



## Economic development and employment

# Financial Market Stability and Capital Market Development

### The challenge

An efficient and stable financial sector is key to developing a broader, deeper economy based on the division of labor. By agglomerating, allocating and monitoring capital, the financial sector assures the most productive use of capital while at the same time risks are transferred, pooled, mitigated and reduced. The financial sector in our partner countries is often unable to fulfill this role in an efficient and sustainable way.

In order on the one side to profit from the financial sector on the individual, corporate and economy level, and on the other side to avoid disruptions of the financial sector which can have negative externalities on the real economy, the financial sector has to be developed and adopted so that it fulfills the specific needs of the respective partner country.

### Our approach

Next to private actors, the government and its various institutions play a distinct role in assuring the efficiency and stability of the financial sector. GIZ supports political and financial decision makers in its partner countries in their efforts to improve the local financial systems.

Creating a stable and efficient financial sector is a complex process involving the interconnectivity of various actors. GIZ faces this challenge by applying a multi-level-approach to “Financial Market Stability and Capital Market Development” which is centered around macro and meso elements and activities.

### Our services

Our services regarding “Financial Market Stability and Capital Market Development” focus on capacity development as well as technical and process oriented advisory services for

our partners. Doing this, we focus on five key areas, which are represented in the following five modules.

#### *Financial Regulation and Supervision*

The regulatory and supervisory authorities shape the frameworks in which financial relationships and interactions take place. GIZ is working together with the relevant financial market authorities in order to create a both enabling and stable environment for the different actors in the financial system. GIZ focuses on two aspects: On the one side we assist both financial market authorities and the banking industry in developing and implementing risk management standards. In this respect, also environmental risk assessment is gaining importance. On the other side, GIZ assists partner countries in complying with international supervisory standards such as the Basel frameworks.

#### *Financial Market Infrastructure*

If obstacles such as information asymmetries and high transaction costs prevail, the financial sector cannot fulfill its role as matchmaker of market participants. The financial market infrastructure helps overcoming market failures and imperfections in the financial sector by reducing transaction costs and information asymmetries. GIZ assists partner countries in the development of payment systems, credit bureaus, deposit insurance schemes and APEX organization. This financial market infrastructure helps deepening, and thus also stabilizing, the financial system.

#### *Monetary Policy*

By controlling the interest rates and / or the supply of money, monetary policy influences inter alia economic growth, inflation, and exchange rates. Thus, monetary policy is a key element in steering the economy. GIZ supports policy makers in developing adequate central bank laws, which reflect adequate objectives and instruments for the central bank. Furthermore GIZ provides assistance to central banks in developing and executing a credible and independent monetary policy.



### *Capital Market Development*

Capital markets broaden the choice of refinancing and investment instruments amongst others for companies and the government. The financial system in most developing countries, however, relies heavily on the banking sector, while the markets for debt and equity remain underdeveloped. GIZ assists partner countries in the development of efficient debt and equity markets by advising regulatory authorities in establishing adequate frameworks and enabling environments. Furthermore we support intermediary institutions such as stock exchanges or clearing mechanisms.

### **The benefits**

The services of “Financial Market Stability and Capital Market Development” enable public and private institutions in our partner countries to create, develop, maintain and manage a financial sector which balances the paradigm of access of participants to financial services and the paradigm of stability of the financial system. Only a financial system that balances these paradigms can serve its various stakeholders in an efficient and sustainable way.

### **An example from the field**

As Vietnam’s integration in the global economic system progresses, its macroeconomic institutions need to keep pace and set the appropriate conditions for a smooth transition to a market-based financial system. An important aspect here is an efficient market for government bonds.

As part of the program to strengthen key market institutions, GIZ provides support to various actors in the government bond market. As a first milestone, GIZ supported the State Securities Commission in the development of a strategy to strengthen the bond market and assisted in the drafting of the securities law. Furthermore, GIZ supported the establishment of an independent clearing house, helped to concentrate the bond trading at Hanoi Stock Exchange and advised in the establishment of a specialized electronic trading system. Thanks to a GIZ supported program for cash-neutral exchange of government bonds, market liquidity could be raised substantially. GIZ also assisted in the development of new products, such as bond indices and bond futures as well as in the drafting of a government regulation on derivatives. Together with GIZ, the Vietnamese partners recently developed a concept for the establishment of a Central Counterparty as well as for transferring cash-settlement from the Central Bank to a commercial bank.

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