

What Do State-Owned Development Banks Do? Evidence from BNDES, 2002–09

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Summary. — Defendants of state-owned development banks emphasize their role in reducing capital constraints and fostering productive investment; detractors point out that they may benefit politically connected capitalists or bail out inefficient firms. We study the effect of loans and equity investments of the Brazilian National Development Bank (BNDES) and find that they do not have any consistent effect on firm-level performance and investment, except for a reduction in financial expenditures due to the subsidies accompanying loans. However, BNDES does not systematically lend to underperforming firms. Our results indicate that BNDES subsidizes firms that could fund their projects with other sources of capital.

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1. INTRODUCTION

This paper studies the implications of long-term credit provided by state-owned development banks. Such banks are financial intermediaries that specialize in providing long-term credit—usually subsidized—to promote industrialization or infrastructure projects (Armendáriz de Aghion, 1999). Different from multilateral banks, state-owned development banks are controlled by national governments and generally have a mandate to support local business activity. These banks have been credited with a central role in the financing of industrialization in East Asia, Latin America, and Europe (e.g., Amsden, 2001; Aronovich & Fernandes, 2006; Cameron, 1961; Rodrik, 2004) and are still important suppliers of credit in emerging and even developed markets. In 2012, Germany's KfW, Brazil's BNDES, and the China Development Bank had outstanding loans representing, respectively, 15.5%, 11.3%, and 12.4% of their countries' GDP (Ferraz, Além, & Madeira, 2013).

Yet, despite their size and importance, we do not have a clear understanding of what development banks do in practice. Although there is a large literature examining state-owned banks (Cole, 2009; Dinc, 2005; Khwaja & Mian, 2005; La Porta, Lopez de Silanes, & Shleifer, 2002), development banks are a peculiar and understudied type of lender. Unlike state-owned commercial banks, which tend to provide generalized lending similar to that of private banks, development banks specialize in long-term lending to promote new industries and firms. In other words, such banks are supposed to have specialized competencies and a clear mandate to spur industrial development (e.g., Armendáriz de Aghion, 1999). Yet we have few studies examining their behavior in detail. Most of the work on development banks and their relationship to industrial policy is either theoretical (Amsden, 1989; Armendáriz de Aghion, 1999; Aronovich & Fernandes, 2006; Bruck, 1998) or based on qualitative case studies of developing or newly industrialized

countries (Amsden, 1989; Amsden, 2001; Fordwor, 1981; Ndongko, 1975; Rodrik, 2004).

In this paper, we use firm-level evidence from Brazil to examine what happens when development banks target local firms and the factors that can explain how banks allocate their loans to and investments in such firms. Brazil offers a good laboratory for this inquiry because the Brazilian National Bank for Economic and Social Development, known as BNDES for its Portuguese acronym, is one of the largest development banks in the world. Founded in 1952 to provide long-term credit for infrastructure projects, BNDES soon became a central venue for the capitalization of domestic and foreign groups investing in Brazil (Leff, 1968). Despite Brazil's privatization wave in the 1990s, BNDES remains an important source of capital in the economy; its loans represent more than 20% of the total credit to the private sector (Figure 1) and the bulk of the long-term credit. We thus built a unique database of

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