Advanced International Capital Movements

October 16, 2025

Contents

I. Class Schedule

1. October 16: AML/CFT, Bond Investment, Quiz1
2. October 30: Mid-term Exam

II. AML/CFT

1. FATF's 40 Recommendations

The **FATF (Financial Action Task Force)** has established a comprehensive framework of **40 Recommendations** that serve as the global standard for combating **money laundering (AML)**, **terrorist financing (CFT)**, and **proliferation financing (CPF)**.

Below is a clear and structured summary suitable for college or graduate students studying **international trade, finance, or compliance**.

🌐 Overview

- **Established:** 1989 by the G7 countries
- **Purpose:** To protect the international financial system from misuse — especially for **money laundering, terrorism financing, and proliferation of weapons of mass destruction**.
- **Nature:** The FATF issues *recommendations*, not laws — but member countries must implement them through national legislation and regulation.

♦ Structure of the 40 Recommendations

A. AML/CFT Framework and Policies (Rec. 1–2)

1. **Risk-Based Approach (RBA):**

   Countries and financial institutions must identify, assess, and mitigate money laundering and terrorist financing risks.

2. **National Cooperation and Coordination:**

   Ensure national policies and coordination among law enforcement, regulators, and policy makers.

B. Money Laundering and Confiscation (Rec. 3–4)

3. **Criminalize Money Laundering:**

   ML must be a criminal offense based on the Vienna and Palermo Conventions.

4. **Confiscation and Freezing:**

   Allow authorities to freeze and seize criminal assets and proceeds of crime.

C. Terrorist and Proliferation Financing (Rec. 5–8)

5. **Criminalize Terrorist Financing**
6. **Targeted Financial Sanctions (Terrorism & Terrorists)**
7. **Targeted Financial Sanctions (Proliferation of WMD)**
8. **Non-Profit Organizations (NPOs):**

   Prevent misuse of charities for terrorist financing.

D. Preventive Measures (Rec. 9–23)

9. **Financial Institution Secrecy Laws:** Must not inhibit AML/CFT implementation.
10. **Customer Due Diligence (CDD):**
    Identify and verify customers, beneficial owners, and the purpose of the relationship.
11. **Record-Keeping:**
    Keep transaction and identification records for at least five years.
12. **Politically Exposed Persons (PEPs):**
    Apply enhanced due diligence to high-risk individuals.

    13–16. **Correspondent Banking, New Technologies, Wire Transfers, etc.**

    17–19. **Third-Party Reliance, Higher-Risk Countries, Enhanced Due Diligence.**

    20–23. **Reporting Suspicious Transactions, Internal Controls, DNFBPs (Designated Non-Financial Businesses and Professions)** — e.g., lawyers, casinos, real estate agents.

E. Transparency and Beneficial Ownership (Rec. 24–25)

24. **Legal Persons:**

    Identify and maintain information on ultimate beneficial owners of companies.

25. **Legal Arrangements (Trusts):**

    Similar transparency requirements for trusts and foundations.

F. Powers and Responsibilities of Authorities (Rec. 26–35)

26–27. **Regulation and Supervision of Financial Institutions**

28. **Supervision of DNFBPs**

29. **Financial Intelligence Unit (FIU):**

Central body to receive and analyze suspicious transaction reports (e.g., Korea's KoFIU, U.S. FinCEN).

30–31. **Law Enforcement and Investigative Authorities**

32–35. **Powers for Confiscation, Mutual Legal Assistance, and International Cooperation**

G. International Cooperation (Rec. 36–40)

36. Mutual Legal Assistance (MLA)
37. Extradition for ML/TF Offenses
38. Freezing and Confiscation Assistance

    39–40. Information Exchange among FIUs and Supervisors

III. Global Bond Markets

🌍 1. What is the Global Bond Market?

The **global bond market** is the worldwide marketplace where **governments, corporations, and supranational institutions** issue and trade **debt securities (bonds)** to raise capital.

- **Purpose:** To finance spending, investment, or refinancing existing debt.
- **Participants:** Governments, central banks, corporations, institutional investors, hedge funds, and individuals.
- **Size:** As of 2025, global bond markets exceed **$130 trillion USD**, making them larger than global equity markets.

💡 2. Classification of Bonds in the Global Market

(1) Domestic Bonds

- Issued by a local borrower in its **own currency** and **home market**.
- Example:
  - **U.S. Treasury Bonds** issued in USD in the U.S.
  - **Korea Treasury Bonds (KTBs)** issued by the Korean government in KRW.

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(2) Foreign Bonds

- Issued by a foreign borrower in a **domestic market**, using the **domestic currency** of that market.
- Examples:
  - **Yankee Bonds:** Issued in the U.S. by a foreign company (e.g., Toyota issuing USD bonds in New York).
  - **Samurai Bonds:** Issued in Japan by a foreign firm (e.g., Apple issuing JPY bonds).
  - **Bulldog Bonds:** Issued in the U.K. by non-U.K. entities (e.g., Korea Electric Power issuing GBP bonds).

(3) Eurobonds

- Issued in a **currency different from the country's domestic currency** and **sold internationally**.
- Example:
  - **Eurodollar Bond:** USD-denominated bond sold outside the U.S. (e.g., Samsung issues a USD bond in London).
  - **Euroyen Bond:** JPY-denominated bond issued outside Japan (e.g., BMW issues JPY bonds in Singapore).

💬 *Note:* "Euro" in Eurobond does **not** mean "Europe" or "Euro currency" — it refers to **internationally issued** bonds.

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(4) Global Bonds

- Bonds issued **simultaneously** in multiple markets and currencies.
- Example:
  - **World Bank Global Bond:** USD-denominated bond issued in New York, London, and Tokyo at the same time.
  - **Apple Global Bond (2023):** Issued USD bonds globally to raise funds for share buybacks and R&D.

🏛️ 3. Major Players in the Global Bond Market

Type of Issuer	Example	Purpose
Sovereign Governments	U.S. Treasury, Japan, Korea, Germany	Fund fiscal deficits
Supranational Organizations	World Bank, IMF, Asian Development Bank	Support development projects
Corporations (MNCs)	Apple, Toyota, Samsung	Finance expansion, M&A, or refinance debt
Municipalities	State or city governments	Fund local infrastructure

🔍 5. Key Characteristics

Feature	Explanation
Liquidity	U.S. Treasuries are the most liquid instruments in the world.
Currency Risk	Global investors face FX risk when investing in foreign bonds.
Credit Risk	Assessed through credit ratings (Moody's, S&P, Fitch).
Interest Rate Risk	Bond prices fall when interest rates rise.
Hedging	Investors use derivatives (swaps, futures) to manage risks.

Bond Investment

📉 1. Relationship Between Bond Price and Market Yield

🔹 Inverse Relationship

- **When market yields (interest rates) rise → bond prices fall.**
- **When market yields fall → bond prices rise.**

This happens because the **coupon payments** on existing bonds become **less or more attractive** compared to the new market rates.

🔸 Example

Market Condition	Market Yield	Effect on Bond Price
Interest rates rise	from 3% → 4%	Existing 3% bonds fall in price
Interest rates fall	from 4% → 2%	Existing 4% bonds rise in price

⏱️ 2. The Role of Duration

Duration measures a bond's **sensitivity to interest rate changes** — in other words, *how much the price of a bond will move if the yield changes by 1%.*

🔹 Types of Duration

1. **Macaulay Duration:**
   Weighted average time (in years) to receive the bond's cash flows.
   - Example: A 10-year bond might have a Macaulay duration of 7.2 years.
2. **Modified Duration:**
   Measures price sensitivity to yield changes.
   - Formula:

$$\text{Modified Duration} = \frac{\text{Macaulay Duration}}{(1+y)}$$

   - Meaning: If duration = 7, a 1% increase in yield → price drops ≈ 7%.

Duration

$$D_{Macaulay} = \frac{\sum_{t=1}^{n} \frac{C_t}{(1+r)^t}(t)}{\sum_{t=1}^{n} \frac{C_t}{(1+r)^t}}$$

$$D_{Macaulay} = \left[\frac{\text{Macaulay Duration}}{\left(1 + \frac{YTM}{f}\right)}\right]$$

- Duration-Price Relationship
  - Price change is proportional to duration and not to maturity

$$\frac{\Delta P}{P} = -D\left[\frac{\Delta(1+y)}{1+y}\right]$$

  - D^* = Modified duration

$$\frac{\Delta P}{P} = -D^* \Delta y$$