Key findings

The allocation of resources of National Development Banks: Does it fit development goals?

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THE VISIBLE HAND:
Development Banks in Transition

Developing countries will not be able to achieve the 2030 Sustainable Development Goals if some regions are left out. Inequalities across regions and populations within countries are fundamental factors explaining the rise of discontent, political instability and ultimately, fragility and internal conflicts. By virtue of their developmental mandate, local expertise and relays, National Development Banks (NDBs) should be able to operate and invest in the most vulnerable regions where the risk is often very high. The purpose of this study is to reflect on the mandates of NDBs and the role they can play to address the scarcity of financing in vulnerable areas.

Objectives and research questions

The starting point of this study is the question of whether public financial institutions and NDBs in particular are well suited to fill financing gaps in underserved markets. The authors seek to know if they are able to operate in the most vulnerable regions, where the risk is often too great for a majority of private actors, and notably for private commercial banks.

Methods

Examining the links between local factors and NBDs activity allows us to shed light on the strength and nature of their development mandates. Using firm-level data for 127 countries over 2006-2018, the paper estimates how a number of factors can determine the probability of getting a loan or line of credit from a public bank, versus a private commercial bank. They range from firm-level factors such as company size or labor productivity levels, to local factors like regional workforce education levels, as well as country-level factors, such as global economic shocks.

Results

First, the paper finds that on average, there is no significant difference in terms of productivity levels between firms accessing private finance, compared to public finance.

Second, NDBs tend to provide more finance in less developed localities, relative to private commercial banks.

This reflects the riskier position public banks are taking compared to private banks in developing countries. It doesn't necessarily mean that public banks are less able to detect riskier investments; it reflects rather their particular strategy regarding development goals. Public banks seem to be able to manage more risks related to the local context, which fall outside of the direct control of the firm but might affect their future portfolio performance. Examples include: insecurity and lower infrastructure resilience to climate shocks.

Evidence also supports the emerging consensus that public banks play a countercyclical role by strengthening their credit offer during difficult times, which is particularly pertinent for the current Covid-19 pandemic.

Recommendations

- **Governments can play an active role in providing access to finance to the private sector directly through NDBs**, when global, national or local conditions are such that private commercial banks consider the risk too high.
- **Adapting the mandate of public banks to take into account the SDGs is a critical step to ensure they remain relevant.** Not reviewing their mandate may prevent NDBs from evolving and adjusting to the ever-changing environment in which they operate, and from realizing their potential as leading actors in vulnerable situations.
- **Designing financing instruments that are adapted to a riskier environment** is necessary to ensure that public banks respond to the special needs that firms are facing in vulnerable areas.

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Access the research paper

THE ALLOCATION OF RESOURCES OF NATIONAL DEVELOPMENT BANKS: DOES IT FIT DEVELOPMENT GOALS?