Banco de Inversión y Comercio Exterior

LII Reunión Anual de la AAEP

Panel sobre
Financiamiento y Banca de Desarrollo

Bancos de Desarrollo:
Algunas preguntas y respuestas

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Bariloche, 17 de noviembre de 2017

Development Banks:

What are they, and what are they for?

Development Banks vs. Commercial Banks

➢ *Commercial Banks:*

- ✓ Are typically privately-owned, but some are state-owned
- ✓ Take deposits from the public
- ✓ Do only first tier (directly to borrowers)
- ✓ Lend to both firms and households
- ✓ Lend both short (mostly) and long term, and for both consumption and investment

➢ *Development Banks:*

- ✓ Are state-owned *(all DB are state-owned, but not all state-owned banks are DB)*
- ✓ Do not take deposits from the public
- ✓ Do both first and second tier (through private commercial banks)
- ✓ Lend only to firms
- ✓ Lend mostly for investment uses (not working capital) and long term
- ✓ Focus on clients underserved by commercial banks

How many DB worldwide? Broad definition: some 400; Narrow definition: some 100.

The Rosy View: Market Failures as DB Rationale

⇨ **Asymmetric information and intermediation costs**

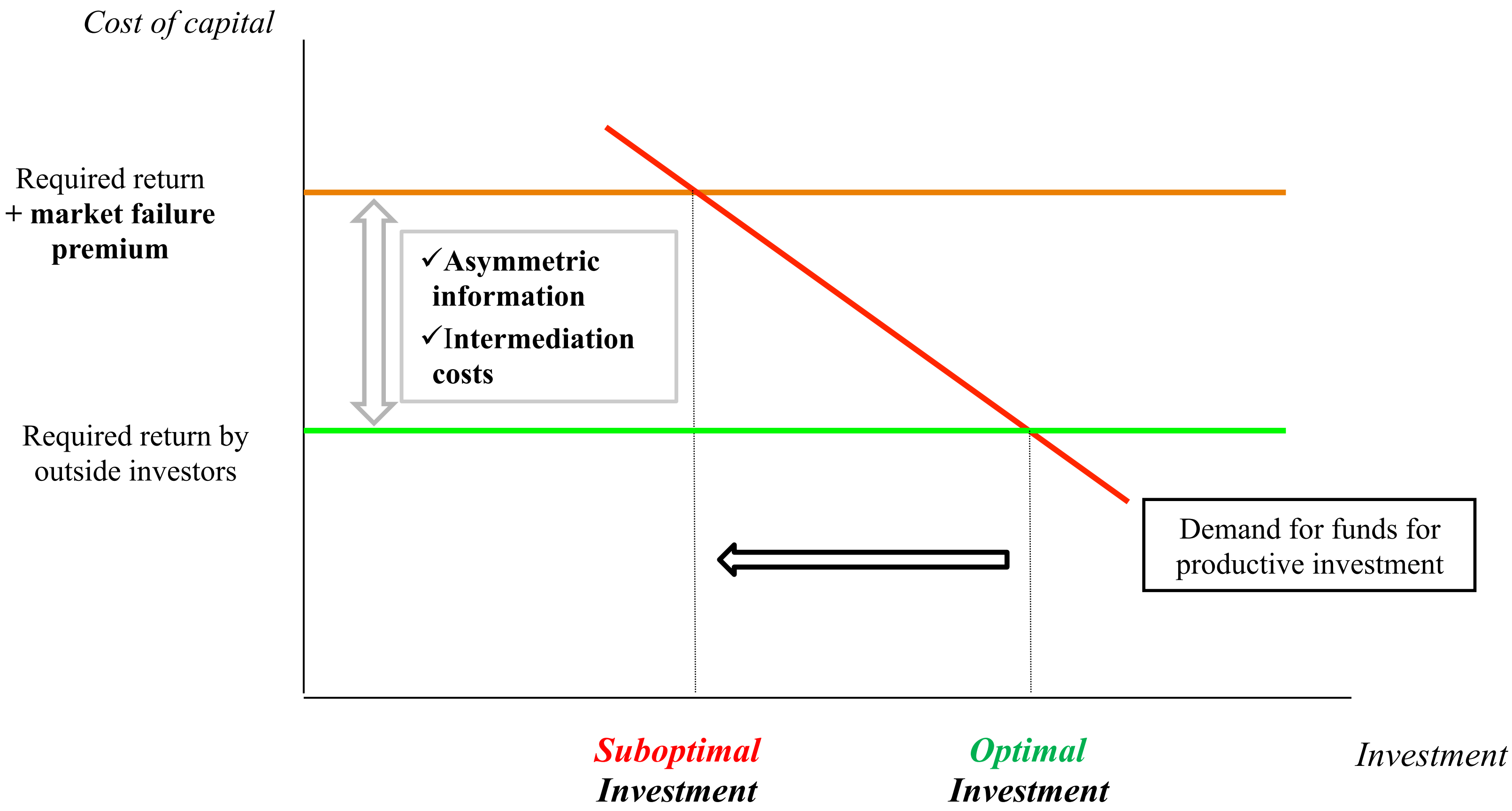
- *Adverse selection*
- *Moral hazard*
- *Financial intermediation costs in connecting savers and borrowers*

Due to opacity and small scale, these barriers are more intense in the case of young firms or first time borrowers

⇨ **Externalities**

- *Underfunding of socially valuable projects with low value to commercial banks*

Productive investment and financial market failures



The Gloomy View: Much Ado about Nothing?

DBs look great on paper, but in practice they face colossal challenges to live up to their promise:

- ✓ Hard to pinpoint firms worth serving *(more on this next)*
- ✓ Agency problems
- ✓ Distortive political interference
- ✓ Fiscal costs

What does the evidence say?

- Not much, mainly due to data constraints:

- Some qualitative surveys on DBs around the world, administered by the World Bank, IDB and the Canadian BDC

- A handful of more rigurous (and data-intensive) studies for LAC, produced by the IDB for such countries as Brazil and Colombia.

    - *Too few studies to pass judgment*

    - *Badly needed transparency and data disclosure to improve accountability and impact evaluation*

Development Banks:

Some questions and answers

Complementarity or competition with comercial banks?

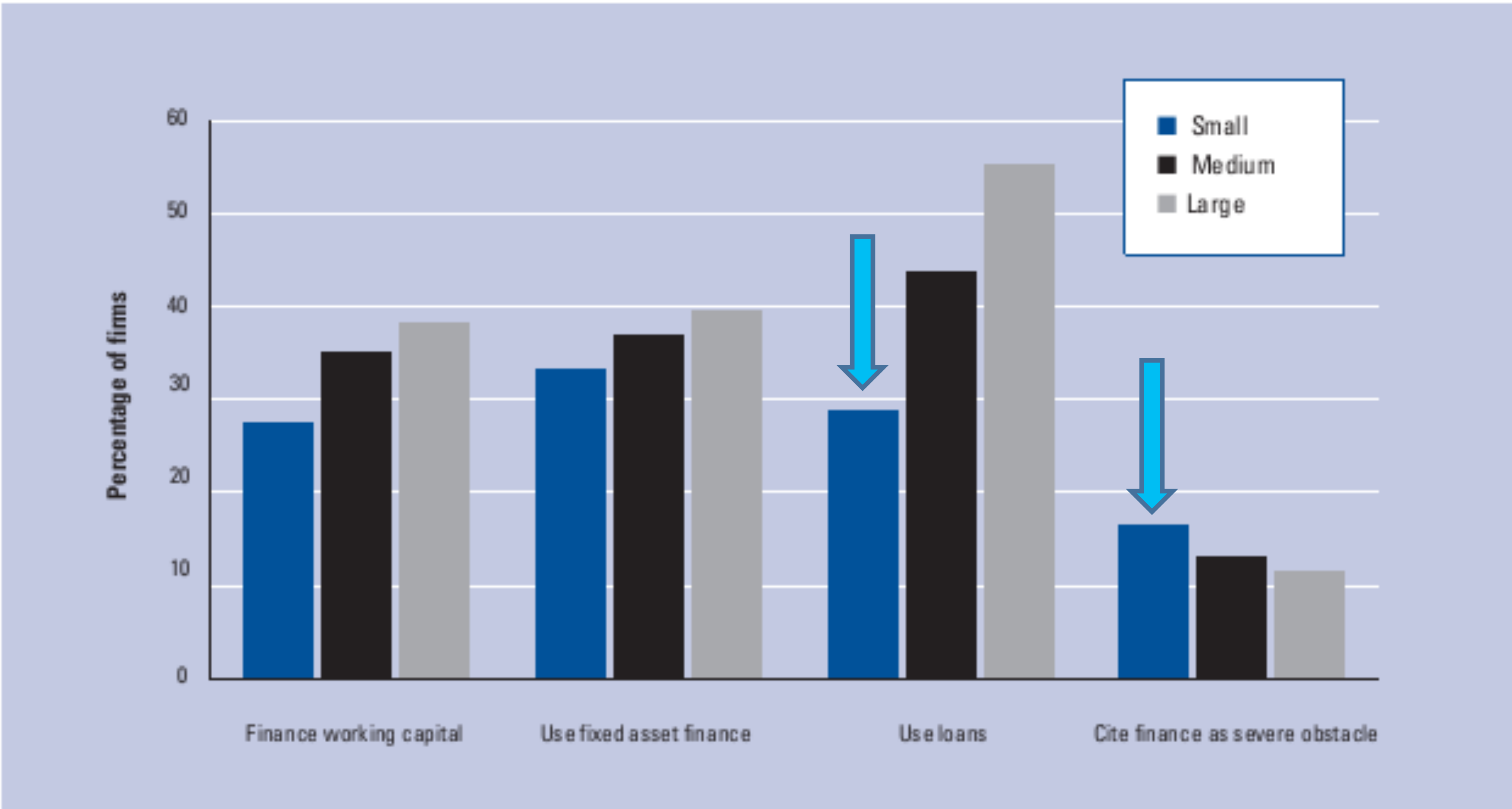
⇨ DBs should do what others banks cannot or do not want to do

❖ Why? Avoid mere **crowding-out**, with zero or negative social value added

❖ How? **Financial inclusion** (small firms) and **longer maturities** (all firms)

Credit supply or credit demand constraints?

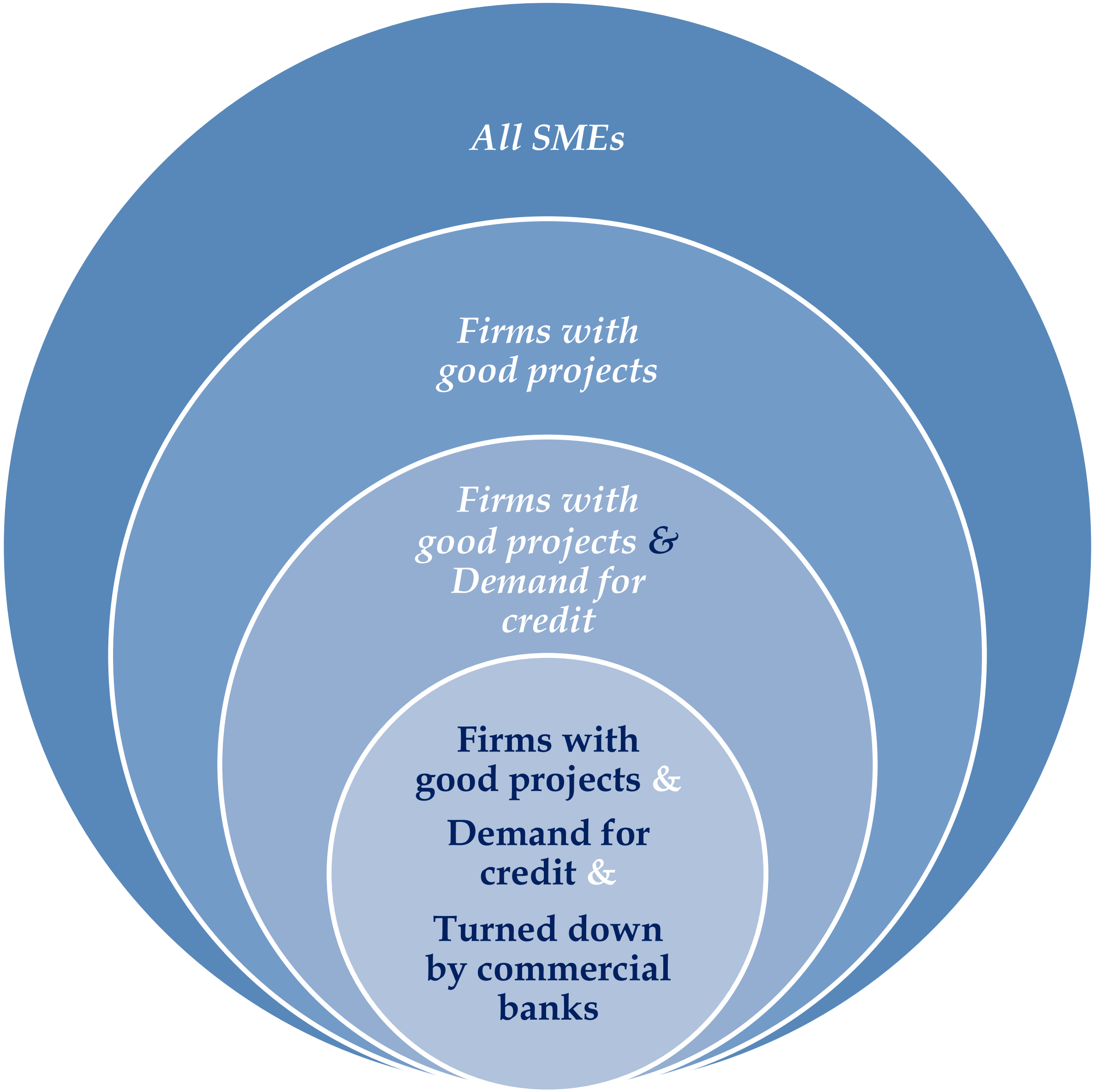
Figure 1: Comparison of financing of small, medium, and large enterprises



Source: The World Bank's Enterprise Surveys and author's calculations. Averages across firms and countries are from Enterprise Surveys undertaken between 2005 and 2009.

Firms of all sizes, and everywhere, prefer self-financing (pecking order)

Massive or selective clientele?



Additional DB debates

- ***High or low target profitability?***
  - ✓ Positive but below market for financial sustainability. Too high returns should be channeled toward more bening loan conditions.
- ***High or low target NPL ratio?***
  - ✓ Reasonably low, but most likely higher than peers -in light of its mandate, DB must tolerate more risk.
- ***First or second tier?***
  - ✓ Both. In first tier, better control over credit allocation. In second tier, broader clientele base and scalable operation.
- ***Small or big firms?***
  - ✓ Mostly small, but big firms provides economies of scale and may need maturity stretching

Additional DB debates

- ***Hard or soft information in screening applicants?***

✓ Both. But in order to complement CBs and not to fish in the same pond, they should lean more towards soft information-based techniques.

- ***Startups and microcredits?***

✓ Not directly. They require screening and monitoring technologies unfamiliar to most banks. But feasible via second tier to specialized intermediaries.

- ***Target firms or sectors?***

✓ Firms, as long as they meet the basic conditions (i.e., genuine financial constraint). Picking winning sectors has typically proved to be an elusive task.

- ***Permanent or temporary DB assistance?***

✓ Temporary, only until building good credit history and hence CBs become willing to take on the client.

- ***Standard or lax regulation?***

✓ Lax, but still under proper control so as to remain accountable.

Additional DB debates

- ***Concessional or market funding?***

✓ Both. Concessional funding enables to maintain acceptable rates to risky borrowers and do long-term lending.

✓ But market funding brings much needed market discipline and hardened budget constraint.

- ***Subsidized or market interest rates?***

✓ Subsidized rates as an exception, not a rule. For firms without credit or only short-term, access is subsidy in itself.

✓ Risky businesses should not pay corporate prime rates, because of:

(a) *Steep administrative costs from lending small amounts to unknown firms*

(b) *Contingent fiscal cost,*

(c) *Subsidized DB loan rates may lead CBs to focus on big clients away from SMEs*

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