementation, evaluation and supervision of some small-sized projects.

Involvement of the municipalities through their municipal associations in the identification and implementation of projects has increased operational efficiency, and a sense of ownership on the part of the municipalities. Paranacidade has developed positive relationships with its municipal clients as a result of its commitment to development and its expertise.

## Lending conditions:

Municipalities borrowing from Paranacidade must pledge an intercept of State devolution funds due to the municipality in case of default.

A federal "fiscal responsibility" law defines strict limits on municipal borrowing. Paranacidade has developed its own software to model maximum borrowing levels of each municipality.

## Non-performing loans:

As a result of the collateral provided by the intercept mechanism and the active involvement of the regional municipal associations non performing loans are essentially zero.

## Paraná Urbano:

Parana Urbano is the name given to the urban development program financed by the FDU and supported by the Inter-American Development Bank. During the period 1996-1999 Paraná Urbano financed 2,356 projects of which 1,942 were investment projects and 414 were institutional development projects. Basic infrastructure represents the largest share of projects at 84 percent, and among these projects, street paving, water and sewerage and heavy equipment constitute the majority. 380 out of 399 Paraná municipalities have benefited from Paraná Urbano.

## Some of the larger Clients of Paranacidade and FDU include:

### Curitiba

Curitiba is the capital of the Paraná state and is classified as a metropolitan city. The city has long been known around the world as one of the best planned and managed cities. However it has recently experienced a significant population growth.

FDU and Paranacidade have been helpful in providing assistance in the development of their water and sewage systems.

### Cascavel

Cascavel is a second level municipality and regional center known for its agriculture, industrial parks, exposition park, cooperatives and higher education schools. Cascavel was created under State Law No. 790 on November 14, 1951 and was dismembered from the municipality of Foz do Iguacu.

### Maringá

Maringá's economy is based on industrial agriculture. The municipality is connected to main major parts of Brazil through its road and railroad network. Maringá was created under State Law No. 790 on November 14, 1951 and was separated from the municipality of Mandaguari.

## SANEPAR

(Companhia de Saneamento do Paraná)

The Sanitation Company of the State of Paraná was created in 1963 as a state sanitation company. After over 40 years of business, SANEPAR is providing water services to up to 98 percent of the population. SANEPAR fully covers its costs, including capital depreciation costs without receiving any direct subsidy from the government. Indirect subsidies are received in the form of loans available from public financial institutions including FDU/Paranacidade. Under Paraná Urbano, SANEPAR received a loan of R\$60 million to assist with increasing the coverage of the sewage system.

**We invite submissions of comments, news items,  
and suggestions for future articles.**

**Please do not hesitate to contact us, your input is  
valued as we develop our newsletter.**

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