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Development Banks from the BRICS

Barbara Barone and Stephen Spratt

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DEVELOPMENT BANKS FROM THE BRICS

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Abbreviations

AAC	Asociación Ambiente y Sociedad de Colombia
ABC	Brazilian Cooperation Agency
ADB	African Development Bank
ADB	Agricultural Development Bank
AEBF	Asian Exim Banks Forum
AEX	Foreign Trade Division [Brazil]
AFD	Agence Française de Development [South Africa]
AfDB	African Development Bank
AI	Industrial Division
AIE	Infrastructure Division
AIIB	Asian Infrastructure Investment Bank
APP	Asia Pulp and Paper
ARF	African Renaissance Fund
ARPA	Amazon Region Protected Areas
ASEAN	Association of Southeast Asian Nations
b/d	barrels per day
BANDES	Bank for Economic and Social Development [Venezuela]
BDC	Business Development Bank of Canada
BNDES	Brazilian Development Bank
BNDESPAR	BNDES Participações S.A.
BRICS	Brazil, Russia, India, China and South Africa
CADF	China-Africa Development Fund
CBRC	China Banking Regulatory Commission
CBSS	Council of the Baltic Sea States
CCP	Chinese Communist Party
CCXG	Climate Change Expert Group
CDB	China Development Bank
CDC	Caisse des Dépôts et Consignations
CDES	Centro de Derechos Económicos y Sociales
CEBRI	Centro Brasileiro De Relações Internacionais
CEC	Committee for Eligibility, Credit and Capital
CEDLA	Centro de Estudios para el Desarrollo Laboral y Agrario
CID	Center for International Development
CINDES	Centro de Estudos de Integração e Desenvolvimento
CIS	Commonwealth of Independent States
CLN	Corredor Logístico Integrado do Norte [Integrated Northern Logistical Corridor]
COFA	Amazon Fund Guidance Committee
COMESA	Common Market for Eastern and Southern Africa
CR	crore
CSR	corporate social responsibility
CTFA	Amazon Fund Technical Committee
DAC	Development Assistance Committee
DAFC	Department of Aid to Foreign Countries
DAR	Derecho, Ambiente y Recursos Naturales
DBSA	Development Bank of Southern Africa
DEA	Department of Environmental Affairs
DEFAM	Amazon Fund Department
DEMAM	Department of Environmental Policies and Studies
DEOPE	Green Financing Department
DEPRI	Department of Priorities and Planning
DFI	development financing institution
DFID	Department for International Development

DOE	Department of Energy
DRC	Democratic Republic of the Congo
EAC	East African Community
ECA	export credit agency
ECGC	Export Credit Guarantee Corporation of India
ECOWAS	Economic Community Of West African States
EDC	Export Development Canada
EIA	environmental impact assessment
EIB	European Investment Bank
ELLA	Evidence and Lessons from Latin America
EPC	Engineering, Procurement and Construction
EPE	Brazilian Government Energy Research Company
ERA	Executive Research Associates
ESCO	energy service company
EU	European Union
EXIAR	Russian Export Credit Agency
EXIM	export-import
FAS	Amazon Sustainable Foundation
FAT	Fundo de Amparo ao Trabalhador
FDI	Foreign Direct Investment
FGCE	Fundo Garantidor de Comércio Exterior [Foreign Trade Guarantor fund]
FIDC	Fundo de Investimento em Direitos Creditórios
FINAME	Machinery and Equipment Financing Programme
FINANEX	Machinery and Equipment Export Financing Programme
FMM	Merchant Maritime Fund
FND	National Development Fund
FNMC	National Fund on Climate Change
FNS	Ferrovia Norte-Sul
FOCAC	Forum on China-Africa Cooperation
FUNTEC	BNDES technology fund
GDP	gross domestic product
GEF	Global Environment Facility
GHG	Greenhouse gas
G-NEXID	Global Network of Exim Banks and Development Finance Institutions
GOI	Government of India
GWEC	Global Wind Energy Council
HIPC	Heavily indebted poor countries
HSRC	Human Sciences Research Council
IBASE	Instituto Brasileiro de Análises Sociais e Econômicas
IBGE	Brazilian Institute of Geography and Statistics
IBRD	International Bank for Reconstruction and Development
IBSA	trilateral development initiative
ICT	information and communications technology
IDB	Inter-American Development Bank
IDBI	Industrial Development Bank of India
IDC	Industrial Development Corporation
IDCR	Indian Development Cooperation Research
IDEAS	India Development and Economic Assistance Scheme
IDI	India Development Initiative
IDS	Institute of Development Studies
IEA	International Energy Agency
IEC	Independent Electoral Commission
IFC	International Finance Corporation
IFCI	Industrial Finance Corporation of India
IMF	International Monetary Fund

IOV	Ouro Verde Institute
IPC	Internationale Projekt Consult
IPEA	Instituto de Pesquisa Econômica Aplicada
IPR	intellectual property rights
ITEC	International Travel and Education Company
JBIC	Japan Bank for International Cooperation
KfW	Kreditanstalt für Wiederaufbau
LAC	Latin America and Caribbean
LGFV	local government financing vehicle
LIBOR	London Interbank Offered Rate
LIHD	Low Income High Level of Debt
LLC	limited liability company
LOC	line of credit
M & E	Monitoring & Evaluation
MEA	Ministry of External Affairs
MIHD	Middle Income and Medium to High Debt
MILD	Middle Income and Low Debt
MOC	memorandum of cooperation
MOF	Ministry of Finance
MOFA	Ministry of Foreign Affairs
MOFCOM	Ministry of Commerce
MOU	Memorandum of Understanding
MSMEs	micro, small and medium-sized enterprises
MW	megawatt
NABARD	National Bank for Agriculture and Rural Development
NAFINSA	Nacional Financiera
NDB	New Development Bank
NDRC	National Development and Reform Commission
NEA	National Energy Administration
NEIA	National Export Insurance Account
NEPAD	New Partnership for Africa's Development
NGO	non-governmental organisation
NHB	National Housing Bank
NIB	Nordic Investment Bank
NPL	non-performing loan
NRF	National Research Fund
NSSD	National Strategy for Sustainable Development and Action
ODA	Official Development Assistance
OECD	Organisation for Economic Cooperation and Development
PACB	Pan-African Capacity Building Programme
PAG	Accelerated Growth Programme
PBC	People's Bank of China
PDVSA	Petroleum of Venezuela
PNP	Progressive Nationalisation Plan
PPP	public–private partnerships
PRC	People's Republic of China
PSI	Sustainable Investment Programme
PTVI	PT Vale Indonesia Tbk
PV	photovoltaic
PwC	PricewaterhouseCoopers
RAISG	Amazon Network for Socio-environmental Information
RBM	results-based management
RDIF	Russian Direct Investment Fund
REMT	Renewable Energy Market Transformation Project
REVE	Wind, Energy and Electric Vehicle Review

ROA	return on assets
ROE	return on equity
SAIIA	South African Institute of International Affairs
SAARC	South Asian Association for Regional Cooperation
SAD	Deforestation Alert System
SADC	Southern African Development Community
SADPA	South African Development Partnership Agency
SAMDI	South African Management Development Institute
SELIC	Special Clearance and Escrow System
SIDBI	Small Industries Development Bank of India
SIP	strategic integrated project
SMEs	small and medium-sized enterprises
SPV	special purpose vehicle
TEAM	Techno-Economic Approach for Africa-India Movement
TFR	Trade and Forfaiting Review
TJLP	long-term interest rate (Central Bank of Brazil)
TMSA	TradeMark Southern Africa
TNC	The Nature Conservancy
UN	United Nations
UNDP	United Nations Development Programme
UNEP	United Nations Environment Programme
US	United States
VEB	Vnesheconombank (Bank for Development and Foreign Economic Affairs, Russia)
VSE	Vale Soluções em Energia
WB	World Bank
WRI	World Resources Institute
WWF	World Wildlife Fund
ZAE	Agroecological Zoning

Introduction: The BRICS New Development Bank

Background

The BRIC acronym was created at the beginning of the 2000s to represent a group of four fast-growing economies – Brazil, Russia, India and China – and was changed to BRICS in December 2010 with the inclusion of South Africa. At its fifth annual summit in Durban at the end of March 2013, the group announced the future establishment of a New Development Bank (NDB) to meet infrastructure investment needs in the developing world. At their sixth annual summit in Fortaleza the following year (July 2014), the BRICS finally agreed on the broader arrangements for the bank – an initial US$50bn fund – and coupled this achievement with the launch of the Contingency Reserve Arrangement (CRA) – US$100bn to be accessed to alleviate members' financial difficulties (US$41bn from China, US$5bn from South Africa and US$18bn from each of the others). The Bank will start lending in 2016.

Despite this achievement, commentators estimate that even if the NDB eventually increases its capital to US$100bn with injections from non-BRICS states and institutions (up to a maximum capital share from non-BRICS countries of 45 per cent), most infrastructure needs in the developing world will remain unmet. Compared to the World Bank and Asian Development Bank – whose subscribed capital is US$223bn and US$162bn respectively – the additional capital available from the NDB is too small to fill the financing gap (Spratt 2014). According to World Bank estimates, South Asia alone requires US$2.5tn over the next ten years, while overall the BRICS states are estimated to need a total of more than US$4.5tn over the next five years for infrastructure development. In consideration of the limited amount of lending that the NDB may provide, the bank may create 'special funds' – i.e. separately funded and managed mechanisms – designed to get round this capital constraint (Spratt 2014).

Although the BRICS countries could choose to finance projects bilaterally, a number of interests have pushed them towards the establishment of the New Development Bank. First is the need to pool risk and limit reputational costs and second is to increase the legitimacy of their operations under the umbrella of South–South cooperation (e.g. China may widen its investments in African land deals or Bolivian bauxite mines under this arrangement).

Along with this progress, some side agreements and arrangements have been made. These include a currency swap agreement between China and Brazil; a China Development Bank loan to South Africa for the development of the Transnet project (a 28,400km high-capacity telecommunications cable connecting the BRICS countries); China–India enhanced cooperation on military and security matters; and the Asian Infrastructure Investment Bank set up by China and involving India and the BRICS Business Council (a forum composed of private and public business leaders from the BRICS countries).

More importantly, since October 2013 China has put forward a plan to establish the Asian Infrastructure Investment Bank (AIIB) which will specialise in financing infrastructure on commercial terms (Yu Du 2014). This will alleviate the huge demand for infrastructure financing in the Asian region. Unlike the NDB's registered capital, the AIIB's will come mostly from China. This will counterbalance US and Japan dominance within the Asian Development Bank and ultimately increase Chinese influence in Asia (Yu Du 2014).

Current arrangements of the New Development Bank

The setting up of the New Development Bank was first suggested by India in early 2012 in order to fund its domestic energy and infrastructure needs, namely power transmission,

roads and ports. Finally, the objectives of the bank were agreed as (i) providing emergency funding at the time of global economic turbulence and (ii) ending or marginalising Western dominance. After initial enthusiasm about the creation of the bank, a number of issues revealed the differences between and different interests of countries in the group. Some of the main points of discussion were:

1. **Capital stock:** China proposed that shares in the bank's capital stock should be proportionate to GDP, but this encountered opposition from other members. The final solution was to divide the US$50bn founding capital equally among the group's members and to give equal voting rights to all.
2. **Headquarters:** The bank's headquarters will be in Shanghai, after initial opposition from India which wanted them to be in New Delhi.
3. **First presidency:** India and Brazil competed for presidency of the first term, which will rotate every five years. Presidency of the first term was ultimately won by India, to be followed by Brazil, then Russia, and finally China in 20 years.

What has so far made negotiations over certain points difficult is the fact that there are strong differences between the BRICS as well as unresolved historical issues, such as the contentious borders between China and India. About the former, analysts have pointed out the BRICS' dramatic economic differences in terms of:

- **Size of economy:** China's economy, for example, is about 28 times that of South Africa.
- **Trade:** Russia, Brazil and South Africa trade predominantly in commodities, while China trades in manufactured products and India in services.
- **Account balance:** Brazil, India and South Africa record a deficit, while China and Russia record a surplus.
- **Political regime:** ranging from Brazil, India and South Africa, which are fully participatory democracies, to Russia, an authoritarian democracy, and finally to China, a single-party socialist state.

The way the New Development Bank will operate largely depends on how the BRICS countries manage to reconcile their views on development cooperation and on the role financial institutions must play in that context. That is why there is increasing interest in understanding BRICS countries' experiences with their own national development banks in order to derive commonalities and differences in the mandates, strategies, operational models, investment strategies and funding sources, etc., of each bank.

BRICS' views on development cooperation and their national development banks

In the aftermath of the cold war, development assistance was a prerogative of Western countries, which promoted their foreign policy objectives and greatly increased their political and economic influence in the recipient countries. Until the mid-2000s, Western countries, grouped under the Development Assistance Committee (DAC) of the Organisation for Economic Cooperation and Development (OECD), represented about 95 per cent of total funds allocated internationally for development projects.

The rules and concepts set out in the OECD-DAC framework, mostly taking the form of Official Development Assistance (ODA), are recognised as different from the *modus operandi* of the BRICS. These latter countries have worked together to gain voice and to influence development policies in international development fora such as the G20.

Since the 2008 financial crisis, the BRICS have gained greater relevance in world geopolitics and are less keen on being subject to a Westernised framework of development and

development assistance. At the 2011 Busan high-level forum on aid effectiveness in South Korea, the BRICS affirmed their critical role in forging a 'new global partnership' for development cooperation on an equal footing, emphasising the need to foster commercial ties rather than depending on an aid model. With the Durban Summit in 2013, and a year later in Fortaleza, the BRICS responded to international demand for sustainable development but with no clear consensus on what this concept actually means and how the New Development Bank will promote sustainable development in the developing world.

Despite this lack of consensus, the BRICS' views on development assistance have conveyed a few common features:

1. BRICS tend to focus mostly on the region in their immediate vicinity.
2. They have a principle of 'non-interference' in the recipient country's affairs and so no conditionality – political, social or environmental – is attached to lending.
3. Development assistance provided is often strongly connected to access to strategic resources or tied to commercial agreements for domestic companies from the donor country.
4. The BRICS engage in South–South cooperation to promote cooperation on an equal footing, which can take the form of exchange of practitioners and providing training, as well as provision of funds at non-concessional rates.
5. Development cooperation encompasses trade, aid and investments.

At the same time, the BRICS' views on development cooperation, as well as the role played by the national development banks in each of those countries, differ substantially. Before moving to a brief overview of each individual country's development cooperation, Table 0.1 shows some features of the prevailing form of development cooperation of four BRICS countries, as found in the literature.

Table 0.1 Basic principles of development cooperation in the BRICS countries

	Objectives	Principles	Instruments	Sector	Ministry responsible
China	Political influence in Asia Economic interest in Africa	Win-win cooperation Non-interference	Tied aid	Infrastructure development More recently capacity building and social development	Commerce
India	Geopolitical influence Asia focus, political stability Economic interest in Africa	Fair relationship	Tied aid Technical assistance	Access to markets and energy Health and education (secondary) In Africa training and purchase of own products Competing with China on natural resources	Foreign Affairs
Brazil	Latin America Portuguese Africa Political and economic interests	Horizontal cooperation	Technical assistance	Varied	Foreign Affairs
South Africa	Africa, mainly SADC Political interest	African renaissance		Defence, security and education	Foreign Affairs

Source: Cirera (2013).

Brazil

Following its domestic socioeconomic achievements, Brazil has increasingly engaged in development cooperation with less developed countries, thus diminishing its position of aid recipient and taking up the role of donor. The terms ‘aid’ and ‘donor’, however, do not truly describe what Brazil pursues in international development cooperation. Brazilian support to other countries is based on Brazil’s successful domestic experiences, which are then ‘exported’ and tailored to the needs of the partner country via technical cooperation. The most appropriate term for such engagement is therefore South–South cooperation.

This enhanced engagement in South–South cooperation, introduced by the administration of President Luiz Inácio Lula da Silva (2003–10), has been interpreted by analysts as related to Brazil’s aspiration to improve its own international positioning in the global economy and to preserve its regional leadership in Latin America. Most of Brazil’s development assistance goes in fact to neighbouring countries, such as Paraguay and Bolivia, and to the broader Andean region (Verdun 2013). Brazilian development aid has also supported the Caribbean region following the 2010 earthquake in Haiti with programmes in education, health and social development. In Africa, Brazil has maintained a leading role in the Portuguese-speaking countries, mostly by providing support via technical assistance and cooperation programmes.

The main agency in charge of development cooperation in Brazil is the Brazilian Cooperation Agency (ABC), which administers received and granted ODA. However, as Brazil’s cooperation programme goes beyond aid, the private sector component is also significant. In fact, the Brazilian Development Bank (BNDES), which makes little use of ODA, plays an important role by providing tied loans for overseas projects in which Brazilian companies hold stakes. Not surprisingly, there is some alignment between public and private sector interests as the country and the sector focus of Brazil’s development assistance and private companies is the same.

As a key instrument in the implementation of the Brazilian government’s foreign policy, the BNDES is subject to supervision by the Ministry of Development, Industry and Foreign Trade. Since it was founded in 1952, the bank has been the driving force behind development of the Brazilian economy. It has also been the only source of medium- to long-term bank credit for private industry, shifting the focus of its operations according to shifts in government priorities. While in the 1990s its operations focused almost exclusively on the privatisation of domestic companies, in the 2000s the BNDES extended its operations overseas in line with the government’s ‘go global’ policy to increase the internationalisation of domestic ‘champion’ companies.

As will be seen in more detail in the Brazil case study in this report, most BNDES disbursements have been received by large companies, while over one-third of funds went to the infrastructure sector (mainly electricity and transport connected to the agro-food industry). BNDES action is restricted by the statutory clause that it only finances projects where Brazilian companies are involved and which increase the export of Brazilian goods. Although the BNDES has been praised for its international outreach under Lula da Silva’s administration, things have changed under President Dilma Rousseff, and mention of the BNDES in foreign policy speeches has disappeared. Time will tell whether the change in political administration will have drawbacks in terms of the role of the BNDES.

Russia

Russia inherited a long history of engagement in development cooperation from the Soviet Union, dating back to the time when ideological motives made the USSR the world's largest donor and creditor. In 1986, the USSR is quoted as having provided about US$26bn of aid (Brezhneva and Ukhova 2013). In the 1990s, with the fall of the Soviet Union, Russia shifted from donor status to that of net aid recipient.

The re-emergence of Russia as an active leader of development cooperation occurred in 2004 when it once again allocated funds from the federal budget for development aid. This one-off government decision was followed a year later by Russia's signing of the Paris Declaration on Aid Effectiveness. This event aligned the country to the OECD-DAC's standard of development assistance, which has created a distance between Russia's views on development cooperation and those of the other BRICS countries.

In 2007, Russia also issued its Concept of Russia's participation in international development assistance. Prepared by the Ministries of Foreign Affairs and Finance, the Concept was signed by President Vladimir Putin on 25 June 2007. At the same time, the creation of an agency for international development assistance was announced. Until this institution is formalised, expenditures, priorities and implementation remain subject to decisions taken by individual ministries or through their coordinated action.

In the Concept of Russia's participation in international development assistance, Russia's priorities for the delivery of development aid are: (i) to build ties with neighbouring countries, (ii) to stabilise the region, and (iii) to promote the integration of Russian capital, goods and labour into recipient countries. The Concept clearly states the importance to Russia of promoting its own political and economic interests through its development cooperation initiatives (Government of the Russian Federation 2007).

A more recent document, Russia's 2013 Foreign Policy Concept (Government of the Russian Federation 2013), sets out the country's programmatic directions and views on foreign affairs. Importantly, the documents mention the power shift from West to East and the consequent opportunities that friendlier cooperation with China and India opens up, both within the BRICS framework and more widely. Finally, as Russia aims to be a link between Europe and the Asia-Pacific region, the Foreign Policy Concept makes working for the establishment of the Eurasian Economic Union a priority.

Russia's development strategy follows some of the OECD principles on development cooperation (e.g. the 0.7 per cent target and the Paris Declaration). For this reason, out of the BRICS countries it is the most in line with the OECD-DAC Committee (European Parliament 2012). A considerable amount of financial aid provided by Russia goes through multilateral organisations such as the World Bank, the United Nations and the Eurasian Economic Community. Russia was also part of the G8 group until 24 May 2014 when the group's Hague Declaration suspended any form of collaboration with Russia in response to the country's annexation of Crimea and its heavy involvement in the Ukraine crisis. Furthermore, the US and EU have imposed an array of sanctions on Russian individuals and businesses. In particular, on 16 June 2014 the US imposed sanctions on the Russian Development Bank (VEB), restricting the bank's ability to access US capital markets.

These recent events have led Russia to deepen its engagement within the BRICS and with the G20 group, as well as bilaterally with countries beyond Western influence (Volchkova and Ryabtseva 2013). An example is the 30-year gas deal worth US$400bn which it signed with China at the end of May 2014 in response to worsening relations with the EU over the Ukraine crisis (Luhn and Macalister 2014). The Ukraine crisis also prompted renewed impetus for the creation of the New Development Bank in Fortaleza in July 2014.

Russian development institutions were created in the 1990s to provide financial support to projects of national strategic interest. The creation of these policy banks occurred mostly by direct order of the government, which provided the capital for their establishment. These are:

- The Bank for Development and Foreign Economic Affairs (Vnesheconombank)
- The Investment Fund of the Russian Federation
- The Russian Venture Company
- The Agency for Housing Mortgage Lending
- The Russian Agricultural Bank
- The Russian State Agricultural Leasing Company (Rosagroleasing).

These banks specialise in different spheres, ranging from the promotion of innovations to export support, venture business development, promotion of housing mortgage lending, small business support, financing of agriculture, etc. By early 2010, the aggregated capital of these banks amounted to RUB 1.2tn (US$26.5bn (about three per cent of Russia's GDP in 2009) (Maidan 2012).

In this complex financial context, the Vnesheconombank (VEB) provides investment and support for domestic and external projects aimed at boosting the competitiveness of the Russian economy. In particular, as this bank is responsible for external operations (insurance of export credits, export guarantees and credits) as well as operations that support small business development in the whole CIS area, this bank is one of the case studies in this report.

India

India is not an emerging donor, rather an emerging leader in South-South cooperation. The country is in fact heavily reliant on ODA from OECD countries, while at the same time acting as a donor in terms of experience and best practice which it shares with other developing countries through technical assistance initiatives.

Since the early 1950s, India has provided support to its neighbouring Asian countries and later has moved towards African countries. The oldest of its technical assistance programmes, the International Travel and Education Company (ITEC), was founded in 1964 and entailed the delivery of training by Indian experts in various fields such as information technology, education and enterprise development.

India's development cooperation is guided by five longstanding principles which were first set out in the Panchsheel Agreement signed by India and China in 1954. These principles are: (i) mutual respect for each other's territorial integrity and sovereignty, (ii) mutual non-aggression, (iii) mutual non-interference, (iv) equality and mutual benefit, and (v) peaceful co-existence (OECD 2012).

Similar to other BRICS countries, India's perspective on development cooperation is therefore based on the values of mutual respect and non-interference in other countries' internal affairs, thus it does not attach any conditionality to its assistance.

The determinants of India's engagement in early forms of South–South cooperation were, and still are, strictly connected to the country's need to foster trade and investments that favour its domestic products and companies. Trade and investments are conceived by India as integral to its development cooperation approach, which aims to engender self-development through economic and technical cooperation.

Among other drivers related specifically to India's foreign policy in Africa, the literature quotes India's quest for strategic autonomy, its desire to play a role in shaping the global system, its need for energy and natural resources, and its diaspora policy (Sahni 2007 in Chidaushe 2010).

Much of Indian financial assistance takes the form of concessional lending via lines of credit (LOCs) tied in some part to the use of Indian exports and often combined with technical assistance and training. The main field targeted by the LOCs is infrastructure development (electricity, energy, irrigation and transport). In June 2012, the India Exim Bank reported over 157 active LOCs worth US$8.2bn. If neighbouring countries in Asia were once the geographic focus of India, Africa has recently become the primary focus.

In terms of its institutional framework, Indian development cooperation is structured around three main institutions: the Ministry of External Affairs (MEA), the Ministry of Finance, and the Export-Import Bank of India (India Exim Bank). Within the MEA, the Development Partnership Administration is a recently created division coordinating the activities of Indian development aid. The main financial institution dealing with India's development cooperation and overseas lending is India Exim, which is one of the country's numerous specialised policy banks, directly supervised by the Ministry of Finance's Department of Economic Affairs. Although India has a highly fragmented banking system, as will be discussed in the India case study in this report, the Exim Bank plays a prominent role in South–South Cooperation and the promotion of trade and investments in the developing world.

China

China is the world's second largest economy in terms of GDP, although its strategic influence in global geopolitics goes much beyond its economic achievements. Indeed, China has a longstanding history of engagement in international development that goes back to the 1960s. At that time, China managed to gain strong influence in Africa, achieving its own objectives in exchange for economic cooperation. A remarkable example of the country's strategic behaviour is the admission of the People's Republic of China to the UN Security Council in October 1971, thanks to votes from African countries at the UN General Assembly. Similarly, China has demonstrated preference for extending loans to countries adhering to the 'One-China' policy (Dreher and Fuchs 2011).

More recently, after successful implementation of the 1978 market reforms and China's economic boom, motives shaping the country's foreign policy have changed. The need for natural resources as well as market access for its manufactured products has increased China's outward-oriented trade and investment policy and the geographic focus of its external operations has shifted accordingly. While previously China secured its influence in the Asia-Pacific region, since the 2000s the bulk of its funds have focused on resource-rich African countries. The same rationale seems to have guided China's recent lending to Latin American countries, such as its oil-backed deals with Venezuela.

China has recently placed stronger emphasis on regional cooperation mechanisms. In particular, the latest released White Paper on Foreign Aid dedicates considerable attention to the Forum on China-Africa Cooperation (FOCAC) and the China-ASEAN summit. These are the two main regional cooperation mechanisms through which the country develops relations with African and Asian countries (State Council of the PRC 2014). It is argued that the reason behind this renewed interest in regional cooperation stems from the need to tackle issues which are global in nature, thus requiring more efficient concerted actions (UNDP China 2014). China's enhanced participation in assistance programmes initiated by multilateral organisations, amounting to 1.76bn yuan (US$287.8m) for 2010–12 (State Council of the PRC 2014) probably fall under the same reasoning.

There is often a blurred line between China's foreign aid and other outward financial flows. Development assistance may indeed be characterised by the simultaneous presence of commercial requirements and investment clauses attached to the extension of grants and loans. For this reason, quantifying China's aid is difficult, as is the division of labour across the several institutions involved in delivering China's foreign assistance.

At the top of the system is the Chinese Communist Party (CCP) Leading Grouping for Foreign Affairs, chaired by the CCP General Secretary and State President Xi Jinping. This core structure defines the general policy directions for all government organisations involved in development assistance. Beneath this body is the State Council, a high-level unit responsible for implementing the CCP's directives and allocating funds at the beginning of every budgetary year.

Under these political bodies, four ministries are involved in the implementation of development assistance operations: the Ministry of Finance, the Ministry of Commerce (MOFCOM), the Ministry of Foreign Affairs (MOFA) and the Ministry of Social Welfare. This latter ministry is responsible only in those operations relating to humanitarian aid – i.e. in the event of a famine or other natural disaster.

More complex is the division of tasks between the remaining three ministries. The Ministry of Finance is responsible for drawing up the foreign aid budget in consultation with MOFCOM. Under this category, all operations similar to ODA – concessionary loans, debt relief and grants – are financed, as well as trade concessions. This ministry is also responsible for the multilateral aid delivered through international financial institutions.

The main body governing China's development aid is MOFCOM. This agency is divided into two branches: the Department of International Cooperation, managing incoming aid, and the Department of Aid to Foreign Countries (DAFC), which supervises outgoing aid. As a measure of the increasing relevance of Africa in China's development assistance, between 20 and 30 DAFC staff are working solely on Africa (Davies *et al.* 2008). The DAFC coordinates China's foreign policy with the MOFA. The MOFCOM also manages concessional loans, working with the China Export-Import Bank (China Exim), which is in charge of evaluating requests.

Last but not least, the Ministry of Foreign Affairs (MOFA) is in charge of institutionalising China's foreign policy, negotiating and defining China's policy towards all regions of the world. With regards to China's Africa policy, MOFA operates in international fora such as the Forum on China-Africa Cooperation (FOCAC), where it has recently started to successfully coordinate with MOFCOM in order to formulate a more coherent foreign policy towards Africa. In terms of aid, MOFA plays an advisory role to MOFCOM. China's engagement in Africa has also benefited from the establishment of the China-Africa Development Fund (CADF), an independent commercial fund created with a capital inception of US$5bn by the China Development Bank in 2006 (see the China case study later in this report for further details).

China's foreign policy is implemented through two main national development institutions: the China Development Bank (CDB) and China Exim. Both institutions play a major role in fostering China's development priorities overseas. While the CDB has mainly been active in the agriculture and infrastructure sectors, particularly in Asia and Latin America, China Exim has operated in the area of export promotion, and with a stronger presence in Africa. The CDB provided US$224.5bn of international funding in 2012, while China Exim provided US$35bn. The China case study in the next section of this report explains the CDB in more detail and also discusses some of the main features of China Exim.

South Africa

South Africa's view on development cooperation has been primarily Afro-centric as the country's priority has been to maintain regional security and stability in the African continent as a whole and, more specifically, within the Southern African Development Community (SADC).

Given its leading economic role in the African continent and its favourable relations with other emerging economies, South Africa was invited to join the BRICS and is so far the only African country in the G20. Indeed, South Africa is the largest African economy. Its GDP is equivalent to a third of sub-Saharan Africa's GDP, South Africa has a well-developed infrastructure and financial market, and highly ranked institutional development. Over time, the country has also built independent economic relations with all the BRIC countries. In particular, with India and Brazil it has set up a trilateral development initiative (IBSA), a coordinating mechanism envisaged to deepen ties among its members and gain voice on global issues in the international community.

Since the 1994 elections brought an end to the apartheid regime, South Africa's perspective on development cooperation has changed. Before that date, the drivers shaping South Africa's development assistance were mainly political, reflecting the regime's efforts to gain acceptance and votes within the UN. During this period, the bulk of South Africa's foreign development assistance supported the 'homelands', territories set aside for black inhabitants within South Africa, which were not recognised by the international community. Established in 1983, the Development Bank of Southern Africa (DBSA) functioned as a major channel of South African aid to the homelands, also providing technical assistance to these territories. In addition, the DBSA has supported the development of small and medium-sized enterprises (SMEs), agriculture, mining, water, energy, transport and social infrastructure development in the whole country and reached out into the broader Southern Africa region after its mandate was reviewed in 1997.

Largely unstrategic and denoting a lack of emphasis on commercial interests, South Africa's development assistance in the post-apartheid era has been guided by three main objectives:

1. to strengthen Africa's institutions
2. to support the implementation of the New Partnership for Africa's Development (NEPAD)
3. to foster dialogue and cooperation in bilateral political and socioeconomic relations.

Although South Africa's development assistance is not formally tied, most of the projects financed still make use of South African inputs in the form of skilled labour and/or technology.

The country's development assistance has been largely carried out via peacekeeping, post-conflict reconstruction, and research for development. South Africa has also delivered humanitarian assistance in the event of natural disasters.

Since 2000, South Africa has opened up to tripartite partnerships, collaborating with a traditional donor to deliver development assistance programmes to a recipient country (usually in Africa). Its outgoing development assistance in 2006 was estimated at between US$363m and US$475m, equal to 0.18 per cent of GDP (Braude *et al.* 2008). Around three-quarters of this was channelled through multilateral organisations and regional development banks.

South Africa is also a recipient of development assistance. However, since 2010, ODA directed to South Africa has seen a gradual decline, while concessionary loans in the field of green energy and the climate change agenda have increased.

The institutional framework of development assistance in South Africa has no central agency appointed to the overall management of programmes. The institutions involved in the process belong to several government departments (with the Department of Defence and the Department of Education accounting for the bulk of expenditures for development assistance) as well as parastatals, government agencies, and other statutory bodies. Within this last category are the Development Bank of Southern Africa (DBSA), the Independent Electoral Commission (IEC), the Industrial Development Corporation (IDC), the Human Sciences Research Council (HSRC), the National Research Fund (NRF), and the South African Management Development Institute (SAMDI).

In this fragmented framework, the main vehicle for disbursement of development assistance funds since 2000 has been the African Renaissance Fund (ARF), an agency created with the broad mandate of funding 'activities of cooperation, democracy and good governance, conflict resolution, social and economic development, humanitarian and disaster relief, technical cooperation and capacity development' (Besharati 2013). The ARF is supervised by the Ministry of Foreign Affairs, which receives recommendations on the disbursement of funds by an Advisory Committee composed of the Director General of Foreign Affairs, three members nominated by the Minister of Foreign Affairs, and two members nominated by the Minister of Finance. The ARF is meant to be reformed and integrated in the South African Development Partnership Agency (SADPA), although this transformation has already been under discussion for several years. However, the SADPA is expected to be set up soon as South Africa needs to better coordinate its aid and development cooperation activities. The SADPA will have a projected annual budget of 500m rand (US$50m) and will overcome the ARF's shortcomings, notably bureaucratic and structural delays, poor coordination, and lack of strategic direction in development cooperation activities.

Due to the historical role played by the DBSA in developing the infrastructure of the country and the broader Southern Africa region, the South Africa case study in this report analyses in more detail the functioning and operations of this development bank.

1 China Country Profile: The China Development Bank

1.1 Summary key features

- The China Development Bank (CDB) is a financial institution with 'full ministerial rank' (Downs 2011: 6), as it is under the direct control of the State Council, China's highest governing body.
- As a 'hybrid' policy-commercial bank, the CDB conducts both policy and commercial operations. It played a major role as a 'policy bank' during the 2008 global financial crisis and domestically it is supporting the urbanisation of the country through the government's local government financing vehicles (LGFVs). At the same time it is engaged in various commercial operations to support Chinese state-owned companies expanding abroad in the name of the 'going global' strategy and to secure long-term access to energy and other natural resources.
- Thanks to the 'quasi-sovereign' nature of its bonds, the CDB is able to provide longer-term loans than other Chinese banks (Provaggi 2013).
- Being a policy bank that also operates as a commercial bank, the CDB does not provide concessional loans (Stuenkel 2013; Provaggi 2013; Sanderson and Forsythe 2013). Interest rates are reported to be higher than those of other domestic (commercial) banks and international banks (such as the World Bank).
- The CDB implements rigorous risk management mechanisms both for the approval of domestic loans (Downs 2011: 14) and foreign deals (risks waived by the provision of oil as collateral, e.g. in the case of Venezuela). As a way to mitigate credit risk the bank directly supervises the money transfer both in domestic asset-backed loans (e.g. Tianjin) and in overseas resource-backed loans (e.g. Venezuela), so as to be sure that loans are paid back.
- No conditionality is attached to its credit. However, domestic loans are secured with land sales that pay off the debt service; external operations are often energy-backed loans.

1.2 Background

The CDB was established at the time of the central government's 1994 financial reforms together with two other banks, the Agricultural Development Bank (ADB) and the Export-Import Bank. The three institutions were funded as 'policy banks', with the objective of providing policy-driven lending, while China's other state-owned banks – the Bank of China, Industrial and Commercial Bank of China, China Construction Bank and Agricultural Bank of China – would act as 'commercial banks' and deal with regular corporate lending (He 2010). In separating policy from commercial operations, the government intended to gain control over lending management, so as to promote more rational, market-based lending in commercial banks (Steinfeld 1998: 71).

The history of the CDB has been intimately connected with that of the person who presided over the bank for more than 15 years, Mr Chen Yuan. He took office in 1998, when the bank had serious profitability problems, with a non-performing loan (NPL) ratio of over 40 per cent (Sanderson and Forsythe 2013: xvi). Under his guidance, the bank improved its risk assessment procedures through an enhanced mechanism of independent assessment (see notes on the organisational structure below) and managed to drop the NPL ratio to below 1 per cent. The CDB has since aspired to become a sound top-ranking international bank (Downs 2011: 8), committed to both achieving commercial profitability and pursuing national interests.

One of the most striking features of the financial system in China is that the CDB and other Chinese commercial banks are on an uneven playing field. First, the CDB has a natural structural advantage over the purely commercial banks as it is financed through long-term bonds (up to 30 years) rather than via short-term deposits. Second, commercial banks are subject to the rules and restrictions of the Commercial Bank Law, which prevents banks from having an outstanding balance of loans to a single borrower exceeding 10 per cent of the bank's capital balance (Downs 2011: 62). As it is also a policy bank, the CDB can conduct both commercial and investment banking activities (Downs 2011: 19; Zhong and Ning 2003). For the same reason, the CDB has greater freedom in major overseas lending than other Chinese commercial banks as it is not subject to China's Commercial Bank Law. Finally, the CDB has a historical advantage, being the preferred lender by local governments due to its strategy of financing LGFVs (Downs 2011: 18).

Given its position as favourite, the CDB is able to provide bigger loans with longer maturities, both domestically and internationally. So far, the majority of CDB loans to Latin American countries were in fact equal to or greater than US$1bn (Gallagher *et al.* 2012).

Box 1.1 The CDB vs the China Exim Bank

Both the China Development Bank (CDB) and the China Exim Bank have played a special role in fostering China's international outreach by supporting the national 'going out' strategy and financing development and commercial projects in a number of foreign countries throughout Africa and Latin America. The two banks have created the conditions for business development overseas and have engaged in infrastructure development projects (roads, power plants, oil and gas pipelines, telecom, and water projects). They have also supported the establishment of Chinese businesses overseas in the energy, mining and industrial sectors (Wang 2007).

Although both banks are under the direct control of the State Council and supervised by the China Banking Regulatory Commission, they operate under different mechanisms and have slightly different mandates. The CDB, as we will examine in the following pages, is a bank tasked with implementing the national economic strategy and allocating resources in order to foster China's economic and social development. The China Exim Bank is instead the world's largest export credit agency, responsible for facilitating the export and import of Chinese products. In 2009, it approved over US$70bn, more than the Export-Import Bank of the United States, the Japan Bank for International Cooperation, and the Brazilian Development Bank (BNDES) Exim combined, as noted by the World Resource Institute (WRI 2013).

The China Exim Bank offers different products in support of China's trade, namely export credits, concessional loans, and loans for contracting and outbound investment. It is important to stress that the China Exim Bank is the sole provider of Chinese government concessional loans (Wang 2007). Also, it has been noted that while the CDB has more stringent lending terms – i.e. higher interest rates – the China Exim Bank provides loans at comparatively lower rates than other international providers such as the World Bank and the US Exim Bank (Gallagher *et al.* 2012).

The two banks also have different sources of funding. The CDB is financed through bonds issued in both the domestic and international markets, while the China Exim Bank receives funds from the People's Bank of China and public institutions, as well as interbank deposits (Friends of the Earth US 2014).

As of 2013, the China Exim Bank had 21 domestic business branches and three overseas representative offices, namely the Representative Office for Southern and Eastern Africa, the Paris Representative Office and the St Petersburg Representative Office. Its total assets as at 31 December 2012 were 1,559bn yuan (approx. US$ 249.3bn) and its net profit equalled 3.8bn yuan (approx. US$ 607.8m). From 2001 to 2010, it provided over US$67.2bn of loans to Africa (Sanderson and Forsythe 2013).

Despite this competition between the CDB and other banks, in some cases synergies may arise. In fact, CDB lending has had the effect of attracting further investments, thus functioning as a sort of 'guarantee' for companies wishing to get further short-term loans from other Chinese commercial banks (Provaggi 2013). Overseas, CDB lending generally seems not to overlap with that of Western banks, with the exception of Brazil and Argentina which has received loans from both Chinese and Western banks (Gallagher *et al.* 2012).

1.3 Origin and mission statement

The China Development Bank (CDB) was founded in March 1994 and is under the direct jurisdiction of the State Council. As reported on its website, the current CDB mission is:

> To provide medium- to long-term financing facilities that assist in the development of a robust economy and a healthy, prosperous community. It aligns its business focus with national economic strategy and allocates resources to break through bottlenecks in China's economic and social development.[1]

Since its foundation, the CDB's main objective has been to support national macroeconomic policies by focusing on the development of infrastructure and basic key industries, i.e. electric power, road construction, railways, petroleum and petrochemical, coal, postal and telecommunications, agriculture and related industries, and public infrastructure.

1.4 History

The first and major event affecting the nature of and role played by the CDB goes back to the central government's 1994 budget reform which forbade local governments from running deficits and selling bonds (Sanderson and Forsythe 2013: 4). This situation put local government administrations needing funds to support the development of infrastructure in urban areas under pressure. In this context, the CDB started financing local governments through Local Government Financing Vehicles (LGFVs), companies set up with the specific purpose of enabling local governments to borrow money to develop urban infrastructure. In this way, the CDB has been the driving force behind China's urban development. The Asian financial crisis further fuelled this role by giving new impulse to the demand for funding in the housing market.

In its initial years, however, CDB performance was poor. Before Chen Yuan took office, in fact, the CDB had accumulated a high non-performing loan (NPL) ratio amounting to over 40 per cent. The whole financing system in China favoured this negative outcome. The high saving propensity of the Chinese combined with the guaranteed three per cent spread between what is paid on deposits and the lending-out rate meant that the Chinese banking system ended up favouring any sort of investment, including non-profitable ones, without any risk control against insolvency. Much of this lending went to inefficient state-owned enterprises and financed state projects with no expected returns.

Between 1997 and 2001, after Chen Yuan had become head of the CDB, the NPL ratio reduced dramatically (from 42.65 per cent to less than 5 per cent in 2001) (Downs 2011: 12). This was achieved thanks to a series of strategies put in place to improve the bank's profitability: the establishment of a better credit risk assessment, the implementation of land-backed deals, and market-based mechanisms to raise funds.

In the early 2000s, when the national priority in supporting growth became the provision of sufficient energy and natural resources, the CDB took on a new role. It started to finance both domestic companies expanding into this sector overseas and foreign companies providing China with energy and natural resources. In 2003, the CDB approved a US$230m

[1] www.cdb.com.cn/english/index.asp (accessed 27 January 2014).

loan to the state-owned company Sinochem to finance its acquisition of Atlantis, a petroleum company based in several countries. Since then, several foreign energy acquisitions have been financed by the CDB.

External operations in the field of energy and natural resources also entailed the development of infrastructure to supply China with oil and mineral resources. In 2006, the CDB financed the China-Kazakhstan oil pipeline and later the Central Asia-China natural gas pipeline.

The enhanced engagement abroad made it necessary for the CDB to internationalise. Since 2006, the bank has dispatched its teams in several countries overseas and reorganised its structure to meet the new needs (see organisational structure in Section 1.6).

The process of internationalisation also required diversification of the CDB portfolio. In 2003, the bank issued the first US$ bond in China and in September 2005 it sold a US$1bn asset-backed bond in New York. In July 2007, the CDB issued its first yuan-denominated bond in the Hong Kong market (Sanderson and Forsythe 2013: 70).

When the collapse of oil prices in 2007–08 favoured Chinese foreign investments in energy and resource assets, the CDB strongly supported the investment of Chinese companies abroad (e.g. the US$30bn loan to the China National Petroleum Corporation in 2009) as well as selling off bonds abroad.

As overseas activities increased, the CDB has placed increasing emphasis on issuing yuan-denominated bonds as a strategy to limit foreign exchange costs and reliance on the US dollar (Friends of the Earth, Banktrack 2012). In 2011, yuan-denominated bonds reached 61.5bn yuan. The bond with the longest maturity was sold in July 2012 in Hong Kong with a maturity of 20 years (Sanderson and Forsythe 2013: 79).

During the 2008 financial crisis, the CDB acted as a countercyclical lender. While the central government provided just 1.18tn yuan of the 4tn fiscal stimulus, the state-owned banks provided the remainder. The CDB took the lead, with 147 LGFVs reported to have received loans and lines of credit from the CDB for an amount of 928.6bn yuan from 2009 to 2011 (Sanderson and Forsythe 2013).

1.5 Mandate and strategy

1.5.1 Domestic operations

CDB domestic operations were largely driven by the needs arising from China's rapid urbanisation. The CDB has used the LGFVs – companies set up by local governments – to finance infrastructure development through low-interest, asset-backed loans. This way of operating gave birth to what is also known as 'the land-backed local government finance model' (see Box 1.2).

1.5.2 External operations

The CDB engaged in a series of cross-border energy and natural resource deals in order to align to the national government's 'going global' strategy, thus financing the expansion of Chinese firms abroad and securing long-term access to natural resources for China (see Box 1.2).

Among operations that support the 'going global' strategy, the CDB contributed to the establishment of China's special economic zones in Nigeria, Mauritius, Egypt, Algeria, Zambia and Ethiopia, where Chinese firms could find profitable investment opportunities as well as gain contracts for building infrastructures. To foster deeper Sino-African relations, the

Forum on China-Africa Cooperation (FOCAC) was established in 2000. The FOCAC aimed to institutionalise dialogue between China and Africa in order to promote African economic development in the framework of South–South cooperation. Through FOCAC, China has upgraded its Africa policy over the years, thus becoming a key trading and investment financing partner for African countries. In 2006, during a FOCAC summit, President Hu Jintao committed further a US$2.3bn to Africa and announced the creation of the China-Africa Development Fund (CADFund) (see Box 1.5).

More recently, the pressing need for energy has pushed China and, as a consequence, the CDB, to turn attention to the renewable energy sector (see Box 1.6).

1.6 Organisational structure

The CDB has 32 branches and four representative offices across China. Each branch has responsibility for a different part of the world, e.g. Chongqing for the Balkans, Henan for South Africa and Sichuan for Nepal, among others (Downs 2011). There are two CDB representative offices in Egypt and Russia. The CDB-funded CADFund has offices all over Africa.

The CDB also has a securities venture, a private equity division – CDB Capital – a leasing arm and credit guarantee company (Sanderson and Forsythe 2013: 41). It has a special system in place for credit risk assessment that relies on four separate bureaux for the evaluation of loan applications. Final approval is given by a lending committee headed by a rotated vice-governor (Downs 2011: 14; Sanderson and Forsythe 2013: 59).

In 1999, Chen Yuan set up an independent International Advisory Council which has been meeting annually ever since. The council – composed of economists and governors of international reputation – discusses relevant global financial issues and management (Sanderson and Forsythe 2013: 62).

In 2008, the CDB was restructured as a commercial bank. Its shareholders are:

- the Ministry of Finance (MoF), which manages the fiscal revenues and expenditures, formulating fiscal and taxation policies and performing financial supervision
- Central Huijin Investment Ltd (Huijin), a wholly state-owned limited liability company, which acts as an investor in key state-owned financial institutions
- the National Council for Social Security Fund, a government agency responsible for the management and operation of the National Social Security Fund.

Table 1.1 China Development Bank shareholders

	Capital contribution	**Number of shares**	**Total (%)**
Ministry of Finance	153.9bn yuan (approx. US$25.5bn)	153,908,000,000	50.18
Central Huijin Investment Ltd	146.092bn yuan (approx. US$23.4bn)	146,092,000,000	47.63
National Council for Social Security Fund	10m (approx. US$1.6m)	6,711,409,395	2.19
Total	310bn (approx. US$49.7bn)	306,711,409,395	100

Source: China Development Bank (2014).

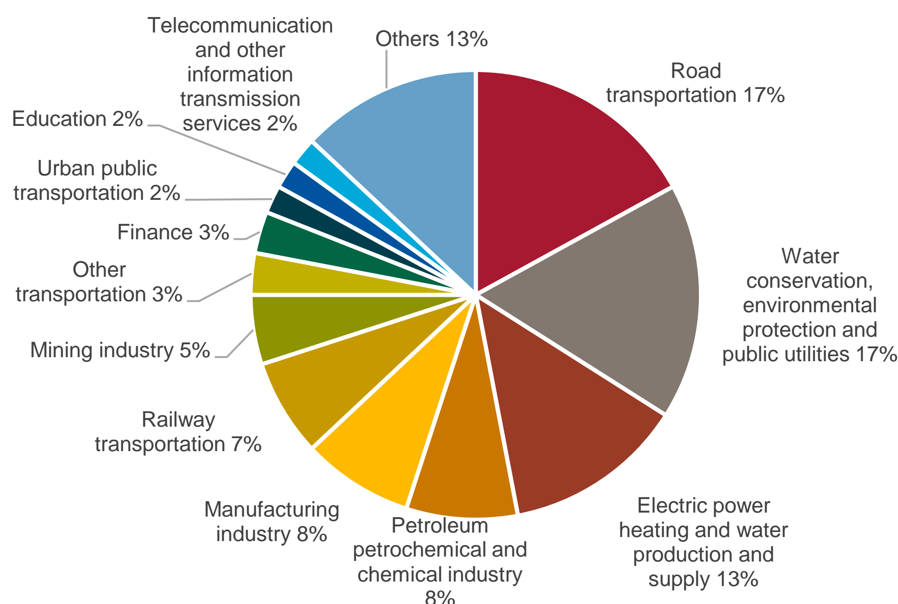
There are two Boards reporting to the bank's shareholders:

- the Board of Directors, made up of 14 directors plus two independent non-executive directors
- the Board of Supervisors, appointed directly by the State Council and composed of five members.

1.7 Sector focus

The main focus of CDB operations has been infrastructure and industrial projects (mainly relating to energy, natural resources and transport). It is estimated that until 2011, half of CDB's loans went to local government lending (Sanderson and Forsythe 2013: 32) for infrastructure development. Among the key large infrastructural projects are the Three Gorges Dam, the Shanghai Expo and the Olympic Games. Along with these major operations, the CDB has also supported the implementation of social programmes such as slum upgrades, migrant worker training and disaster relief.

Figure 1.1 Sector distribution of loans and advances to customers (as at 31 December 2012)



Source: Adapted from China Development Bank (2013).

Table 1.2 CDB loans by sector, percentage of total

	2001	2008	2012
Public infrastructure	9.6	28.8	20.6%
Roads	15.9	20.3	17.2%
Power	36.7	15.7	11.4%
Petrochemicals	4.2	4.4	7.3%
Railways	14.4	3.2	7.2%
Telecoms	3.3	2.3	1.4%
Agriculture	–	2	2.2%
Coal	–	1.2	1.3%
Other	16.1	22.1	31.5%

Source: China Development Bank (2013).

1.7.1 Domestic operations

The main focus has been on urban infrastructure: roads, bridges, railroads and communications, ports, electric power. More recently, in the framework of China's clean energy agenda, the CDB has financed Chinese renewable energy projects.

1.7.2 External operations

In the CDB's annual financial reports there is no sector breakdown of the overseas lending. However, it was reported by a CDB official in 2009 that the majority of CDB foreign currency lending abroad goes to energy and natural resource projects (Friends of the Earth, Banktrack 2012: 7).

Also, in Gallagher *et al.* (2012) it is reported that over two-thirds of the outstanding loans to Latin America went to loans-for-oil deals.

In Ethiopia, CDB financing was directed to the manufacturing industry, e.g. leather and glass (Sanderson and Forsythe 2013).

1.8 Geographic focus

Table 1.3 Total CDB operations by geographic area (in yuan millions)

	Eastern China	Central China	Western China	Overseas	Total
Deposits with banks and other financial institutions	69.34%	0.22%	0.25%	30.18%	100.00%
Derivative financial assets	35.23%	12.42%	3.65%	48.71%	100.00%
Loans and advances to customers, net	40.07%	19.39%	24.04%	16.49%	100.00%
Available-for-sale financial assets	97.89%	1.29%	0.73%	0.09%	100.00%
Debt securities classified as receivables	98.57%	–	–	1.43%	100.00%
Other financial assets	69.40%	6.18%	10.85%	13.57%	100.00%
As at 31 December 2012	46.10%	17.02%	20.85%	16.03%	100.00%
As at 31 December 2011	45.33%	18.19%	21.31%	15.17%	100.00%

Source: China Development Bank (2013).

1.8.1 Domestic operations

The CDB has focused on urban areas, predominantly in the eastern regions.

Table 1.4 Outstanding loan balance (main activity)

	Eastern China	Central China	Western China	Overseas
Loans and advances to customers, net	40.08%	19.39%	24.04%	16.49%

Source: China Development Bank (2013).

1.8.2 External operations

The CDB does not release information on the geographic focus of its lending overseas. However, the literature reports some figures that help in quantifying CDB lending to different areas of the world.

Some authors have estimated that the bank's outstanding loans to Africa equalled US$13.7bn as at July 2012 (Sanderson and Forsythe 2013: 103). Our calculation, based on Chinese development finance activities in Africa from 2004 to 2012 returned a total of slightly less than US$10bn.[2]

CDB loans to Latin American countries for the period 2005–11, however, amounted to approximately US$62bn, according to the data collected for a recent study by Gallagher *et al.* (2012). Most of those loans went to Venezuela, Brazil, Ecuador and Argentina.

Russia and Central Asia reported US$28bn in financial support by mid-2011 (Friends of the Earth, Banktrack 2012: 10).

According to ThompsonOne and Bloomberg League tables, which list 158 CDB deals between 2002 and 2011, the highest number of transactions occurred with Taiwan (28) and Australia (26), followed by Indonesia (12) and Russia (10) (Friends of the Earth, Banktrack 2012: 10).

1.9 Financial performance

Table 1.5 Selected financial indicators (as at June 2013)

Total equity	497,851m yuan (approx. US$79,853m)
Total assets	7,520.3bn yuan (+20.28% year-on-year) (approx. US$1,205bn)
Total profits (as at 31 March 2012)	64,139m yuan (approx. US$10,283m)
Net loans and advances	6,237bn yuan (approx. US$1,000bn) (82.93% of the total assets) – of which 78% (4,872bn yuan) in yuan-denominated loans and 22% (1,364bn yuan) in foreign currency-denominated loans
Net operating income	83.4bn yuan (+36.97% year-on-year) (approx. US$13.3bn)
Non-performing loan ratio	0.30%
Return on assets ratio	0.92%
Return on equity ratio	13.37%

Source: China Development Bank (2012).

1.10 Sources of finance

Low-interest bonds with long-term maturities of up to 30 years are the main source of the CDB's funding (as opposed to commercial banks that rely on deposits).

Until 1998, CDB bonds were bought by state-owned commercial banks at a fixed rate. Since 1998 they have been sold on the Chinese interbank bond market, i.e. through market auctions at a rate that varies according to the commercial interest rate and issuance volume (He 2010). Until 2011, the bond market rates were determined by lending and deposit rates.

As CDB bonds are guaranteed by the central government and the People's Bank of China (PBC), the PBC would have to provide short-term loans if the CDB had a liquidity shortage (Friends of the Earth, Banktrack 2012). CDB bonds have a zero risk weighting (i.e. they are 'quasi-sovereign' bonds), which means that banks do not have to hold any capital against them. Commercial banks can buy CDB bonds by using people's savings (deposits) and earn return at no risk (yields on CDB bonds are higher than the deposit rate but lower than the lending rate).

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[2] Data collated from http://aiddata.org/.

Since 2000, the CDB has also been able to underwrite corporate bonds and, after 2005, sell asset-backed securities (Downs 2011: 17).

The CDB exploited the market-based mechanism to raise funds. After 1998, it began selling bonds on the Chinese interbank bond market. In 2000, it obtained a licence to underwrite corporate bonds and in 2005 sold the first asset-backed bond in New York.

1.11 Instruments deployed

1.11.1 Domestic operations

The CDB used LGFVs to finance the development of infrastructure by local governments. However, LGFV projects produced very few returns as the projects barely covered their operating costs. However, returns from these LGFV projects/infrastructure investments were guaranteed by the selling or leasing of the land local governments had expropriated and which was used for the development of infrastructure projects via the LGFVs.

Box 1.2 The land-backed local government finance model via local government financing vehicles (LGFVs)

The land-backed local government finance model relies on the use of local government financing vehicles (LGFV) – companies set up by local governments – to provide local administrations with the necessary funds to complete infrastructure projects. Loans to the LGFVs are provided at low interest rates and asset-backed. The collateral most commonly used in these deals is land; the LGFVs sell or lease the land provided to them by the local government (mostly land expropriated from farmers for little compensation) in order to repay the interest on the CDB loans. Land selling/leasing represents an extra source of revenue for local governments and has been subject to rampant inflation. The CDB's financing of LGFVs has ultimately generated a self-sustaining cycle that increases the value of land with the provision of more services and infrastructures. Thus, the value of the land covers the interest on the loans.

Examples

Wuhu

Years of agreement	1998–2010
Type of instrument	Loans
Details	The CDB issued bonds and lent money to the city of Wuhu via an LGFV company which borrowed money to build local infrastructure against assets (mainly land) that the local government had transferred to it. The LGFV was able to repay the CDB from the sale of the land which meant that the local authorities did not incur any debt. As building infrastructure increased the value of the land, the LGFV was able to borrow more money. The system relied on the unfair expropriation of land from farmers, with little or no compensation.
Borrower	Wuhu Construction Investment Company
Amount	5.39bn yuan (approx. US$864m)
Sector	Urban infrastructure
Term	Ten years
Loan rate	n/a
Estimated returns on investment	Wuhu Construction Investment Company assets increased from 319m to 21.4bn yuan
Conditions	Loans and interest were repaid through land sales
Comments	CDB lending brought in more lending from other institutions

(Cont'd)

Box 1.2 (cont'd)

Tianjin

Year of agreement	2003
Type of instrument	Loans
Details	CDB loans went to Tianjin's land bank to finance the development of local infrastructure. The land bank could then sell the land to pay back the loans. The process was under the direct control of the CDB as the land revenues were stored in the land bank's CDB account, from where the loans and interest were deducted directly.
Borrower	City's land bank (later set up as an LGFV)
Amount	50bn yuan (approx. US$8bn)
Sector	Infrastructure development
Terms	24bn yuan soft loan 26bn yuan hard loan 15 years' maturity
Loan rate	On average, 8 per cent below normal loans (10 per cent from the benchmark rate for the soft loan; 10 per cent from the benchmark rate for the hard loan for the first five years)
Estimated returns on investment	Land sales income increased by 20 per cent between 2004 and 2006 and by 67 per cent between 2008 and 2009
Conditions	15 years of land usage rights sales (used as collateral and as a source from which to pay back the loans)
Comments	The biggest loan agreement in China at the time (Sanderson and Forsythe 2013: 23)

1.11.2 External operations

The CDB operates under different mechanisms to promote Chinese investments overseas:

1. Energy-backed loans: the CDB finances foreign governments and national oil and gas companies
2. Loans and lines of credit to support 'going global' Chinese state-owned enterprises
3. Equity funds: the CDB takes equity stakes in Chinese companies operating abroad.

Box 1.3 The CDB's energy-backed loans

In line with China's priority of securing energy to meet its national development needs, the CDB extends loans to countries rich in oil and natural resources. To reduce the risk of payment default, the CDB secures the agreements with energy-backed contracts and sets up a system for direct control of the loan payments through the borrower's CDB account. Loans, interest and other fees are deducted directly from the oil revenues, which are deposited by the foreign oil companies into their own CDB accounts. Other conditions may be attached to these types of deals, such as the borrower's obligation to purchase equipment from Chinese firms or to contract Chinese companies to implement infrastructure projects.

The CDB's energy-backed loans serve three objectives:

1. to secure long-term access to natural resources
2. to provide market opportunities for the Chinese firms
3. to reduce the risk of payment defaults.

Analysis of bilateral oil flows through data registered with Chinese customs indicates that not all oil purchased by China's state-owned oil companies is then shipped back to China (Sanderson and Forsythe 2013). This finding supports the hypothesis that China would sell oil to American countries rather than using the whole amount for domestic needs (see the Venezuela case).

(Cont'd)

Box 1.3 (cont'd)

Examples

Venezuela

Year of agreement	(a) 2008; (b) 2009; (c) 2010; (d) 2011; (e) 2012
Type of instrument	(a) and (b) CDB capitalises the China-Venezuela Joint Investment Fund (c) a dual-loan facility of US$20.6bn (d) two other loans (e) CDB capitalises the China-Venezuela Joint Investment Fund
Details	CDB loans went to finance the development of infrastructure and social projects in Venezuela. Chinaoil payments of PDVSA's oil go into a BANDES account at CDB that deducts directly the interest, principal and other fees from BANDES account.
Borrower	Venezuela's Bank for Economic and Social Development (BANDES)
Amount	Total US$40bn
Sector	Infrastructure development
Terms	(a) three years; (b) three years; (c) ten years
Loan rate	From 0.5 per cent to 2.5 per cent above the LIBOR
Estimated returns on investment	n/a
Conditions	Loan (a) secured by a three-year contract between Venezuela's national oil company PDVSA and the China National United Oil Corporation (Chinaoil) for the delivery of 100,000 barrels a day (b/d) of fuel oil to Chinaoil. Loan (b) secured by another three-year contract that stipulated a minimum of 107,000 b/d (at oil prices above US$60 per barrel) and a maximum of 153,000 b/d (at oil prices below US$42 per barrel). Loan (c) US$10bn plus 70bn yuan In 2012 the total was 419,000 b/d of oil.
Social and environmental concerns	The CDB presented Venezuelan President Hugo Chavez with a 600-page long-term strategic plan for boosting Venezuela's development between 2010 and 2030 (Sanderson and Forsythe 2013).
Comments	There is a gap between the volume of oil sold to Chinaoil and that actually shipped to China, suggesting that oil has probably been stored and sold in the Americas.

Russia

Year of agreement	2009 (February)
Type of instrument	Loans
Details	The CDB provided a combined loan of US$25bn to Rosneft (US$15bn) and Transneft (US$10bn)
Borrower	The Russian national oil company, Rosneft The Russian pipeline monopolist, Transneft
Amount	US$25bn
Sector	Oil
Term	20 years, with a five-year grace period where only the interest has to be paid
Loan rate	5.69 per cent per year
Estimated returns on investment	Rosneft estimated that it would repay US$25.9bn over the US$15bn loan, so the CDB would increase its gross interest income by US$10.9bn.
Conditions	Rosneft received 60 per cent of the loan and had to provide 60 per cent of the oil (180,000 b/d). Transneft received 40 per cent of the loan and had to provide 40 per cent of the oil (120,000 b/d).
Social and environmental concerns	n/a
Comments	n/a

(Cont'd)

Box 1.3 (cont'd)

Ghana

Year of agreement	2011 (December)
Type of instrument	Two loan tranches
Details	The CDB signed a deal with Ghana, providing an energy-backed loan to support the realisation of various projects including a liquid petroleum gas processing project, a port, a railway, oil transportation facilities and a road.
Borrower	Ghana National Petroleum Corporation
Amount	US$3bn
Sector	Multiple/infrastructure development with a focus on oil and gas exploitation
Term	One 15-year loan; one ten-year loan
Loan rate	295 basis points above the LIBOR for the 15-year tranche; 285 basis points above the LIBOR for the ten-year loan
Estimated returns on investment	n/a
Conditions	Chinese contractors must implement projects worth 60 per cent of the loan. An 'off-taker agreement' obliges Ghana to sell 13,000 b/d of oil to Unipec Asia for 15 years and six months.
Social and environmental concerns	n/a
Comments	CDB lending followed Ghana's discovery of oil in 2007, and its exploitation started in 2010.

Box 1.4 The CDB's support to Chinese state-owned companies 'going global'

The CDB decided to support Chinese state-owned enterprises 'going global' through so-called 'vendor financing'. This is a credit line that helps Chinese firms operating abroad to provide their foreign buyers with money from the CDB under favourable conditions. The use of this innovative mechanism has helped embryonic industries such as telecommunications to attract clients from all over the world and to get the best position in the international markets.

In order to reduce the credit risk, the loan, once approved by the CDB-appointed branch (Shenzhen for the Huawei case), has to be managed by a foreign agency bank of the countries where the Chinese firm operates. This enables the CDB to share the risk with other financial institutions that are more knowledgeable about the credit risk situation in the foreign country.

Examples

Huawei and ZTE

Year of agreement	Started in 2004
Type of instrument	Lines of credit
Details	The CDB extended credit to Huawei and ZTE, two Chinese phone makers with low international competitive advantages that wanted to expand abroad. CDB credit lines went to overseas telecom operators interested in buying equipment from Huawei and ZTE.
Borrower	Clients of Huawei and ZTE (e.g. the Brazil land line company Take Tele Norte Leste Participacoes)
Amount	US$30bn to Huawei US$15bn to ZTE
Sector	Telecommunications
Term	n/a

(Cont'd)

Box 1.4 (cont'd)

Loan rate	Two-year grace period and an interest rate of two percentage points over the LIBOR
Estimated returns on investment	7–10bn yuan (Sanderson and Forsythe 2013)
Conditions	An agreement with a foreign agency bank is required for the management of the loans.
Social and environmental concern	n/a
Comments	Thanks to the CDB's credit lines, Huawei expanded in Brazil, Mexico and several African countries.

Box 1.5 Equity funds

The CDB operates through its subsidiary, CDB Capital, which over the years has invested in more than 17 funds, including Chinese-foreign funds – the China-Africa Development Fund, the Sino-Belgian Fund and the ASEAN Fund. Its domestic private equity funds include Hony Capital, the Bohai Industrial Fund and the Mianyang Industrial Fund (China Development Bank 2011). CDB Capital's total assets under management were more than 50bn yuan in 2010.

Examples

China-Africa Development Fund (CADFund)

Year of agreement	Established on 14 March 2007
Type of instrument	Equity investment Quasi-equity investment in stocks and bonds Fund investments Investment management and consulting services
Details	The CADFund operates under market economy principles and therefore makes profits and assumes the risks of its losses. Together with other funds, the CADFund also provides management, consulting and financial advisory services for Chinese enterprises going abroad. The CADFund facilitates Chinese investment in Africa, by investing directly in Chinese companies operating or willing to do so in Africa. It provides them with low-interest bearing loans and on-site facilitation services (Executive Research Associates 2009). When an African enterprise identifies a suitable Chinese partner, the latter applies directly to the CADFund.
Country/region	Africa (48 African countries plus China)
Amount	US$1bn in 2007 US$2bn in 2012
Sector	Agriculture and manufacturing industries Infrastructure, including power generation, transportation, telecommunications and water supply Natural resources, such as oil, gas and raw materials Industrial parks for Chinese enterprises in Africa
Term	n/a
Loan rate	n/a
Estimated returns on investment	If the fund gets to raise US$5bn, it is estimated that this will originate US$50bn of investments in Africa (Sanderson and Forsythe 2013: 98) It has had no returns on investments so far. Money comes from investors.
Conditions	n/a
Comments	The CADFund has been compared to the Britain's Commonwealth Development Corporation (money comes from the state although it claims to work under market principles).

1.12 Financing terms

Little information is present in the literature on the financing terms of CDB loans.

One clear feature is that the CDB extends longer-term loans than other commercial banks (Downs 2011: 18). The longest maturity was given to Russia: in 2009 the Russian Rosneft and Transneft received respectively a US$15bn loan and a US$10bn loan, both with a 20-year maturity.

Most Chinese loans to Latin American countries have been around or greater than US$1bn, with the largest loan – US$20bn – going to Venezuela.

Some authors put forward the hypothesis that the CDB sometimes provides loans at a higher interest rate than the commercial rate (Provaggi 2013), especially the one offered by other financial institutions, namely the World Bank (WB) and the Inter-American Development Bank (IDB). For example, in 2010 the CDB offered Argentina a US$10bn loan at 600 basis points above the LIBOR, while the WB's US$30m loan had a spread of 85 basis points (Gallagher *et al.* 2012).

1.13 Conditionality

1.13.1 Domestic operations

Asset-backed loans: the repayment of the loans and their interest by the LGFVs is guaranteed by the selling/leasing of assets such as land and buildings.

1.13.2 External operations

Although no policy conditionality is attached to CDB loans, commercial requirements are present both in the form of energy-backed deals (e.g. Venezuela, Ghana, Russia, Ecuador, Brazil) and 'off-taker agreements', such as the obligation to buy Chinese goods correspondent to a certain percentage of the loan received (e.g. 60 per cent of the loan amount in the case of Ghana).

1.14 Environmental and social policies and practices

The CDB has adopted a range of policies aimed at monitoring and improving the impact of its lending. In 2004, the bank issued its *CDB Lending Assessment Handbook*, containing specific guidelines related to the assessment of loan applications, financing criteria, and environmental assessment, etc.

The CDB's environmental assessment is compliant with the 2003 Law on Environmental Impact Assessment. The bank therefore requires all loan applications to have an environmental impact assessment (EIA) report and claims that environmental compliance is an important aspect of the loan evaluation process.

CDB environmental assessment is undertaken throughout the loan cycle and is structured around two phases – pre- and post-lending – when the bank examines the borrower's environmental compliance and violations (Global Environmental Institute 2010).

Table 1.6 The CDB's environmental guidelines

Pre-lending	1.	Clients must be in compliance with all environmental laws of the People's Republic of China.
	2.	All loan applications require an environmental impact assessment (EIA). For highly-polluting and energy-intensive industries such as coal mining, oil and gas exploration and development, power generation and transmission, and hydropower, EIAs must be approved by the relevant environmental authorities. EIAs must be completed by an independent evaluator.
	3.	Environmental standards and costs can be written into loan covenants in order to commit borrowers to environmental promises.
	4.	The Bank can exercise the 'one-ballot veto' procedure which allows loans to be rejected by the credit committee solely for environmental reasons.
	5.	The Bank assigns two personnel to carry out due diligence for each loan application, one to evaluate the loan and the other to evaluate the client.
	6.	The Bank also has an appraisal department to assess environmental and social risks, and also manages environmental and social issues across business units.
Post-lending	7.	In order for loan requirements to be considered fulfilled, clients must provide proof from a relevant environmental department that the project meets environmental protection requirements.

Source: Friends of the Earth US (2014: 38).

Among the CDB's social responsibility initiatives for supporting energy conservation and emission reduction, it has adopted a series of other non-binding documents, namely:

- the Environmental Impact Assessment Framework for Lending to Small or Medium-Sized Enterprises
- the Circular on the Publication and Distribution of a Work Plan on Energy Conservation and Emission Reduction
- the government's Eleventh Five-Year Plan on Environmental Protection
- Guidelines on Environmental Protection Project Development Review
- Guidelines on Special Loans for Energy Conservation and Emission Reduction
- a Work Plan on Loans for Pollution Control and Emission Reduction.

Box 1.6 The CDB's approach to the renewable energy sector

China's growth has been characterised by a heavy dependence on the consumption of energy, largely from non-renewable resources, which has resulted in highly unsustainable rates of air and water pollution. In this context, the shift towards more sustainable energy consumption and achieving the goal of producing 20 per cent of energy from renewable resources by 2020 has been recognised as a national priority. China adopted its renewable energy law in 2006, but since 2009 the government has emphasised the need to develop 'strategically important and emerging industries', namely the energy conservation and environment protection industry, the new energy industry (nuclear, wind, solar and biomass), a new generation of information technology industry, the biotechnology industry, a high-end equipment manufacturing industry, a new materials industry, and a new-energy vehicles industry.

In agreement with the National Energy Administration (NEA), the National Development and Reform Commission (NDRC) and the Ministry of Industry and Information Technology the CDB was charged with drafting the State Council's Decision on Cultivating and Developing Strategically Important and Emerging Industries, later promulgated by the State Council on 10 October 2010. Since then, the government has encouraged financial institutions to increase credit support for the renewable energy industries and a special fund was established for this purpose.

(Cont'd)

Box 1.6 (cont'd)

In alignment with this strategy, the CDB has extended approximately US$47.3bn credit lines to Chinese solar and wind companies since 2010 (Sanderson and Forsythe 2013: 149), investing about 13 per cent of those funds in wind and 13 per cent in solar (Spratt *et al.* 2014). More precisely, it was recorded that US$9.1bn went to the LDK Solar company, US$6.5bn to Sinovel Wind, US$7.6bn to Suntech Power Holdings and US$4.6bn to Trina Solar (Sanderson and Forsythe 2013: 149).

The CDB also adapted its internal procedures to its new target sector and therefore issued Guidelines of Solar Power Development Project Evaluation, a document to be used as an integral part of its policy lending.

With regard to lending terms obtained by renewable energy projects, it has to be taken into account that this sector was recognised as one of the national priority industries. Its enterprises are therefore entitled to borrow loans with an interest rate that is 10 per cent lower than the benchmark and, since June 2012, they have had a 20 per cent concession (Spratt *et al.* 2014). Despite this general rule, it was noted that interest rates agreed by the CDB have been higher than those offered by other commercial banks, making the only advantage of borrowing from the CDB the ease of raising additional and cheaper credit from other institutions once CDB approval has been obtained. Solar companies such as Yingli have been able to borrow money from commercial banks at an average interest rate of 6 per cent (Sanderson and Forsythe 2013: 154) and get long maturity.

As revealed by previous IDS research on wind and photovoltaic (PV) projects, renewable projects typically obtain long-term lending, i.e. with maturity of between 10 to 15 years (based on a construction period of one year). Taking as an example the Huaneng New Energy Company, a wind-power enterprise, the long- to short-term ratio over the three-year period 2008–10 was respectively 66 per cent: 34 per cent; 80 per cent: 20 per cent; 78 per cent: 22 per cent. The loan ratio for such projects is typically 80 per cent. Generally, the typical capacity of a wind-power project is 49.5 megawatts (MW), which would need approximately 350m yuan in bank loans. Most of the centralised PV projects have a capacity of 10MW each, which would need about 170m yuan of bank loans (Spratt *et al.* 2014).

Another feature of CDB engagement in the renewable energy sector is that it favours companies operating in partnership with local governments. Before 2002, the CDB only lent to state-owned companies (Spratt *et al.* 2014). Results from the IDS research mentioned above reveal that PV companies applying for CDB loans partner with local governments. The study also mentions the case of Yingli, a solar company whose application for a loan in 1998 was rejected because it came from a private company. The company was eventually able to receive financial support from the CDB when the government of Baoding High-tech Zone arranged the purchase of 60 per cent of Yingli's shares via one of its subsidiary state-owned enterprises.

The substantial support offered by the CDB to solar and wind companies had the effect of increasing international competition for many US and EU solar companies, which led to some eventually filing for bankruptcy. In October 2011, a group of solar panel makers led by Solar World Industries America signed a petition against Chinese PV cell and panel makers for using illegal government subsidies to sell in the US market (Sanderson and Forsythe 2013: 155). The following year the US announced the application of anti-dumping duties of about 31 per cent to Chinese PV products entering the US market. Solar World applied to the European Commission to take similar action.

1.15 Debated issues

1.15.1 Environmental issues

According to some authors, CDB lending follows the 'non-interventionist' principle by which borrowers are freed from any policy conditionality attached to CDB's lending. Although this is not entirely true, as China requires its borrowers to purchase Chinese goods as part of its lending deals, more important aspects such as environmental and social responsibility concerns remain largely unaddressed.

In 2005, CDB incorporated some provisions of the Western-style social environmental guidelines into its own lending procedures (i.e. all loan applications require an environmental impact assessment (EIA), highly polluting and energy-intensive industries need their EIAs to be carried out and approved by independent environmental authorities, etc.). However, it was estimated that more than 170 environmental accidents occurred in 2010 (Gallagher *et al.* 2012: 26) and, despite the publication of the Green Credit Directive by the China Banking Regulatory Commission (CBRC) in 2012, the CDB has not yet implemented its provisions.

Looking at the social and environmental impact of CDB lending, the bank has engaged in a growing number of environmental protection initiatives for a total of 232bn yuan (approx. US$38.15bn). Projects financed by the CDB include urban and river environmental protection infrastructure, industrial pollution control and ecological projects.

At the same time, however, the CDB has also financed some controversial projects such as the Sino-Myanmar oil and gas pipelines, which have been estimated to generate environmental and social problems related to the practice of land confiscation and loss of livelihood for local farmers, and increased militarisation of the area, corruption, and environmental degradation (Friends of the Earth, Banktrack 2012: 25). More disruptive environmental damage has been recorded by the Asia Pulp and Paper (APP) Group which operates in Indonesia and China and is involved in logging, plantation development, pulp production and various processing activities. The environmental impact of this group has been an increase in deforestation, millions of tons of CO_2 emissions, and social unrest due to land expropriation.

In conclusion, although the CDB's environmental policy has been greatly improved, the bank has not yet adopted international standards such as the Equator Principles.

1.15.2 Social issues

The innovative LGFV system put in place by the CDB to support China's urban growth rests on exploitation of the land, the conversion of land from rural to urban use, and the expropriation of farmers' land rights. More precisely, local governments using land as collateral against borrowing from the CDB via LGFVs authorise the expropriation of farmers' land rights[3] and the conversion of rural land to urban development. There is a price premium arising from this rural-to-urban conversion of land, which represents an extra entry point for local governments. Land valued as 'rural' increases in value once planning permission has been granted and it is deemed 'urban'. Critics point out that the social impact of this practice is extremely controversial and much higher than estimated in monetary terms. First, the price paid for the expropriation is often very low compared to the value of the land (especially after it has been converted). Second, compensation is paid to the village and then by the village to the household, making the farmer's actual compensation uncertain. Third, even where farmers obtain a 'fair price' as compensation, the impact on their daily lives and the lives of their families is high. There is a high risk of families becoming more vulnerable to poverty since farming is often their only skill and they are unable to relocate to other jobs. Fourth, this practice is fuelled by and fuels one of the major problems with China's current development model. Rural-to-urban migration has created a mass of 'second-class' citizens who hold rural residence permits but actually live in the cities. These rural migrants do not have access to the same social assistance as those with urban residence permits and put the labour market, space and other resources under a great deal of pressure.

1.15.3 Adverse impact on the economy

As mentioned previously, the CDB has been a hybrid bank for a long time. On the one hand it is a policy bank entitled to sell bonds with sovereign rating (therefore able to get less

[3] In China land is owned by the state; it is not the property of the farmers. Farmers, however, are given the right to cultivate land in exchange for producing a certain amount of crops.

expensive funds by selling quasi-risk free bonds to commercial banks). On the other hand, it operates as a commercial bank and became a proper commercial bank on paper in 2008 (Sanderson and Forsythe 2013: 74). This double role has created the basis for an uneven playing field between the commercial banks and the CDB. However, if the commercial banks complain about the CDB stepping into their sphere of competence (when the CDB acts as a commercial bank while maintaining the privileges of a policy bank), they would not benefit from the complete conversion of the CDB into a commercial bank. In fact, the CDB bondholders would record enormous losses from a possible downgrading of them (Sanderson and Forsythe 2013).[4]

1.15.4 Transparency and accountability issues

Although the non-performing loan (NPL) ratio of the CDB appears to be very low, the reliability of such a figure is questionable, especially if one takes into consideration the recent problem of local government debt. On both the domestic side and internationally there is a question about how it has been possible for the CDB to maintain such a low NPL ratio while lending to countries with a high risk of default.

Another issue is the mismatch between the policies and practices of the CDB. Putting this in context, the CDB has on several occasions stated its commitment to green finance, more specifically ‘to serving as a pioneer in developing creative, green finance models... [and to]… enhance Green Credit and financially support the Tai Lake Clean-up Campaign’ (Friends of the Earth US 2014: 31). Nevertheless, the CDB has maintained its strong focus on and support to the coal industry, with data showing no sign of decreasing disbursements in favour of those sectors (*ibid.* 2014).

[4] Ba Shusong estimates losses of 71.5bn yuan if the bonds are rated AAA (Sanderson and Forsythe 2013: 84)

2 Brazil Country Profile: The Brazilian Development Bank (BNDES)

2.1 Summary key features

- The Brazilian Development Bank (BNDES) is a wholly state-owned financial institution, responsible for over 70 per cent of long-term financing in Brazil.
- Since the BNDES is funded via the Worker's Assistance Fund, it has the statutory obligation to employ those funds for projects that increase the country's employment and production levels.
- During the 2008 financial crisis, the BNDES played the role of countercyclical lender. Such operations were funded by an increased share of funding from the National Treasury.
- The BNDES has a pervasive role in all sectors of the Brazilian economy: agribusiness, information technology, aircraft, oil and gas, consumer goods, pharmaceuticals, retail, engineering services, tourism, education, sports and cultural goods.
- To address the needs of such a variety of sectors and clients (small to medium enterprises as well as large firms), the BNDES operates through mergers and acquisitions, funds for research and development, export promotion, programmes for social inclusion, urban development and, finally, environmental protection and the promotion of renewable resources.
- The largest share of the BNDES operations is represented by financial support to large companies, either in the domestic market or for their expansion abroad. This support may take different forms, ranging from lines of credit offered to participation in the capitalisation of the company.
- The largest share of the BNDES disbursements goes towards high-risk projects (especially the hydroelectric mega-projects), which may have both controversial environmental and social impacts. For this reason, the BNDES has in place a system of environmental and social appraisal and is in dialogue with civil society organisations which, however, point out the shortcomings in the BNDES' approach to environmental and social concerns related to the projects it finances.

2.2 Background

The BNDES is a 100 per cent stated-owned company, operating under private law, serving as the key instrument for the implementation of the government's industrial and infrastructure policies (BNDES 2013a). It is the main banking institution in Brazil, providing more than 70 per cent of long-term bank lending in the country (Colby 2012). The size of its credit operations equals 5 per cent of the Brazilian GDP (Mantega 2005). Compared to other international financial institutions, the BNDES is the second largest credit provider in the world, after the China Development Bank and followed by the World Bank in third position (although way behind the BNDES, whose loans value in 2010 was more than three times that provided by the World Bank) (BNDES 2012a).

The BNDES provides subsidised credit to respond to failure of the domestic financial market, where the interest rate is extremely high – this was set at 10.75 per cent in February 2014. This historically high interest rate has been quoted as an important constraint on Brazil's economic development (Segura-Ubiergo 2012; Hausmann 2008). Various arguments have been put forward to explain it, including (i) the high levels of public debt (Favero and Giavazzi 2002), (ii) the many episodes of debt default (Rogoff 2005), (iii) the relatively low level of domestic savings (Hausmann 2008; Fraga 2005; Miranda and Muinhos 2003), (iv) the lack of

full Central Bank independence (Rogoff 2005), (v) jurisdictional uncertainty (Arida *et al.* 2004), and (vi) the long history of high and volatile inflation (Segura-Ubiergo 2012). One of the arguments also pointed to the causal responsibility of the BNDES – that providing public lending at below market rates has contributed to segmentation of the credit market, leaving the Central Bank in control of only part of the credit market (Segura-Ubiergo 2012: 10).

The BNDES' more favourable lending terms have resulted in the private sector banks being crowded out from corporate credit markets (Boadle 2013). Despite this effect, the BNDES' strategy has been to cooperate with other private financial actors. This is evident if one looks at the fact that about 50 per cent of BNDES' lending is 'indirect' and therefore passes through other private banks. While this seems to be the preferred modality for small-project lending, for big projects BNDES also offers co-financing opportunities to other private financial institutions and works together with multilateral and Western donors. Indeed, the Inter-American Development Bank (DB) and the BNDES co-finance a number of projects (e.g. highways and electrical power projects), and the BNDES has been recognised as one of the most important and active partners of the DB. The amount of financing the BNDES received via the DB equalled 17 loans for a total amount of US$4.2bn (Ryan *et al.* 2012).

2.3 Origin and mission statement

The BNDES was founded on 20 June 1952 with the priority of expanding the economic infrastructure and providing long-term financing credit in order to foster the country's development.

By law (Art. 3 of Federal Law) the Banco Nacional de Desenvolvimento Econômico e Social (BNDES) is: 'the main instrument for the execution of the Federal Government's investment policy, having as its foremost purpose to support programs, projects, construction and services related to the Country's economic and social development'.

Officially its mission is 'to foster sustainable and competitive development in the Brazilian economy, generating employment, while reducing social and regional inequalities'.[5]

2.4 History

Originally established as the 'BNDE' (Banco Nacional de Desenvolvimento Econômico) in 1952, the bank included the 'S' (for Social) in the 1980s after widespread criticism – mainly from Brazilian civil society organisations – that the socio-environmental perspective was not sufficiently integrated into the bank's lending.

Since its establishment, the BNDES has been the financial instrument for the implementation of the federal government's industrial and infrastructure policies. The focus of the BNDES' operations has therefore changed along with national government priorities.

In the 1950s, the central focus was on infrastructure (both in terms of energy and transport) and the steel industry.

In the 1960s, attention was directed more towards the development of heavy industry and the provision of consumer goods. An increasing role was also played by small and medium enterprises. This phase also saw the start of support to technological development.

In the 1970s, the BNDES' actions were instrumental in the implementation of the national import substitution industrialisation, a policy strategy defined by the federal government to promote domestic development via substituting foreign imports with domestically produced goods. The long-term financing offered by the BNDES played a crucial role in realising the

[5] www.brasil.gov.br/.

import substitution policy. Similarly, the BNDES intervened in the 1980s, supporting the development of the energy sector and agribusiness.

In the 1990s, the BNDES became 'the operational arm of the Privatization Program',[6] both by planning and by executing the reforms (Lazzarini *et al.* 2012). The bank, in fact, acted on two sides: providing loans to the acquirers and at the same time becoming an 'acquirer' itself by purchasing minority stakes in several state-owned companies.

More recently, the BNDES has turned its attention to promoting Brazil's competitiveness by supporting strategic sectors of the economy and the international expansion of national champions. It is doing this by financing the development of infrastructure (both energy and logistics) and by fostering the shift of gains made from its oil discoveries into the development of the petrochemical industry. It also promotes social inclusion and engages in programmes directed at reducing extreme poverty through initiatives such as the national programme for strengthening family farming (BNDES Social Fund).

The BNDES has acted as a 'countercyclical lender' (Colby 2012), for example, during the 2008 global financial crisis when the bank was one of the main agents responsible for the maintenance and expansion of credit, contributing 36 per cent of the total increase in financing operations and the maintenance and/or creation of over three million jobs in 2009 (Di Miceli da Silveira 2010).

Between mid-2009 and mid-2011, BNDES lending to the country's producers grew by 70 per cent (Ghosh 2011), with a lending record of US$96.3bn in 2010 (Grabel 2013). Measured in terms of length of financing, the BNDES accounted for 67 per cent of bank loans with maturity over five years (Torres Filho 2011).

Much of this increase in BNDES disbursements in recent years comes from the National Treasury in the form of direct transfers through special programmes, i.e. the Accelerated Growth Programme (PAG) and the Sustainable Investment Programme (PSI). The programmes have provided specific credit lines for infrastructure projects (energy, logistics, social and urban infrastructure, and public administration). The total disbursement in 2011 amounted to R$19,827m (approx. US$8,605m), the largest share of which, over 74 per cent, went for energy projects (about 310), followed by logistic projects (94), social and urban infrastructure projects (85) and finally public administration projects (18) (Verdun 2013: 16).

In 2011, with the 7.635/2011 Presidential Decree, the BNDES obtained authorisation to gather resources abroad to finance projects beyond national borders. The only condition is that projects have to be performed by Brazilian companies or by nationally controlled foreign companies in which the BNDES can hold shares (Kraychete and Cristaldo 2013).

2.5 Mandate and strategy

2.5.1 Domestic operations

BNDES objectives have changed over time in line with priorities set by the government. It has provided long-term subsidised financing to companies, covering virtually all sectors of the economy. This strategy has meant that the BNDES is less exposed to crises in any specific sector.

On various occasions, the BNDES has acted as a countercyclical financial source – for example, during the global crisis of 2008–09 (Araujo 2013; Colby 2012) – enacting measures

[6] Interview with Sérgio Besserman Vianna (planning director of the BNDES (1996–69) and president of the Brazilian Institute of Geography and Statistics (IBGE) included in *BNDES – 50 Years of Development*, www.bndes.gov.br/SiteBNDES/bndes/bndes_en/Institucional/Publications_and_Presentations/book50years.html.

that have reduced the bank's compulsory reserves, cut the prime interest rate, and expanded low interest rate and easy credit. The main goal has been to promote the sustainable and competitive development of the Brazilian economy by generating jobs and reducing social and regional inequalities. With the foundation of the EXIM Brazil (Agência Crédito à Exportação do Brasil SA) in 2010, the BNDES acquired a new tool to strengthen Brazilian foreign sales by increasing opportunities for market access for Brazilian high added-value products and services. The BNDES credit division carries out the risk analysis of EXIM Brazil's operations.

2.5.2 External operations

In the 1990s, the BNDES began to act as a founding agent promoting the internalisation of important sectors of the Brazilian productive structure. It started by financing the export of capital goods to Latin America through FINANEX, the Machinery and Equipment Export Financing Programme. Later, in 1997, through the BNDES-Exim, BNDES offered credit lines on a broader range of financeable goods (not only capital goods as before), including intermediate products and consumption goods. Since 1999, BNDES has also managed the Exports Guarantee Fund, connected to the Ministry of Finance, which has now become the Foreign Trade Guarantor Fund (Fundo Garantidor de Comércio Exterior – FGCE), a private instrument responsible for offering guarantees to EXIM Brazil operations.

More recently, the BNDES' strategy (mainly started in 2003 under the government of Luiz Ignácio Lula da Silva) has been to support the outward foreign investment of Brazilian companies (Araujo 2013) in order to contribute to the social and economic development of Brazil by reaching new markets, learning new technologies, and promoting Brazil. The strategy has privileged the financing of big Brazilian companies in a few strategic sectors.

BNDES activities aimed at strengthening the links between foreign direct investments and the export of industrial goods and engineering services, and research and development projects. Substantial support was given to services surrounding the activities of Brazilian companies abroad, such as starting subsidiaries in other countries, creating strategic partnerships, maintaining long-term supply contracts, managing distribution channels, and other forms of foreign direct investment (FDI) (Araujo 2013).

2.6 Organisational structure

The BNDES is directed by the Board of Directors and the Administrative Council, members of which are appointed by the president of Brazil.

The so-call 'BNDES System', the operative centre of the BNDES, is composed of the following subsidiaries:

- FINAME: provides indirect financing for the purchase of machines and equipment
- BNDESPAR: the investment arm of the BNDES which operates through capital ventures, equity, and the issue of debentures
- BNDES Limited: focusing on improving the bank's visibility in the international financial community and supporting the internationalisation process of Brazilian companies
- EXIM Brazil: in charge of the internationalisation and trade support (pre- and post-shipment).

The process of credit approval involves the following bodies:

- Department of Priorities and Planning (DEPRI) which performs the pre-screening analysis of credit requests and determines if the project conforms with BNDES priorities.

- Classification and Credit Committee dealing with the financial risk assessment
- Competent Operational Division, which does the bulk of the work in the project analysis phase, working with the client to structure the project and define the contract. Operational divisions are divided into strategic sectors, such as the Foreign Trade Division (AEX), the Infrastructure Division (AIE) and the Industrial Division (AI).[7] Since 2009, the BNDES has opened subsidiaries abroad. The first office was opened in August 2009 in Montevideo, Uruguay. In November of the same year, it created BNDES Limited, an office with operational autonomy in London, capitalised with about £58m/US$95m (Biller 2013). In December 2013, the BNDES broadened the scope of its activities in Africa beyond the Portuguese-speaking countries and opened its third international office in Johannesburg.

The important bodies that support BNDES external operations are:

- EXIM Brazil – a subsidiary of the BNDES with access to its foreign trade division and operations portfolio.
- BNDES Credit Division, in charge of the risk analysis of EXIM
- Exterior Foreign Trade Guarantor Fund – Fundo Garantidor de Comércio Exterior (FGCE) – a private instrument managed by the BNDES and responsible for offering guarantees to EXIM Brazil operations.

2.7 Sector focus

Historically, the BNDES has concentrated its activities on the petroleum and basic infrastructure sector, but more recently its focus has been on mining, commodities, food processing and the creation of Brazilian multinational firms (Spink 2013). The BNDES has also been recognised as the institution that has channelled funds towards the strategic sectors of the Brazilian economy – e.g. renewable energy sectors, deep-water pre-salt oil exploration and production – so as to promote the modernisation and restructuring of the Brazilian economy (Colby 2012).

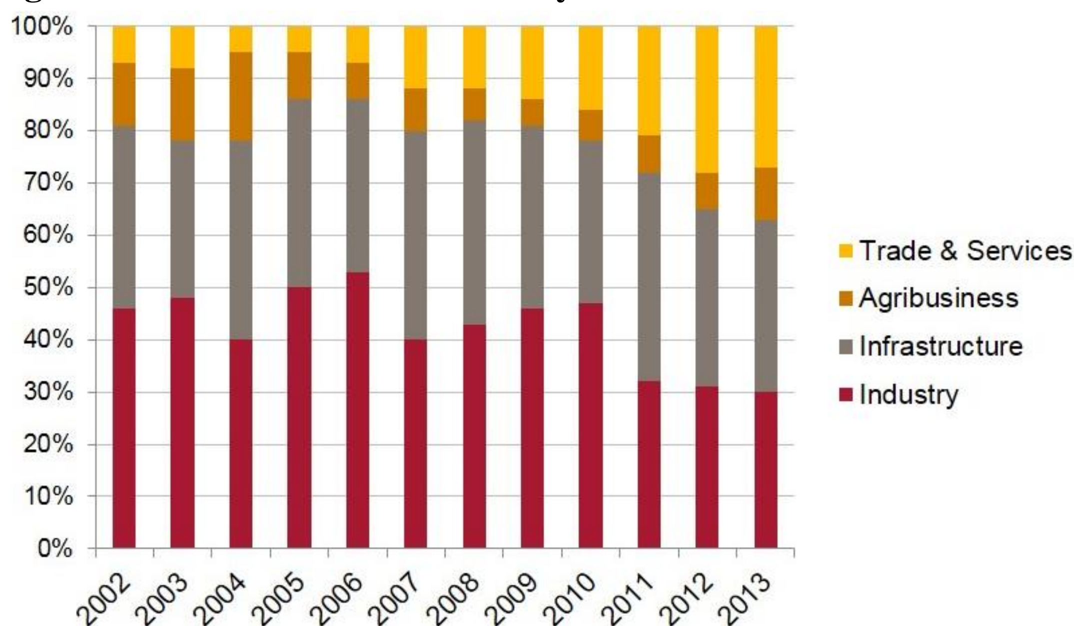
The BNDES has also extensively supported the export of goods and services of Brazilian firms to Latin America and Africa, mainly linked to the following sectors: infrastructure projects; the construction of hydroelectric power plants, aqueducts and pipelines; transportation operations; subways, highways and railways; and wind farms (Seibert 2011). More specifically, the BNDES has provided support for the export of heavy equipment for energy, rail locomotives, ships, aircraft and arms across countries in Africa, the Middle East and East Asia (TFR 2010).

The BNDES credit operations portfolio has the following sector structure (as at 31 March 2012):

1. Infrastructure (45.3%)
   a. Electricity and gas (42.6%)
   b. Transport (33.7%)
2. Industry (35.1%)
   a. Coke, oil and fuel (35.8%)
   b. Extraction (10.9%)
   c. Metallurgy (10.8%)
   d. Pulp and paper (9.7%)
3. Trade and services (19.1%)
   a. Pubic administration (57.8%)
   b. Finances and insurance (12.9%)
4. Agriculture and cattle raising (0.5%)

[7] www.bndes.gov.br/SiteBNDES/bndes/bndes_en/Institucional/Corporate_Governance/Project_Selection_Process/.

Figure 2.1 Annual disbursement by business sector from 2002 to 2013



Source: Adapted from BNDES Financial Area – Accounting Department (2013b).

Table 2.1 Sectorial distribution of the BNDES portfolio (%)

	Stakes in companies[a]	Purchase of debentures[b]
Electric energy	10.9	15.2
Mining	19.8	14.3
Telecommunications	1.7	12.6
Services	–	12
Foodstuff	4.9	10.3
Metallurgy	–	9.9
Consumer goods	–	7.2
Oil and gas	47.4	6
Pulp and paper	6.6	–
Others	8.7	12.5
Total	100	100

[a]Value of the portfolio for corporate shares in 2012: R$94.4bn (approx. US$40.3bn)
[b]Value of debentures in 2012: R$18bn (approx. US$7.68bn)
Source: BNDES (2012b).

Box 2.1 Oil and gas sector

The Brazilian oil and gas industry has extended its activities as a result of exploration and production in deep and ultra-deep waters, in the so-called ‘pre-salt’ layer. Thanks to its pre-salt reserves, Brazil could be the nation with the highest reserve increase by 2020, climbing up to 8th position in the ranking of the world's oil reserves (PWC 2013).

The BNDES’ financing role:

- BNDES Oil and Gas Structuring credit line targets the supply of goods and services in the field of oil and natural gas.

(Cont’d)

Box 2.1 (cont'd)

- BNDES Investment Support Programme (PSI) is a credit line to stimulate the production, acquisition and export of technology and capital goods.
- BNDES Finem credit line supports projects for installation, expansion and management of refineries and the development and production of oil fields.
- BNDES Proengenharia supports technical and engineering projects in the sectors of capital goods, defence, automotive, aviation, aerospace, nuclear, oil and gas, chemical and petrochemical.
- The FINAME programme finances the incorporation of parts and components supplied by BNDES-registered manufacturers into machinery and equipment
- The BNDES provides funds through the Progressive Nationalisation Plan (PNP) in order to increase the local content of manufactured products. Projects with a minimum local content of 30 per cent are eligible and this content must reach 60 per cent within three years.

The BNDES' oil and gas financing portfolio reached R$83bn in 2012, mainly centred around the energy company Petrobras and its subsidiaries (Santos 2013). The volume of loans increased from R$3.3bn in 2011 to R$7.8bn in 2012.

The BNDES created a special unit, the Department of Oil and Gas and Production Chain, to stimulate domestic development of supply chains, mainly in the pre-salt projects and in the domestic field (PwC 2013). Interviews with managers in this department support claims that activities in this field will continue to expand in future. Priscila Branquinho das Dores, Head of the Department of Oil and Gas, has estimated that in the next four years her department will finance a further R$8bn. Ms Das Dores also emphasised the progressive diversification of the bank's portfolio in the coming years, with the BNDES tending to decrease the share of refining investments (R$4.4bn in 2011) currently centred around Petrobras (PwC 2013).

Box 2.2 Renewable energy sector

In Brazil, 49.7 per cent of the energy supply comes from renewable sources (BNDES 2013c). Compared to the world average (13 per cent) and that in developed countries (6 per cent), the relevance of this sector is even clearer. The BNDES has been the largest provider of project finance to the renewable energy industry, at first domestically and, more recently, in operations abroad.[8]

In 2012, the BNDES financed US$11.9bn in the clean energy sectors, including hydro and other renewable energy projects, manufacturers, research, energy efficiency, transmissions and distribution in America (UNEP 2010b). The main focus over this period has been on bioenergy and wind projects, e.g. R$26m (US$115m) went to the sugarcane producer Usina de Acucar Santa Terezinha, R$210m (US$104m) to the Energias Renovaveis do Brasil for a biomass project, and R$378m (US$185m) to Forca Eolica do Brasil.

The BNDES cooperates both with the private sector and multilateral institutions for the implementation of clean energy projects.

In 2007, Vale Soluções em Energia (VSE) was created from a partnership between the BNDES and Vale. VSE's main objective is the development of technology programmes, focusing on environmentally sustainable processes and the use of renewable energy sources. The company also complies with Corporate Climate Change Guidelines and aims to reduce its greenhouse gas emissions. That is why, since 2008, it has undertaken a series of investments in hydroelectric facilities in order to reduce carbon dioxide emissions from its electricity consumption. VSE has managed to shift 45 per cent of its electric power supply needs to hydroelectric plants in which it has stakes, i.e. the large hydroelectric plants Igarapava, Porto Estrela, Funil, Candonga, Eliezer Batista, Amador Aguiar I, Amador Aguiar II, Machadinho, and Estreito, and small plants, namely Glória, Ituerê, Mello, and Nova Maurício (Vale 2012).

(Cont'd)

[8] A government official reported that US$5bn of subsidised credit had been pledged to renewable energy projects in developing countries by the BNDES, ranging from ethanol mills in Mozambique to wind farms in Central America (UNEP 2010b).

Box 2.2 (cont'd)

Multilateral institutions supporting BNDES operations in the field of clean energy include the European Investment Bank (EIB). IN 2011, the EIB agreed to provide a €500m loan to the BNDES for small and medium-size investments in the renewable energy and energy efficiency sectors in the framework of Brazil's Climate Change Mitigation Programme.

A final point to be noted is that the financing conditions offered by the BNDES for projects in the renewable energy sector are more favourable when compared to the average conditions applied to other sectors (Motta Veiga and Rios 2013). The interest rates granted to these projects is reported to be 1.4 per cent below those offered for coal or oil thermal plants. The financing terms vary from 16 to 20 years for renewable energy projects compared to the 14 years allowed for conventional plants. Moreover, the maximum financing participation for such projects ranges between 70 and 90 per cent, while for coal or oil thermoelectric plants it is capped at 50 per cent (IDB 2013).

Table 2.2 Disbursement – green economy and climate change (in R$bn)

	2008	**2009**	**2010**	**2011**	**2012**
Renewable energy and energy efficiency	5.7	5.7	6	7.1	6.1
Hydroelectric energy (over 30MW)	3.7	8.4	6.2	5.2	7.1
Public passenger transport	0.6	1.4	0.7	0.9	1.5
Cargo transport	1.5	2	1.4	1.6	2.6
Water and sewerage management	0.8	1.6	1.9	1.5	1.5
Solid waste management	0.2	0.2	0.5	0.5	0.4
Forests	0.2	0.3	0.6	0.6	0.7
Agricultural improvements	0.1	0.4	0.5	0.3	0.3
Adapting to climate change and risk-of-disaster management	–	–	0.1	0.6	0.6
Others	0.1	0.1	0.1	0.2	0.1
Total	12.9	19.9	18	18.5	20.8

Source: BNDES (2012b).

Table 2.3 Annual disbursements by number of projects

Sector	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**
Hydroelectric power plants	10	17	13	9	9	19	22	17	11	10
Thermal plants	3	1	1	1	–	–	3	5	7	6
Wind power plants	–	–	1	3	1	2	2	13	11	10
Small hydros	4	6	8	27	37	46	41	39	32	22
Cogeneration	3	1	–	–	–	–	2	3	5	5
Nuclear	–	–	–	–	–	–	–	–	1	1
Distribution	1	4	8	11	13	17	15	20	19	18
Transmission lines	5	8	11	6	13	7	12	17	17	24
ESCOs	–	–	–	–	2	5	2	4	4	5
Railways	1	5	5	8	5	6	6	5	8	7
Roadways	15	12	13	11	11	4	16	19	20	22
Ports and terminals	3	4	4	6	7	4	8	14	10	16
Navigation	10	9	11	9	9	11	12	6	9	8
Other	–	–	3	3	2	1	–	–	1	3
Total	55	67	78	94	109	122	141	162	155	157

Source: Pinto (2012: 23).

(Cont'd)

Box 2.2 (cont'd)

Table 2.4 Electrical power industry: approved operations 2003 to 2012

Segment	Capacity	Projects	BNDES R$m	Investment R$m
1. Generation (MW)	47,039	353	92,859	149,779
Hydro (>30MW)	32,955	47	59,720	94,435
Thermal	6,056	16	12,737	24,237
Hydro (< 30MW)	2,253	116	7,424	11,310
Biomass and cogeneration	1,959	44	3,422	4,610
Wind	3,815	130	9,557	15,188
2. Transmission (km)	26,922	86	14,858	29,845
3. Distribution		77	13,952	24,028
4. Energy efficiency		19	101	133
Total		535	121,770	203,786

Source: BNDES (2013c: 11).

Table 2.5 Financing terms for the credit lines offered for renewable energy projects

Industry	Maximum amortisation term	BNDES maximum support (%)	Financial cost	Basic spread
Generation hydroelectric projects	20 (Hydro's capacity higher than 1,000MW) 16 (Hydro's capacity from 30MW to 1,000MW)	70	100% TJLP[a]	0.9
Gas and cogeneration thermoelectric projects	14	70	100% TJLP	0.9
Coal and oil thermoelectric projects	14	50	50% TJLP 50% TJ-462[b]	1.8
Alternative sources (small hydroelectric, wind, solar)	16	80	100% TJLP	0.9
Biomass (Boiler < 60 bar)	16	80	100% TJLP	0.9
Biomass (Boiler > 60 bar)	16	90	100% TJLP	0.9
2. Transmission	14	70	100% TJLP	1.3
3. Distribution	6	50	50% TJLP 50% TJ-462	1.3
4. Railways	15	80	100% TJLP	0.9
5. Roadways	15	60	70% TJLP 30% TJ-462	1.3
6. Other investments in logistics	15	70	100% TJLP	0.9

Note: Total loan cost: financial cost + basic spread + risk spread (0.46% p.a. to 3.57% p.a.)
[a]TJLP (Taxa de Juros de Longo Prazo) – a subsidised credit rate set by the National Monetary Council
[b]TJ-462 = TJLP + 1% p.a.
Source: Pinto (2012: 29).

(Cont'd)

Box 2.2 (cont'd)

Examples

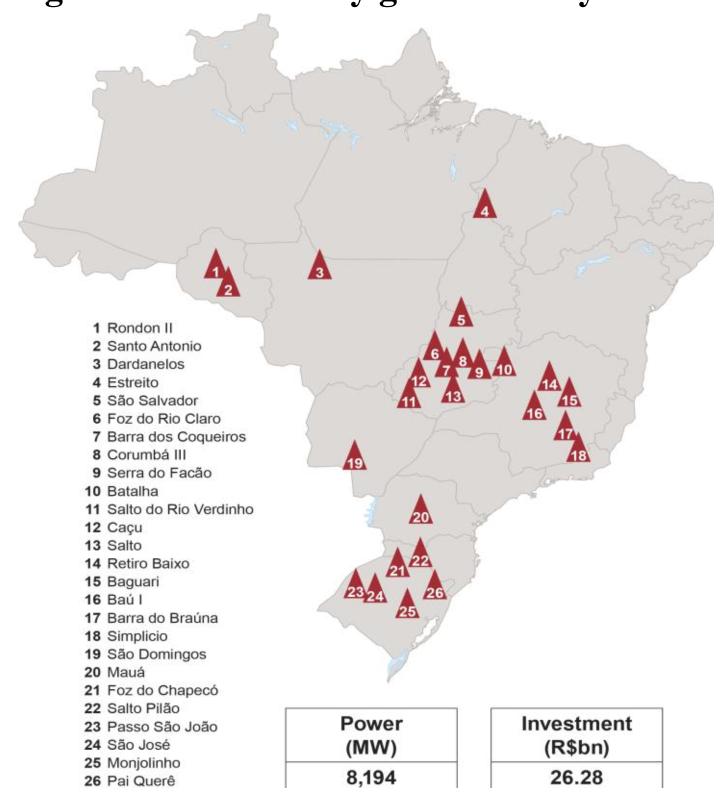
Hydroelectric

BNDES support to major hydroelectric projects since 2007

Projects	**BNDES support**	**Investment in R$m**	**MW**
Belo Monte	22,500	28,869	11,233
Jirau	9,545	15,702	3,750
Santo Antônio	8,129	17,813	3,569
Angra III	6,146	10,488	1,405
Estreito	2,661	3,607	1,087
Fóz do Chapeço	1,656	2,207	855
Simplício	1,034	1,667	334
Mauá	739	991	361
Serra do Facão	588	850	213
Caçu e Barra dos Coqueiros	543	694	155
Dardanelos	485	755	261
Salto	290	407	108
Salto do Rio Verdinho	250	342	93
Total	54,567	84,391	23,424

Source: BNDES (2013c: 13).

Figure 2.2 Electricity generation hydroelectric plants



Source: Miranda Farias (2008: 11).

Sugar cane and ethanol

Brazil launched its first ethanol programme (ProAlcool) in 1975 as a direct response to the dramatic rise in imported petroleum prices (1973) in the short term and to reduce dependence on oil in the long term. ProAlcool increased the sugar cane output of producers and at the same time managed to maintain low ethanol prices for consumers.

Box 2.2 (cont'd)

Thanks to over 30 years of strong support from the government, sugar cane-based ethanol now substitutes half of the gasoline that would be used if no other sources were available (Friends of the Earth 2008). The BNDES played its role through providing subsidised credit to the companies operating in this sector. The Brazilian government created the National Agro-Ecological Zoning of Sugar cane (Zoneamento Agroecologico da Cana de Açúcar), indicating which areas of the country are most suitable to grow sugar cane. Companies intending to build sugar cane refineries within the designated areas could access long-term subsidised loans from the BNDES (Ninô de Carvalho 2013).

In recent years, the recession and a weaker oil price drove investors to reduce their investments in new ethanol plants. This lack of investments contributed to reducing the quality and quantity of sugar cane available for milling (BNDES 2013c).

The drop in BNDES disbursement to the sugar-ethanol sector has occurred in those parts of the funds disbursed via 'direct' modality, while the 'indirect' financial transfer made via accredited financial institutions remained relatively constant between 2011 and 2012. The indirect disbursement over these two years was sustained through the BNDES Prorenova, a R$4bn (US$2bn) programme created to encourage the production of sugar cane by financing the renewal of old sugar cane fields and expanding the cultivated area. In 2012, the BNDES Prorenova portfolio reached approximately US$700m and was responsible for the renewal of approximately 315,000 hectares and the planting of 87,000 hectares with sugar cane. This programme contributed to resumption in the productivity of Brazilian sugar cane crops and to a reduction in the unused industrial capacity in sugar and ethanol production, which is expected to drop from over 20 per cent in 2010–12 to less than 5 per cent in 2013–14 (BNDES 2013c).

The cost of financing BNDES Prorenova's operations is the Long-term Interest Rate (TJLP) plus 1.3 per cent per year of the BNDES' Basic Spread for the medium-large and large companies with a gross operating income equal to or higher than R$90m. For these companies, BNDES' maximum participation is up to 80 per cent. For the micro, small and medium-sized enterprises (MSMEs), the cost of financing is instead equal to the TJLP plus 0.9 per cent per year of the BNDES' Basic Spread and the maximum participation rate is up to 90 per cent of the eligible items.

Table 2.6 BNDES disbursements to the sugar-ethanol sector (in US$bn)

	2008	2009	2010	2011	2012
Total disbursements to the sugar-ethanol sector	3.5	3.2	4.3	3.5	2.1
of which direct	1.4	1.5	1.5	1.7	0.7
of which indirect	2.1	1.7	2.9	1.8	1.5
Total disbursements to the sugar-ethanol sector as % of BNDES' total disbursements	7%	4.7%	4.5%	4%	2.7%

Source: BNDES (2013c).

Table 2.7 Distribution of BNDES disbursements per nature of activity (in US$bn)

	2008	2009	2010	2011	2012	Var. 2011–12
Agriculture	0.4	0.3	0.5	0.5	0.6	7%
Industrial	2.6	2.6	3.4	2.5	1.2	–52%
Co-generation	0.5	0.3	0.4	0.5	0.3	–34%
Total	3.5	3.2	4.3	3.5	2.1	–40%

Source: BNDES (2013c).

(Cont'd)

Box 2.2 (cont'd)

Wind

In Brazil in recent years, as in other Latin American countries (Argentina, Uruguay and Peru), there has been an increased interest in the wind sector. Brazil's interest stems from its high-quality wind resource, the oversupply in the global wind market and the downward pressures on costs in the industry.

In 2011, the BNDES alone put R$3.4bn into wind farm projects, providing 1,160MW of new wind energy capacity.[9]

Table 2.8 Evolution of wind turbine capacity power in Brazil (in MW)

Year	'97	'98	'99	'00	'01	'02	'03	'04	'05	'06	'07	'08	'09	'10	'11
MW	3	17	19	22	24	22	24	24	29	237	247	339	606	931	1,509

Source: REVE (2012).

Despite the huge potential of this sector, most of Brazil's renewable resources still come from hydroelectric sources. BNDES financing, through the machinery and equipment financing programme (FINAME), imposes a nationalisation index of 60 per cent as a condition to access funding. The reason for this rule is that the BNDES aims to foster the development of a national wind manufacturing industry. Since the BNDES is the main long-term lender, whose financing costs are much lower, the immediate result of this has been a rapid expansion of the local supply chain.

The BNDES' rules to license and verify the local content of wind turbines manufactured in Brazil are complex. There are physical targets that need to be met, showing a gradual increase in the number of domestic components in the equipment used. For instance, manufacturers of wind turbines with a 'step-up' gear box must comply to at least three of the following rules (Rothmann 2013):

- Manufacturing of towers in Brazil, with at least 70 per cent of the steel plates manufactured in the country or domestically-reinforced concrete
- Manufacturing of blades in Brazil in their own plant or that of a third party
- Assembly of the Nacelle (main part of the wind turbine) in Brazil, in their own plant
- Assembly of the hub (the part that houses the Nacelle) in Brazil, with a domestic dye-cast.

By January 2016, manufacturers are also committed to have gradually increased local components in their production process until they cover the whole chain (Rothmann 2013).

In July 2012, the BNDES disqualified six foreign wind turbine suppliers (Fuhrländer, Siemens, Vestas, Suzlon, Clipper and Acciona Windpower) which did not comply with the financing requirements of FINAME.

The expected impact of the BNDES' rules on the development of the wind industry is controversial. Some point out the impulse given to the development of the domestic sector, while others stress the fact that such strict requirements may slow down growth in this sector, drive up prices, and be challenged internationally. The local content requirements are quoted as among the main challenges affecting the energy sector, accompanied by the lack of sufficient transmission and distribution lines (GWEC 2012).

[9] See REVE (2012).

2.8 Geographic focus

The BNDES has a pervasive presence domestically. Along with its domestic focus, over the past decade the bank has also embraced operations that support the expansion of domestic firms abroad. In this last field, the BNDES has become the most important public lender in Latin America, providing credits either directly or indirectly through intermediaries. In Africa, the BNDES first focused attention on the Portuguese-speaking countries, but in more recent times has extended its support to other countries.

2.8.1 Domestic operations

Table 2.9 BNDES operations in 2012 per region

	North	Northeast	Central-West	Southeast	South
Number of operations (units)	51,486	138,451	100,104	427,210	311,189
Number of operations (%)	5.01%	13.46%	9.73%	41.54%	30.26%
Number of operations (var. % 2008–12)	6.84%	6.44%	5.00%	3.94%	3.11%
Disbursement (in R$bn)	13.3	21.0	20.1	72.4	29.9
Disbursement (%)	8.6%	13.5%	19.39%	46.4%	18.6%
Disbursement (var. % 2008–12)	1.66%	1.76%	1.03%	0.42%	0.67%

In the North Region, 58 per cent of the total disbursement went to infrastructure projects, mainly hydroelectric plants (Belo Monte, Santo Antonio, Jirau, Teles Pires and Estreito), railways (Carajàs railway) and electric energy transmission lines (BNDES 2013a: 57).

Over the last five years, the Northeast Region has catalysed a larger share of BNDES disbursement, recording a positive growth variation of 1.76 per cent between 2008 and 2012). These funds have been directed to large-scale projects: thermoelectric plants, hydroelectric plants, wind parks, refineries, shipyards, steel mills, pulp mills and an airport (BNDES 2013a: 58).

The Central-West Region is characterised by an increase in lending to micro and small enterprises, accounting for over 90 per cent of total operations in the region (BNDES 2013a: 58).

2.8.2 External operations

The BNDES' presence abroad started much earlier in Latin America than in Africa.

In Latin America

Between 2001 and 2010, the amount of BNDES disbursement made to South America, through the BNDES-Exim post-shipment line of financing, reached US$3.6bn, of which 49.2 per cent went towards Argentina and 19.8 per cent towards Venezuela (Niko 2011: 85–86),

Between 2000 and 2012, BNDES expenditures for infrastructure exports in Latin America mainly went to Argentina (50.89%), Venezuela (27.85%) and Ecuador (11.7%) (Kraychete and Cristaldo 2013).

The BNDES' interest abroad, and in Latin America in particular, is also focused on energy. The bank has backed more than 350 power projects since 2003, accounting for over 28,000MW of new electric generation capacity (Ryan *et al.* 2012).

Table 2.10 BNDES expenditures in support of Brazilian exports destined for infrastructure projects in South American countries 2000–12 (US$m)

	Argentina	Ecuador	Paraguay	Peru	Uruguay	Venezuela	Total
2000	–	89.8	–	–	7.3	–	97.1
2001	–	33.3	13.8	–	9.5	16.1	72.7
2002	–	3.3	16.3	–	–	18	37.6
2003	–	–	24.8	–	–	25.4	50.2
2004	–	112.3	17.2	–	–	44	173.5
2005	150.5	57	8	–	–	3.9	219.4
2006	–	55.8	–	–	2.6	10.4	68.8
2007	308.9	17.4	–	–	3.1	39.5	368.9
2008	260.1	0.5	–	–	2.4	6.8	269.8
2009	325.4	–	–	–	1.7	25	352.1
2010	172.5	–	–	129.9	–	315.2	617.6
2011	361.1	–	–	96.7	–	392.9	850.7
2012*	103.1	–	–	–	–	23.2	126.3
Total	1,681.60	369.3	80.2	226.6	26.6	920.4	3,304.70
%	50.89	11.17	2.43	6.86	0.80	27.85	–

Source: Kraychete and Cristaldo (2013: 79).

Table 2.11 BNDES-Exim post-shipment disbursement to Latin America countries (US$m)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Argentina	56.22	14.72	0.39	1.16	216.32	5.44	310.11	276.01	385.62	541.47
Bolivia	2.47	13.53	1.64	0.13	–	0.88	–	–	–	
Chile	2.24	2.56	26.11	23.27	30.37	66.76	31.73	120.27	11.99	102.41
Colombia	19.56	5.99	0.56	–	–	–	–	–	–	–
Ecuador	37.78	39.43	0.40	112.33	57.03	117.58	17.37	0.64	0.12	–
Paraguay	14.37	17.59	26.14	17.22	8.01	–	–	–	1.27	–
Peru	10.71	3.49	5.02	9.00	5.65	0.85	0.38	0.38	0.22	135.14
Uruguay	23.96	3.32	–	0.31	–	2.63	3.20	2.35	2.05	–
Venezuela	17.09	81.17	55.62	44.08	26.13	25.33	70.32	43.21	48.07	315.20
Total	184.4	181.8	115.9	207.5	343.5	219.5	433.1	442.9	449.3	1,094.2

Source: Niko (2011: 87).

In Africa

The BNDES' focus on Africa has increased over the last decade, thus stimulating the expansion of bilateral trade. The bank's strategy for Africa has to be interpreted as the consequence of the directions received by government through the Productive Development Policy that in 2008 issued a number of directives and practical measures for strengthening trade relations between Brazil and Africa (World Bank-IPEA 2012). Under the Integration with Africa Programme (Programa Integração com a África), Brazilian companies willing to invest in Africa could benefit from credit that amounted to R$477m (US$265m) in 2007, rising to R$649m (US$360.5m) in 2009. Stolte (2012) estimated that the BNDES provided US$766m in 2009 and US$466m in 2011.

In 2012, the BNDES granted US$3.2bn to Angola for various construction (streets, basic sanitation, housing, technological centres) and industry and agriculture projects (machinery and technical equipment) (BNDES 2012a). In early 2006, Angola had already received a US$1.5bn credit line resulting from the strategic bilateral partnership agreement aimed at increasing Brazilian influence in the new African ethanol industry.

Another two African countries, Mozambique and South Africa, received credits of respectively US$80m for construction projects (Nacala airport) and US$35m for public transport projects (BNDES 2012a).

The BNDES has granted lines of credit to be used for the financing of Brazilian enterprises in infrastructure and construction projects. A large share of BNDES credit lines going to sub-Saharan Africa (32.5 per cent) went for projects carried out by Odebrecht, one of Brazil's biggest companies and a leader in the areas of civil construction and resources (Stolte 2012). Out of the top 20 Brazilian transnational companies, six that operate in some of the strategic economic sectors (energy, mining, construction and infrastructure) have already invested in Africa (Seibert 2011). Three big companies, which possess the necessary financial resources to operate in Africa, are:

- *Odebrecht Construction* in Angola, Botswana, Democratic Republic of Congo, Djibuti, Gabon, Libya, Liberia, Mozambique and South Africa
- *Petrobras Oil* in Angola, Benin, Gabon, Libya, Namibia, Nigeria and Tanzania
- *Vale Mining* in Angola, Democratic Republic of Congo, Gabon, Guinea, Liberia, Malawi, Mozambique, South Africa and Zambia (Stolte 2012).

The BNDES has also engaged in the development of sugarcane-based ethanol processing plants in Africa. In 2010, the bank offered a credit line of US$3.5bn to Brazilian companies working in Ghana and Mozambique. For Ghana, in particular, it was possible to gain access to the Swedish biofuel market thanks to the Brazilian funding and expertise via a tripartite agreement (between Brazil, Ghana and Sweden). Under this deal, the BNDES financed the Ghanaian corporation Northern Sugar Resources with US$260m to plant 30,000 hectares of sugarcane in the northern part of the country. The sugarcane produced would then be processed by a plant built by Odebrecht and finally all the ethanol produced would be purchased by the Swedish Svensk Etanolkemi AB (Sekab) under an agreement over ten years (World Bank-IPEA 2012)

2.9 Financial performance

Table 2.12 Selected financial indicators (as at June 2013) in US$m

Total equity	24,902
Total assets	329,043
Total profits (as at 31 March 2012)	3,657
Total disbursements	39,871
Capitalisation*	7.57
Net operating income	1,472
Non-performing loan (NPL) Ratio**	0.14%
ROA ratio	0.46
ROE ratio	6.96

* Equity/total assets
**2011 value (Ferraz *et al.* 2013).
Source: BNDES (2013b).

Table 2.13 Other financial indicators (as at 31 March 2012) in R$m

	2008	2009	2010	2011	2012
Total assets	277,294	386,633	549,020	624,827	715,486
Credit and on-lending portfolio, net after allowances	215,989	283,671	361,575	425,518	492,148
Company shares*	25,293	34,012	107,476	99,601	94,391
Debenture portfolio, net after allowances	8,078	12,176	17,839	18,127	18,021
Public bonds and securities	10,600	35,917	25,638	51,329	61,525
Other assets	17,334	20,857	36,492	30,252	49,401
Total liabilities	277,294	386,633	549,020	624,827	715,486
National Treasury	43,207	144,213	253,058	310,774	376,042
FAT/PIS-PASEP**	146,088	152,540	163,091	177,947	194,655
Foreign fundraising	17,486	16,463	19,778	22,449	23,275
Other obligations***	45,246	45,789	47,194	52,645	69,345
Net equity	25,267	27,628	65,899	61,012	52,169
Net profit	5,313	6,735	9,913	9,048	8,183
Earnings from financial intermediation	4,312	5,815	9,891	7,206	11,578
Earnings from company shares	6,024	3,990	6,159	6,962	2,644
Tax expenses	(2,425)	(2,784)	(4,879)	(3,549)	(3,618)
Other revenue/(expenses)	(2,598)	(286)	(1,258)	(1,571)	(2,421)

*Includes investments in non-affiliated companies, affiliated and other investments, after impairment allowances
** FAT (workers' support fund from payroll taxes) and PIS/PASEP (a social fund that collects contributions paid by companies for the social benefit of their workers: unemployment insurance, child benefit and allowances, etc.
***Includes resources from the FGTS, FI-FGTS, Merchant Maritime Fund (FMM), the National Development Fund (FND) and other financial development funds.
Source: BNDES (2012b).

2.10 Sources of finance

Table 2.14 BNDES capital structure

Source	2011	2012
FAT/PIS-PASEP	28.5%	27.2%
National Treasury	49.7%	52.6%
Other governmental sources	3.5%	3.3%
Fundraising abroad	3.6%	3.3%
Other obligations	4.9%	6.4%
Net equity	9.8%	7.2%

Source: BNDES (2012b).

Loans made by the National Treasury have been the largest source of BNDES' capital over the last decade. The second largest source of funding is represented by the FAT/PIS-PASEP.

The FAT (Fundo de Amparo ao Trabalhador) funds come from payroll taxes and are therefore subject to a BNDES' statutory obligation that requires them to be used for projects aimed at increasing Brazilian employment and production (Armijo 2013: 14). The PIS-PASEP is a social fund that collects contributions paid by companies for the social benefits of their workers: unemployment insurance, child benefit and allowances, etc.

Because of the large share of funds provided to the BNDES by the FAT/PIS-PASEP programme, the bank has a statutory obligation to employ those funds for projects that increase employment and production of the country. The capital coming from these public sources (the National Treasury, FAT/PIS-PASEP) is provided at below-market rate – TJLP (Taxa de Juros de Longo Prazo) – a subsidised credit rate set by the National Monetary Council and then used as a benchmark to finance key sectors of the economy via the BNDES. As the market rate – the SELIC (overnight lending rate set by the central bank) and the LIBOR rate (for loans issued in US$) – is much higher than the TJLP rate, the return on investments for taxpayers is much lower when directed to the BNDES, which provides subsidised financing to its clients.

Until 2008, the FAT was the major financial contributor to the BNDES, but with the breaking of the financial crisis and the enhanced role of the BNDES as a countercyclical lender, the National Treasury has increased its financing to the BNDES enormously (Franck 2012) through special programmes, namely the PAG (Accelerated Growth Programme) and PSI (Sustainable Investment Programme), which accounted for half of BNDES funding by 2011 (Armijo 2013: 14).

In the 1970s, the bank began raising funds in the international markets. Now it counts on foreign fundraising both in terms of loans from multilateral organisations and syndicated loans and issuances of bonds. The BNDES' international partners are for instance the Inter-American Development Bank (IDB); Kreditanstalt für Wiederaufbau (KfW); Japan Bank for International Cooperation (JBIC); Nordic Investment Bank (NIB); China Development Bank (CDB), World Bank (WB), European Investment Bank (EIB).

Table 2.15 Bond issuances held by the BNDES

Issuing year	Market	Value (currency millions)	Coupon (%)	Maturity
1998	Eurodollar/144-A	US$1,000	6.37	16 Jun 2018*
2009	Eurodollar	US$1,000	6.50	10 Jun 2019
2010	Eurodollar	US$1,000	5.50	12 Jul 2020
2010	Euro MTF	EUR 750	4.13	15 Sept 2017
2011	Euro	CHF 200	2.75	15 Dec 2016

*The bond was renegotiated in June 2008.
Source: BNDES website.[10]

BNDES revenues come from the spread charged on its lending operations and from capital investments. The relative share of these two sources of revenue has changed over time. In 2003, the revenue from intermediation was R$4.4bn and from investment R$1.5bn, while in 2011 the former reached R$6bn and the latter R$7bn (Colby 2012: 18–19). The BNDES' profitmaking from its capital investment is partly explained by its ability to source capital at below-market rate and then reinvest it in government bonds while waiting to offer it again to its clients at a subsidised rate (Lazzarini *et al.* 2012; Colby 2012).

[10] www.bndes.gov.br/SiteBNDES/bndes/bndes_en/Institucional/The_BNDES_Abroad/ForeignFundraising/foreignfundraising_market.html.

As a consequence of the higher return of its credit operations, the BNDES' credit portfolio also makes up the largest share of the bank's flow of resources – which in 2012 amounted to R$160bn. The return on credit operations contributed 77.4 per cent to the total 2012 BNDES releases. The National Treasury, which provides the largest share of BNDES capital contributed just 15.6 per cent to the releases. (This is a 'net' contribution computed after deducing the payment of debt, dividends and taxes.)

2.11 Instruments deployed

BNDES support takes the following forms:

- **Financing:** financing modalities differ according to the purpose and nature of the project to be financed. Several products are available disciplined by rules for financing and operating procedures. (See Table 2.16 for a list of instruments.)
- **Non-reimbursable resources:** grants given for investments of a social, cultural (educational and research), environmental, scientific or technological nature (i.e. the Amazon Fund, BNDES Mata Atlantica and the BNDES technology fund, FUNTEC)
- **Subscription of securities:** shares, simple debentures, convertible debentures, subscription bonds, options and other derivative products, receivables-backed funds – called Fundo de Investimento em Direitos Creditórios (FIDCs) – (e.g. participation in private equity funds such as the Climate Change Fund, Caixa Ambiental, Vale Florestal Fund, ECOO11). The BNDES operates through the BNDES Participações S.A. integral subsidiary (BNDESPAR) to provide support to Brazilian publicly-listed and private companies by means of subscription of shares, convertible or permutable debentures, mutual fund shares and other securities. It is present in all growth stages of companies – e.g. seed companies, start-ups, capital venture funds, equity private funds (BNDES annual report 2011). The BNDES holds stocks in over 200 firms and about 39 funds (as at June 2012) for an amount of R$105.4bn (approx. US$45bn) (Magalhães Junior 2012).

For its external operations, the BNDES operates through the following instruments:

- **BNDES-Exim Brazil:** the newly created credit agency facilitates operations that support the export sector, e.g. the sale of heavy equipment for energy, locomotives, ships, spacecraft and aircraft.
- **Exim-pre-shipment (Pré-Embarque):** an instrument to finance the production of goods to be exported. Operations are accomplished through other financing agents (BNDES indirect operations) and cover up to 100 per cent of the production value of the goods or services that are destined for the foreign market.
- **Exim-post-shipment (Pós-Embarque):** an instrument that entails the direct involvement of the BNDES and is directed at providing buyer/supplier credit for the financing (up to 100 per cent) of the commercialisation of goods and services in foreign countries.

Table 2.16 BNDES instruments for financing and operating procedures

Type	Instrument	Description
Direct	BNDES Finem	Financing for undertakings with a minimum value of R$10m
	BNDES credit limit	Credit for clients in good standing
	Subscription of bonds/securities	The purchase of minority shares or convertible debentures of a temporary nature or investments by means of closed funds
	Project finance	Financing supported by a project's cash flow
	BNDES securities and guarantees	Provides guarantees with the aim of reducing the participation level in projects. Used in large-scale projects.
	BNDES bridge loans	Financing for a project, granted in specific cases, to speed up investments by granting resources during the structuring period of a long-term operation.
	BNDES-Exim post-shipment	Financing to commercialise Brazilian goods and services abroad
Indirect	BNDES automatic	Financing up to R$20m for micro, small, medium-sized or medium-sized-to-large companies, and up to R$10m, if the client is a large company
	BNDES Finame	Financing for the production and sale of machinery and equipment
	BNDES Finame agriculture	Financing for the production and sale of agricultural machinery and equipment
	BNDES Finame leasing	Commercial lease of machinery and equipment
	BNDES Exim pre-shipment	Financing to produce Brazilian goods and services earmarked for export
	BNDES Exim	Financing for domestic production earmarked for export and sale of goods and services abroad
	BNDES card	Pre-approved revolving credit for the purchase of products, inputs and services

Table 2.17 BNDES-Exim instruments (in US$m)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Pre-shipment	1,304	970	1,278	1,981	1,921	3,166	4,475	3,493	4,903	6,180
Post-shipment	1,779	1,633	2,670	2,025	1,940	2,697	1,863	698	1,694	2,150
Total	3,083	2,603	3,948	4,007	3,862	5,863	6,337	4,191	6,597	8,330

Source: Galetti (2010: 53).

Box 2.3 Support to national champions 'going global'

Around 60 per cent of the BNDES portfolio is invested in large companies (Franck 2012: 9). In terms of equity holdings, over 80 per cent by value is made up of shares of state-owned or semi-private large companies, such as Petrobras and Vale, also considered among the so-called 'national champions' (BNDES 2012a).

BNDESPAR, a wholly owned subsidiary of the BNDES, is strongly oriented towards investments in the oil and gas companies, among which Petrobras makes up over 33.2 per cent of the BNDESPAR portfolio. Similarly, 20 per cent of BNDESPAR's investments go to the mining sector in which Vale, the largest mining company in Brazil, operates. The electric power sector, where Electrobras and CPFL Energia are the largest operators, accounts for 16 per cent of BNDESPAR operations (Franck 2012).

(Cont'd)

Box 2.3 (cont'd)

The rationale guiding the BNDES' support to large companies is that it encourages the insertion and strengthening of companies in the international market so that they can grasp opportunities to develop their overseas markets.

The instruments the BNDES uses to support the internationalisation of companies are the subscription of bonds and securities.

Companies eligible for BNDES support for internationalisation are:

- companies with headquarters and administration in Brazil which can be domestically controlled, including any subsidiaries abroad
- foreign companies whose shareholders with more significant voting capital and more influence on activities the companies carry out are in Brazil
- companies that are directly or indirectly controlled by an individual or group of individuals domiciled and residing in Brazil
- companies controlled by a government entity in Brazil.

The type of investments eligible for support relate to the building of new branches, purchasing, expanding or modernising installed plants, and equity investments.

The maximum support guarantee is 60 per cent of the investment.[11]

Examples

Petrobras oil company

Petroleo Brasileiro SA (Petrobas) is a partially state-owned company, heavily supported by the BNDES. In 2012, over 30 per cent of the BNDES portfolio was made up of loans to Petrobras. In response to the downward economic swing, BNDES financing to Petrobras increased by 291 per cent in 2008 and 129 per cent in 2009, making the company's publicly financed debt owned by the BNDES over 77 per cent of the total (Barbosa 2013).

Between 2009 and 2013, Petrobras invested US$174.4bn, of which US$15.9bn (nine per cent) was directed to international activities. For the 2010–14, period the quota allocated to international activities reduced to five per cent (US$11.7bn) of the total US$224bn investments. In this second period, Petrobras increased its domestic engagement in pre-salt exploration and production (ADB 2011).

In Africa, Petrobras is present in 28 countries, including Nigeria, Angola, Libya, Namibia, and Tanzania, with several oil exploration projects (mainly offshore). Its oil production in Africa (57,444 barrels of oil equivalent per day) makes up about 24 per cent of its international production. Its specialisation in deep-water oil production contributes to its presence in the Gulf of Guinea, where the geology is very similar to that of the Campos Basin in Brazil.

Aside an established presence in oil-producing areas in Angola, Libya and Nigeria, Petrobras has more recently turned to investment in frontier exploration projects, such as the acquisition of a 50 per cent stake in Benin's Block 4 from Compagnie des Hydrocarbures Beninoise (New African 2012). In the aftermath of approval in 2011 of national legislation requiring ten per cent biofuel in Mozambique, Petrobras is planning to start producing ethanol in the country in 2014, supported by the BNDES. Petrobras Biocombustível is going to launch a new project on sugar cane and ethanol production, based on the establishment of an ethanol factory in Mozambique with an initial production capacity of 20m litres a year to supply Mozambican customers (New African 2012).

Petrobras also represents a model company for African countries. In Nigeria, the government is willing to turn the Nigerian National Petroleum Corporation into something similar to Petrobras, a more commercially driven upstream oil company (New African 2012).

(Cont'd)

[11] www.bndes.gov.br/SiteBNDES/bndes/bndes_en/Institucional/The_BNDES_Abroad/internationalization.html.

Box 2.3 (cont'd)

Vale metals and mining company

Vale is the world's second largest company in metals and mining. The company has invested about US$ 2.5bn in Africa, with a presence in Angola, the Democratic Republic of Congo, Gabon, Ghana, Guinea, Liberia, Mozambique, South Africa and Zambia. The focus of its operations has been mining exploration, mainly related to iron ore and copper. Its investments in Africa over the period 2010–15 are planned to reach US$15–20bn (ADB 2011).

Table 2.18 Vale investments in Africa 2009–11

Value of investment	Country	Project	Year
US$4bn	Mozambique	Moatize Coal Project: Coal production and export	2011
US$65m	South Africa	Teal: copper company (50:50 joint venture)	2009
US$145m	Zambia	Kokola North Copper Project	2010
US$5bn	Guinea/Liberia	Simandou Iron Ore Project	2010

Source: ADB (2011: 6).

Vale's main shareholders:

- Valepar, which owns 52.7 per cent of Vale's common shares, is a special-purpose company created as a result of the first stage of Vale's privatisation in 1997, when Valepar acquired Vale's controlling stake from the Brazilian government.
- BNDESPAR, a wholly owned subsidiary of the BNDES, owns 11.51 per cent of Valepar and 6.3 per cent of Vale's common shares (Vale 2013).

Direct linkages with the BNDES:

- Vale's outstanding debt is principally owed to the BNDES and Brazilian commercial banks, denominated in Brazilian reals and other currencies (Vale 2013).
- Vale and the BNDES are parties to the Mineral Risk Contract that provides authorisations for the joint development of certain unexplored mineral deposits in the Northern System mine site. In September 2012, the parties entered into a financing agreement of R$3.9bn to expand logistics infrastructure in Vale's Northern System site (Vale 2013).
- The BNDES has provided Vale with R$7.3bn (US$3.6bn) of credit facilities (Vale 2013).
- The BNDES holds a total of R$774.5m (US$379.0m) in debentures of Vale's subsidiary Salobo Metais S.A. (Vale 2013).

Indirect linkages with the BNDES:

- BNDESPAR also holds a total of R$1.685bn (US$824m) in Vale debentures, which finance the expansion of the Ferrovia Norte-Sul (FNS) railroad. BNDESPAR is in the control group of several Brazilian companies with which Vale has commercial relationships and it has a direct stake in Vale's subsidiaries Tecnored Desenvolvimento Tecnologico S.A., Vale Solucoes em Energia S.A. and Vale Florestar Fundo de Investimento em Participacoes (Vale 2013).
- Nelson Henrique Barbosa Filho, Director of Vale since April 2011, was an adviser to the presidency of the BNDES in 2005–06 (Vale 2013).
- Renato da Cruz Gomes, Director of Vale since April 2001, held various positions at the BNDES from 1976 to 2000 (Vale 2013).
- Luciano Galvão Coutinho, Director of Vale since August 2007, has been President of the BNDES since 2007 (Vale 2013).
- Luciano Siani Pires, Chief Financial Officer and Executive Officer for Investor Relations at Vale since August 2012 and Member of Vale's Executive Risk Management, Finance and Disclosure Committees, held several executive positions at the BNDES, including Executive Secretary and Chief of Staff of the Presidency, Head of Capital Markets and Head of Export Finance, from 1992 to 2008 (Vale 2013).

(Cont'd)

Box 2.3 (cont'd)

Table 2.19 Financing terms agreed with Vale by the BNDES and other financing partners

Financial institution	Currency	Date	Available for	Total amount available	Amount drawn at 31 December		
					2012	2011	2010
Revolving credit facilities							
Revolving credit facility – Vale/Vale International/ Vale Canada	US$	April 2011	5 years	3,000	–	–	–
Credit lines							
Nippon Export and Investment Insurance (Nexi)	US$	May 2008*(a)	5 years**	2,000	300	300	150
BNDES	R$	April 2008*(c)	5 years**	3,572	1,753	1,368	941
Loans							
Export-Import Bank of China Bank of China Limited	US$	September 2010(d)	13 years	1,229	837	467	291
Export Development Canada (EDC)	US$	October 2010(e)	10 years	1,000	975	500	250
Korean Trade Insurance Corporation ('K-Sure)	US$	August 2011(f)	12 years	528	409	161	–
BNDES							
Vale Fertilizantes	R$	November 2009(g)	9 years	20	20	18	18
PSI 4.50%	R$	June 2010(h)	10 years	379	343	258	100
Vale Fertilizantes	R$	October 2010(i)	8 years	121	110	109	91
PSI 5.50%	R$	March 2011(j)	10 years	50	43	43	–
CLN 150	R$	September 2012(k)	10 years	1900	1032	–	–
Vale Fertilizantes	R$	October 2012(l)	6 years	44	44	–	–
PSI 2.50%	R$	December 2012(m)	10 years	89	–	–	–

Source: Vale (2013: F-35).
*Memorandum of Understanding (MOU) signature date.
**The availability for application of projects is five years.
(a) Mining projects, logistics and energy generation. Vale through its subsidiary PT Vale Indonesia Tbk (PTVI) applied in the amount of US$300m for the financing of the construction of the Karebbe hydroelectric plant, Indonesia and withdrew totally.
(b) Mining projects, logistics and energy generation.
(c) Credit lines to finance projects.
(d) Acquisition of 12 large ore carriers from Chinese shipyards.
(e) Financing investments in Canada and Canadian exports.
(f) Acquisition of five large ore carriers and two capsize bulkers from two Korean shipyards. The maturity period is counted from each vessel delivery.
(g) Gypsum storage in Uberaba plant.
(h) Acquisition of domestic equipment.
(i) Expansion of production capacity of phosphoric and sulfuric acids at Uberaba plant (Phase III).

2.12 Financing terms

The BNDES provides concessionary credit that accounted for over 30 per cent of total credit in the country between 1997 and 2007 (Castelar Pinheiro 2012). The financing cost structure is as follows:

- Direct operations: financing cost + BNDES fee + risk premium = interest rate
  - Risk premium: margin to cover non-performing loans 0.0–3.57 per cent per annum
- Indirect operations: financing cost + BNDES fee + financial intermediation tax + financial institution spread = Interest rate
  - Financial intermediation tax: 0.0–0.5 per cent (SMEs exempt)
  - Financial institution spread: determined by the accredited financial institution
- The financing cost is calculated on the TJLP (long-term interest rate).
- The basic BNDES spread is based on the margin to cover operational expenses, 0.0–2.5 per cent per annum (0.9 per cent p.a. for SMEs).
- The Amortization Schedule varies from five to 15 years.

Collaterals: pledge on company´s shares; concession rights pledge; company receivables; corporate or banking guarantees; mortgage.

2.13 Conditionality

As the protection and development of local manufacturing is a key strategy of the Brazilian government, the BNDES makes its lending to some strategic sectors (such as renewable energy) conditional on securing local content in the project (PWC 2013). (For more information, see Box 2.2 Renewable energy sector.)

2.14 Environmental and social policies and practices

In 2008, the BNDES signed a 'Green Protocol' with the Ministry of Environment in which it committed to adopt social and environmental criteria in its financing operations. In 2009, the BNDES created an Environmental Division, previously encompassed under the social department.

The current structure of the BNDES Environmental Division is:

- Department of Environmental Policies and Studies (DEMAM): in charge of drafting environmental policies and provision of technical support
- Green Financing Department (DEOPE): development and execution of financial instruments and strategies related to sustainable environmental initiatives
- Amazon Fund Department (DEFAM): management of the Amazon Fund
- Legal Department (JUAMA): in charge of the legal aspects of operations, including checking compliance with environmental legislation.

In the framework of the World Bank Development Policy loan in 2010, the BNDES upgraded its commitment to sustainable development and on 9 November 2010 it issued the Social and Environmental Responsibility Policy (Resolution 2023/2010), in which economic, social and environmental aspects are incorporated into the view on development. With this document, the BNDES also commits to promoting respect for human rights, ethics and transparency, and to opposing any kind of discrimination and violation of human and social standards aligned to the international norms of behaviour.

There are also some sectorial guidelines (e.g. traceability for the cattle industry; Agroecological Zoning (ZAE) of cane sugar for the sugar and alcohol sector; energy production requirements related to emission limits; the accepted combustion systems;

solutions for the final disposal of ash from burning coal and from desulphuriser waste; restrictions on the use of water; and a compensation plan for greenhouse gas emissions) that set 'indicative' rules for projects in these sectors. They are designed from the joint work of the operational areas, the planning area and the Environment Area. The sectorial guidelines are not compulsory, i.e. there is no obligation to follow them as they are not included in contractual clauses, nor monitored or controlled (Franck 2012: 12).

The Committee for Eligibility, Credit and Capital Markets (CEC) is responsible for examining requests for financial support and also examines the environmental impact and makes recommendations about what policies have to be adhered to. Since the 1990s, following pressure from non-governmental organisations and trades unions, the BNDES has included social and environmental conditionalities in its process of project evaluation. In recent years, these conditions have become stricter for natural resource-intensive projects and projects to be developed in the Amazon (Motta Veiga and Rios 2013).

Despite the environmental and social safeguards in its project approval process, the majority of the BNDES portfolio (at least in value) is still made up of activities with a high impact risk.

Table 2.20 Impact risk of the BNDES portfolio

Level of risk	Description of risk category	Number of operations (%)	Value of the operations (%)
A	Activities present risks of significant environmental impact, or with regional scope. Licensing requires impact studies, preventive measures and mitigating efforts.	16	59
B	Activities present slight or local environmental impact. This requires assessment and specific measures.	46	30
C	Activities present no environmental risk.	38	11

Source: BNDES (2012b).

Box 2.4 The Amazon Fund

The Amazon Fund was created by the Brazilian Federal Government in 2008 and placed under the management of the BNDES, which is allowed to retain 3 per cent of proceeds to cover costs related to managing the fund (IDB 2013). The Fund obtained financial resources from the Government of Norway (US$1bn), the Kreditanstalt für Wiederaufbau (KFW) (€21m) and Petrobras (US$4m).

The main objective of the Fund is to provide financial support through non-reimbursable investments to projects aimed at preventing, combating, and monitoring deforestation in the Amazon (IDB 2012). Full Amazon Fund objectives are:

- management of public forests and protected areas
- environmental control, monitoring and surveillance
- sustainable forest management
- economic activities developed from sustainable use of the forest
- ecological and economic zoning, land-use planning and land-title regulation
- conservation and the sustainable use of biodiversity, and
- recovery of deforested areas.

(Cont'd)

Box 2.4 (cont'd)

Governance of the Fund:

- The BNDES, in charge of the management of the Fund: raising funds, analysing, approving, contracting, monitoring projects, and finally rendering accounts (IDB 2013)
- Steering Committee (COFA), responsible for setting the guidelines and priorities for the disbursement of funds, assessing the compliance of projects against the guidelines and monitoring results
- Technical Committee (CTFA), appointed by the Ministry of Environment and responsible for certifying reduced emissions from deforestation calculations made by the National Institute of Space Research and the Brazilian Forest Service (IDB 2013)

Project approval depends on meeting the following conditions:

- Eligibility: (i) projects must directly or indirectly contribute to reducing deforestation;[12] (ii) be compliant with the Amazon Fund guidelines and criteria of financing; (iii) meet the operational criteria of BNDES; and (iv) GHG emission reductions cannot be negotiated in carbon markets
- Pass the first assessment by the BNDES Priority Department of the Planning Division and a committee of senior executives
- Obtain a technical recommendation for approval by Amazon Fund staff
- Have final approval by the board of directors.

There is a results-based management framework (RBM) in place. Obtaining funds is linked to the achievement of reduced deforestation that is demonstrated if deforestation in the year prior to payment is lower than the average for the previous ten years (IDB 2013).

Monitoring and evaluation (M&E) procedures:

- The BNDES reports twice a year to the COFA on the fund's performance and fundraising progress.
- An external audit is carried out annually.
- Completed projects are required to deliver a report and an impact assessment highlighting environmental achievements.
- An annual meeting of the BNDES and donors must be held to discuss future directions of the fund.

Table 2.21 Scale of Amazon Fund operations (as at December of year)

	2009	2010	2011	2012	2013*
Number of projects	5	13	23	36	45
Amount (US$m)	40	99	134	189	270

Source: Amazon Fund (2013a).
*November 2013

Geographical distribution of supported projects:

- Paraíba 12 projects (27 per cent)
- Interstate 10 (22 per cent)
- Mato Grosso 8 (18 per cent)
- Amazonas 5 (11 per cent)

(Cont'd)

[12] Up to 20 per cent of the funding can be devoted to projects targeting other Brazilian biomes or other tropical countries to monitor and control their deforestation levels.

Box 2.4 (cont'd)

Sample projects:

IMAZON – AMAZON INSTITUTE OF PEOPLE AND THE ENVIRONMENT (US$5.5m; area covered: 66,640 km^2)

Description: IMAZON is a non-profit research institution working to promote sustainable development in the Amazon through studies, support for public policy formulation, broad dissemination of information and capacity building. Founded in 1990 and located in the metropolitan region of Belém (Pará, Brazil), IMAZON is a member of the Amazon Network for Socio-environmental Information (RAISG). In partnership with Google, IMAZON has developed the Deforestation Alert System (SAD), a monitoring technology available worldwide (Imazon 2013). In 2012, the BNDES contributed 18.86 per cent of the funds received in that year. The financed projects are about the collection of environmental and land-related data on rural properties in order to register land owners at the Environmental Rural Registry (state of Pará).

TNC – THE NATURE CONSERVANCY (US$9.1m; area covered: 120,000km^2)

Description: TNC promotes the environmental registration of rural producers operating in the sectors of wood production, cattle-raising and soybean harvesting in 12 municipalities of the Mato Grosso and Pará states.

IOV – OURO VERDE INSTITUTE (US$3.1m)

Description: IVO is involved in the environmental recovery of degraded areas by introducing sustainable forest management, agricultural production and animal-raising practices and helping family farms in six municipalities of Mato Grosso.

ARPA – PROTECTED AMAZON AREAS (US$11.4m; area covered: 320,000km^2)

Description: ARPA works to halt deforestation by creating and consolidating new conservation units.

FAS – AMAZONAS SUSTAINABLE FOUNDATION (US$11m; area covered: 100,000km^2)

Description: FAS prevents and controls deforestation by providing payment for environmental services, promoting sustainable productive activities and raising the living standards of the population in the forest.

Source: Amazon Fund (2013b).

Box 2.5 The Climate Fund

In 2010, Brazil founded the National Fund on Climate Change (FNMC), an institute that would provide finance to mitigation and adaptation projects as well as support studies on climate change and its effects. The BNDES is the institution appointed to manage this fund (Decree Nº 7,343 of 26 October 2010).

By law (the Petroleum Law) it was established that, together with funds coming from public, private, national and international donors, some of the resources to finance Climate Fund operations would come from a tax on profits in the oil sector. The 2011 FNMC budget was approximately US$132m (R$ 226m), while the estimated revenues were R$300m (approximately US$176m) per year (IDB 2012).

The Fund is a key instrument of the Brazilian government to implement the National Policy on Climate Change by offering support to projects that aspire to reduce greenhouse gas emissions and adapt to climate change. The Fund provides support to six types of investment projects related to the following areas:

1. Efficient means of transport
2. Efficient machinery and equipment
3. Renewable energy
4. Waste into energy
5. Wood coal
6. Combating desertification.

2.15 Debated issues

2.15.1 Environmental issues

- **The BNDES's energy strategy risks further contributing to climate change.** Aligned to the strategy of the Brazilian government, the BNDES supports hydropower development in the Amazon region with disruptive development impacts on forests and methane emissions together with other social, human and environmental impacts as claimed by numerous civil society organisations, represented in the BNDES Platform.[13]
- **Not having signed the Equator Principles.** Despite having signed the Green Protocol and made great improvements in promoting environmental and social safeguards, unlike other Brazilian banks (Banco do Brasil, Itau, Bradesco), the BNDES still has not signed the Equator Principles (Franck 2012). The BNDES also chose not to adhere to the International Finance Corporation (IFC) performance standards which guide the financial sector in incorporating social and environmental criteria into project finance (NGO Reporter Brazil and Biofuel Watch Center 2011).
- **No independent evaluation of the environmental impacts of financed projects.** The BNDES has been accused of being an important driver of deforestation in Brazil (Franck 2012: 13) due to its investments in cattle ranching, soybean plantations and hydropower plants. The reason behind this has been identified as the lack of appropriate and systematic assessment of the environmental impacts of BNDES-financed projects. The environmental impact assessments carried out are often undertaken by the same companies involved in constructing the project, which means they lack independence.

[13] A network established in 2007 and composed of over 25 organisations, involved in sector-based mobilisation movements that watch BNDES operations, promoting the respect of social and environmental safeguards. The platform draws on previous work carried out in the framework of the 2005 programme on Development and Rights launched by the Instituto Brasileiro de Análises Sociais e Econômicas (IBASE), a Rio de Janeiro-based civil society organisation.

2.15.2 Social issues

- **Sector-specific regulations are insufficient in practice.** Despite the BNDES putting in place sector-specific regulations related to the cattle raising industry, the meatpacking and slaughtering industry, and sugar-alcohol production, environmental and social violations are still being reported. For example, there is evidence of use of child and slave labour, indigenous land invasion and deforestation by companies running projects in those sectors.
- **Serious violations of legal, health and safety conditions, culminating in the use of slave labour.** The BNDES does not pay enough attention to the legal, health and safety conditions of workers in the companies getting its loans. The lack of safe working conditions caused numerous deaths on the construction sites of the large Belo Monte, Santo Antonio and Jirau hydroelectric plants. Although it was notified of health and safety violations by the local authorities, the BNDES extended its loans to such projects. Some of the companies financed by the BNDES have been reported for serious labour violations, culminating in the most extreme cases with the company being included on the Ministry of Employment's slave labour 'dirty list'. The BNDES generally only revokes financing of a company after it has been included on such a list. For example, Cosan – the largest producer of sugar and ethanol in Brazil – was officially included on the list in 2011. Critics of the BNDES point out that it should have taken action against the Cosan group well before it was included on the list as relevant irregularities had been reported during inspections of its plants – i.e. 'the extinction of individual labour contracts, excessive working hours, overtime, unhealthy and hazardous activities and operations, unpaid dismissal fees, problems with individual protection equipment, production incorrectly recorded, irregular working papers, labour intermediation, among others' (NGO Reporter Brazil and Biofuel Watch Center 2011: 16). The view of NGOs and civil society organisations is that the BNDES should not finance companies reporting such violations even if they have not yet been placed on the Ministry's 'dirty list'.
- **Invasion of indigenous land.** The BNDES has not taken into account the impact of projects on indigenous communities when approving several loans. For example, the huge Belo Monte hydroelectric project proposes to divert 80 per cent of the flow of the Xingu River and, as well as devastating an extensive area of the Amazon forest, will displace over 20,000 people, including indigenous peoples and other traditional communities (International Rivers 2012). In September 2013, some 150 indigenous people occupied one of the sites to demonstrate against the project (Amazon Watch 2013b).

2.15.3 Adverse impact on the Brazilian economy

- **Energy efficiency overlooked.** The BNDES does not prioritise energy efficiency. Rather, it has extensively supported energy projects such as hydroelectric dams so as to guarantee that demand meets the energy supply (from renewable resources). As argued by a WWF-Brazil study, investments in energy efficiency that would cut 40 per cent of the expected demand between 2007 and 2020 would save the equivalent energy produced by 14 Belo Monte hydroelectric plants, saving up to US$19bn and reducing the installed capacity by 78,000 MW (Banktrack 2014). To gain better understanding of the proportion of investments going to energy efficiency, International Rivers reports that in 2009 the BNDES disbursed US$8bn to Brazil's electric sector, of which only 0.1 per cent (about US$9.5m) went to energy efficiency projects (International Rivers 2012). The BNDES therefore seems myopic in considering the most valuable investments for the long-term sustainable development of the country.

- **Business interests dominate.** Strictly connected to the point made by WWF-Brazil, Franck (2012) argues that the BNDES would support a green economy dominated by business interests at the expense of Brazil's natural resources, environment and population. In this respect, the study quotes the controversial hydroelectric mega projects (e.g. the Belo Monte dam), nuclear power plants (e.g. Angra 3), unsustainable cattle-raising practices in the Amazon forests and finally the sugar cane plantations that are invading indigenous areas.
- **Displacement of agricultural crops to less productive areas.** Through its support for the expansion of sugar cane plantations to feed sugar-alcohol processing plants, the BNDES has been blamed for the displacement of other agricultural crops to less productive areas.
- **Reinforcing inequality** (Armijo 2013: 21). The BNDES finances large-scale, almost monopolistic, corporations, which account for over 70 per cent of all its disbursements, with the ten largest corporations making up 36 per cent of the total. Perversely, these bigger firms access cheaper credit than small businesses and poorer households, which have to borrow at higher rates. BNDES subsidised funding for such big companies is not really justified as they could easily raise funds from other commercial banks or in the international capital market (Castelar Pinheiro 2012).
- **The crowding-out effect.** The BNDES undermines the development of the private capital market in Brazil (Armijo 2013). The BNDES' presence in the Brazil capital market means that the market is heavily influenced by the state. The BNDES borrows from the government (Treasury) at a TJLP rate that is currently 5 per cent a year. This rate is much lower than the Central Bank's target overnight interest rate, making BNDES lending significantly cheaper than the market rate. This makes it very difficult for commercial banks to compete with the BNDES (Castelar Pinheiro 2012). The crowd-out effect has been smoothed in some cases as the BNDES managed to 'crowding in' other private banks and investors in some strategic projects, e.g. the Belo Monte dam, which has been co-financed by BTG Pactual and the Caixa Economica Federal.
- **Public money for centrally-prioritised investments.** The BNDES is said to provide long-term funding to be used in strategic sectors as set by the National Sustainable Development Strategy. In this position, the BNDES' subsidised financing is justified by the economic argument for government provision of public goods (Wheatley 2009). As a consequence, critics point out that the BNDES should restrict its operations to its core competency sectors (namely infrastructure, heavy industry, innovation and special purpose funds) instead of being present in every sector of the Brazilian economy.
- **Concessionary finance has the effect of raising Brazilian interest rates** (Arida 2005; Romero 2011; De Mello and Garcia 2012; Armijo 2013) as the state has to borrow at a much higher rate in order to fund the BNDES. In this context, the BNDES also falls beyond the authority of the Central Bank as BNDES interest rates are not determined by the Central Bank. Brazilian monetary policy affects the interest rates provided by other commercial banks (Castelar Pinheiro 2012).
- **Low profitability of funded projects.** Some of the projects financed by the BNDES have been found to have high costs and produce low returns, e.g. the Belo Monte dam which reached R$44bn (US$25bn). At the same time, some argue that the BNDES' use of public money to finance big companies at the expense of Brazilian taxpayers also has little economic justification. The money going to Petrobras, for instance, has been criticised for being excessive. The Finance Ministry borrows to lend to the BNDES, which in turn lends or buys stocks in Petrobras. This circle seems to fuel chronic inflation (Gall 2011).

2.15.4 Transparency and accountability issues

- **No external assessment.** There is no public discussion on Treasury allocations to the BNDES and no external assessments of the bank (Castelar Pinheiro 2012).
- **No detail on the Ombudsperson.** In 2003, the BNDES created an Ombudsperson responsible for replying to public and private suggestions, reporting misconduct, and dealing with complaints. Despite the importance of this institution in terms of accountability, the BNDES gives little information about its functioning and regarding complaints received.[14]
- **No public consultation carried out prior project finance approval.** The BNDES, through its portal BNDES Transparente, publishes a list and short description of approved projects by sector every three months. However, this is an *ex post* action and does not enable stakeholders to comment in advance on projects to be financed. As argued by Franck (2012), other multilateral development banks (e.g. the World Bank/IFC) disclose information prior to project finance being approved in order to leave room for discussion that is then taken into consideration by the Board approving the projects (Franck 2012: 15). Also, the BNDES provides very little information on the projects it finances, and should give more detail (NGO Reporter Brazil and Biofuel Watch Center 2011). For example, the bank does not publish the legal, social, environmental and land-related safeguards it demands from projects it funds, and gives no details regarding enforcement procedures related to the safeguards (such as appropriate adjustment measures and sanctions). In the case of the BNDES' socio-environmental policies, the lack of consultation with civil society organisations through Platforma BNDES may support ineffective policies. As argued, the BNDES should monitor closely the projects it funds, assess their impact and publicise what audits have been carried out and any sanctions that have been applied.

[14] See Accountability Counsel, www.accountabilitycounsel.org/resources/arg/the-brazilian-development-banks-ombudsperson/.

3 India Country Profile: The Exim Bank of India

3.1 Background

The development finance framework of India is highly fragmented. There are four types of development bank:

- **Industrial development banks:** e.g. the Industrial Finance Corporation of India (IFCI), Industrial Development Bank of India (IDBI) and Small Industries Development Bank of India (SIDBI)
- **Agricultural development banks:** e.g. the National Bank for Agriculture and Rural Development (NABARD)
- The Export-Import Bank of India (Exim Bank).
- **Housing development banks:** e.g. the National Housing Bank (NHB).

The Industrial Finance Corporation of India (IFCI) was the first development bank in India, established on 1 July 1948 under the Industrial Finance Corporation Act of 1948. Its objective is to provide medium- to long-term financial assistance to medium- and large-scale industries. Its resources come from (i) the issuing of shares and bonds ownership capital, (ii) borrowing from the Reserve Bank, the IDBI and central government, and (iii) deposits from the public, state governments and local authorities. The IFCI finances the manufacturing, services and infrastructure sectors.

The Industrial Development Bank of India (IDBI), was established on 1 July 1964 under an Act of Parliament. It was originally a wholly owned subsidiary of the Reserve Bank of India, but on 16 February 1976 its ownership was transferred to the Government of India. The bank provides credit facilities and other services to almost the whole range of Indian industrial activities, including manufacturing and services. It is also the principal institution coordinating the activities of other financial institutions in the country that promote and finance industrial development in India.

The Small Industries Development Bank of India (SIDBI) was set up on 2 April 1990 through an Act of Parliament for the promotion, financing and development of micro, small and medium-sized enterprises (MSMEs). Originally it was a wholly owned subsidiary of the Industrial Development Bank of India but now its shareholders are spread among various state-owned banks, insurance companies and financial institutions. As the SIDBI provides concessional credit to MSMEs, it has played an important role in India’s economic recovery following economic downturns.

The National Bank for Agriculture and Rural Development (NABARD) was established on 12 July 1982 by a special Act of Parliament. Its objective is to promote and develop agriculture, small-scale industries, cottage and village industries, handicrafts and other rural crafts, and other allied economic activities in rural areas. It was set up as an apex bank with the mandate to provide refinancing for lending institutions working in rural areas, as well as to promote institutional development and monitor client banks and other lending institutions.

The National Housing Bank (NHB) is an apex bank and was created on 8 July 1988 under the 1987 National Housing Bank Act. It is owned by the Reserve Bank of India and is in control of the country’s housing financial system. In this role, the NHB provides financial and other support to housing finance institutions both at local and regional levels.

The Exim Bank interacts with several international banks, multilateral institutions (the World Bank, International Finance Corporation, Multilateral Investment Guarantee Agency and

International Monetary Fund) and export-credit agencies (the Export-Import Bank of the United States, other US government agencies, industry associations and corporations).

Within this framework, the Exim Bank of India was created in 1981 as the leading development financial institute for the promotion of India's international trade.

As a consequence of India's expanding role in the global economy, the central government assigned the Exim Bank the task of channelling government credit towards foreign countries and/or Indian exporting companies by setting up lines of credit. Until 2004, the Exim Bank had a virtual monopoly in this (*Economic Times* 2004), but since then has shared the task with other national banks (the State Bank of India, the Bank of Baroda and the Indian Overseas Bank). The Exim Bank has also cooperated with other domestic institutions to fulfill this assignment. In 2013, for instance, it signed a Memorandum of Cooperation with the Small and Medium Business Development (SME) Chamber of India for the promotion of exports, which entails activities aiming to channel export finance, identify potential export markets, carry out research, and provide training and education (The Hindu Business Line 2013).

Since 1996, the Exim Bank has been part of the Asian Exim Banks Forum (AEBF), which comprises export credit agencies (ECAs) from India, Australia, China, Japan, Korea, Malaysia, Thailand (all founding members), Indonesia, the Philippines and, shortly, Vietnam. The Asian Development Bank has permanent observer status in the Forum.

In March 2006, the Global Network of Exim Banks and Development Finance Institutions (G-NEXID) was set up in Geneva and the Exim Bank of India became a member. The aim of G-NEXID is to foster enhanced South-South trade and investment cooperation.

In April 2010, the Exim Bank signed the Framework Agreement on Financial Cooperation within the BRICS Inter-Bank Cooperation Mechanism, together with Brazil's Banco Nacional de Desenvolvimento Economico e Social (BNDES), the Russian State Corporation Bank for Development and Foreign Economic Affairs – Vnesheconombank, the China Development Bank, and the Development Bank of Southern Africa.

In 2012, India's Exim Bank signed a memorandum of understanding (MOU) with the Ecobank Group (Togo) to support cross-border transactions and projects of common interest, facilitate India-Africa trade and investment, and the establishment of joint ventures (Exim Bank of India 2013a: 52).

In 2013, the bank signed a memorandum of cooperation (MOC) with the IDBI to co-finance, co-arrange, syndicate rupee and foreign currency loans, jointly finance export-oriented projects in India, and provide a refinancing facility to Indian export-oriented companies (in both Indian rupees and foreign currencies), particularly in the MSME sector (Exim Bank of India 2013a).

3.2 Origin and mission statement

The Exim Bank of India was established in 1981 by the Government of India to deal with international development and the integration of Indian companies into the world economy. Its official mandate is to: 'not just enhance exports from India, but also to integrate the country's foreign trade and investment with the overall economic growth'.[15]

[15] See www.eximbankindia.in/?q=organization.

Its main objectives as stated in the constituent act are:

> providing financial assistance to exporters and importers, and for functioning as the principal financial institution for coordinating the working of institutions engaged in financing export and import of goods and services with a view to promoting the country's international trade… act on business principles with due regard to public interest.
> (Export-Import Bank of India Act 1981)

3.3 History

When India introduced market-oriented economic reforms in 1991, the Exim Bank acquired a more powerful position in facilitating imports and augmenting exports according to newly-issued foreign policy measures. It was in 2003–04, however, that the Exim Bank was appointed to enhance the country's engagement with other developing countries.

In its 2003 budget speech, the Indian government launched the India Development Initiative (IDI), a new approach to development cooperation that officially shifted India from a recipient of foreign assistance to an aid donor (Fuchs and Vadlamannati 2013).

In 2004, as a result of this changing approach, the India Development and Economic Assistance Scheme (IDEAS) was launched to provide lines of credit through India's Exim Bank (Fuchs and Vadlamannati 2013; Chaturvedi 2012).

3.4 Mandate and strategy

The Exim Bank was created to provide financial support to exporting and importing companies and importers and to function as the principal financial institution for coordinating the working of institutions engaged in financing the export and import of goods and services with a view to promoting the country's international trade.

It supports Indian companies to 'invest abroad for, inter alia, setting up manufacturing units and for acquiring overseas companies to get access to the foreign market, technology, raw material, brand, IPR etc'.[16]

The strategy behind Exim Bank operations is that of promoting India's political, economic and commercial interests, as openly stated by the Government of India (Fuchs and Vadlamannati 2013). The whole structure of Indian aid, relying on lines of credit extended to overseas governments, has been interpreted as an instrument for Indian companies to gain access to overseas markets as well as to foster Indian investment abroad (Price 2005; Agrawal 2007; Kragelund 2008).

The lines of credit extended to African governments seem to have focused on oil-rich nations and there is also evidence of overlapping commercial and business interests for the Indian companies operating in those countries (both companies involved in infrastructure development and oil companies operating in the same countries). This has been explained in the literature as India's open interest in contributing comprehensively to the economic development of the developing countries to which it has extended aid, so as to create more business opportunities for Indian companies in all fields of the economy (Fuchs and Vadlamannati 2013). In those oil-rich African nations, Indian companies have reached sectors such as information and communications technology (ICT), infrastructure and agriculture (Agrawal 2007; Chanana 2010; Katti *et al.* 2009; Sinha and Hubbard 2012; Naidu 2008; Naidu and Herman 2009).[17]

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[16] See www.eximbankindia.in/?q=oif.

[17] This is a result of the Government of India's Techno-Economic Approach for Africa-India Movement (TEAM-9) programme which is implemented by extending lines of credit worth US$500m to nine West African countries (Kragelund 2008).

3.5 Organisational structure

The managing body of the Exim Bank is the Board of Directors, which is under the control of the Government of India, as appears clearly in its statute. The government nominates a chairman and a managing director, plus another two full-time directors (Press Information Bureau Government of India Cabinet 2011). Members from the Ministry of Finance, Ministry of External Affairs and Ministry of Commerce and Industry are also on the Exim board. The number of directors nominated by the government, however, cannot exceed 12.

The Board of Directors also comprises of one director nominated by the Reserve Bank; one nominated by the Development Bank and, finally, one nominated by the Export Credit and Guarantee Corporation Limited.

The functions of the bank are divided between the following divisions:

- Corporate Banking, responsible for financing programmes directed at Indian export-oriented companies.
- Project Finance/Trade Finance, in charge of administering export credit services (e.g. supplier's credit and pre-shipment credit)
- Agriculture Business, managing agricultural sector financing
- Small and Medium Enterprise, handling credit proposals from SMEs
- Export Services, delivering advisory and information services related to investment promotion
- Support Services, namely Research and Planning, Treasury and Accounts, Loan Administration, Internal Audit, Management Information Services, Information Technology, Legal, and Human Resources.

The Bank's Head Office is in Mumbai and there are nine regional offices in India. Overseas, the bank has representative offices in Johannesburg (South Africa), Dakar (Senegal), Addis Ababa (Ethiopia), Dubai (Emirates), London (UK), Singapore and Washington DC (US).

3.6 Sector focus

Table 3.1 Sector-wise exposure

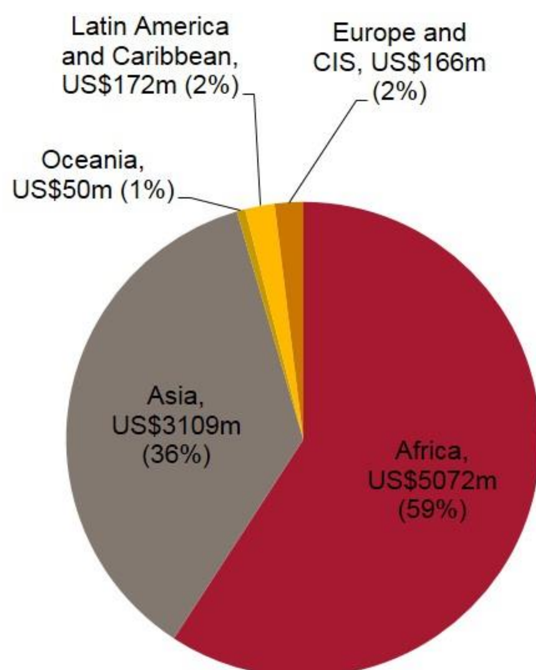
Sector	**(%)**
Ferrous metal and metal processing	10.41
Engineering, procurement and construction (EPC) services	9.41
Textiles and garments	8.06
Drugs and pharmaceuticals	6.28
Auto and auto components	5.55
Chemicals and dyes	5.50
Petroleum products	4.83
Capital goods	3.46
Non-ferrous metal and metal processing	3.31
Renewable energy	3.16
Other	40.03

Source: Exim Bank of India (2013a: 52).

3.7 Geographic focus

The Exim Bank has offered over 140 lines of credit (LOCs) to overseas governments and other financial entities. About 100 of these targeted African countries with a special focus on the agricultural sector (Vaidyanathan 2013). In 2012, the 18 LOCs extended by Exim India for financing exports of Indian projects, products and services in Africa totalled US$1,499m and reached the majority of countries in West Africa. In 2013, the Exim Bank allocated LOCs worth US$808.61m to African countries and US$697.37m to the Asian region.

Figure 3.1 Geographic distribution of the operative lines of credit (as at 31 March 2013)



Source: Adapted from Exim Bank of India (2013a).

Table 3.2 Geographic distribution of the operative lines of credit (as at 31 March)

	2005	2011*	2012	2013
Total	US$953m	US$7,054m	US$8,160	US$8,560m
Africa	32%	54%	53%	59%
Asia	42%	43%	42%	36%
Oceania	–	1%	1%	1%
Latin America and Caribbean	21%	1%	2%	2%
Europe and CIS	5%	1%	2%	2%

*as at 31 October 2011
Source: Exim Bank of India (2013a).

Most interest by Indian investors operating in Africa is concentrated in South Africa. Other countries are Algeria, Angola, Egypt, Morocco, Nigeria, Kenya, Ghana, Tanzania, Zambia, Côte d'Ivoire, Uganda, Kenya, Ethiopia and Mozambique (Jones 2013). In these countries the Exim Bank offered LOCs linked to infrastructure projects (power, road and rail), soft skill development, capacity building, technology knowledge transfer and training in exports (CII Africa Conclave 2012).

Table 3.3 Geographic allocation of Exim India credit lines in 2013

Region		Entity	Amount (US$m)
East Africa			93
	Burundi	Government	80
	Mozambique	Government	13
West Africa			325.6
	Economic Community Of West African States (ECOWAS)	ECOWAS Bank of Investment and Development	150
	Mali	Government	100
	Senegal	Government	27.50
	Togo	Government	15 and 13.10
	Nigeria	Nigerian Exim Bank	20
Southern Africa			50
	Zambia	Government	50
Central Africa			340.01
	Chad	Government	40.32
	Democratic Republic of Congo (DRC)	Government	168
	Republic of Congo	Government	70
	Central African Republic	Government	39.69 + 20
Asia			697.37
	Nepal	Government	250
	Republic of Maldives	Government	40
	Sri Lanka	Government	382.37
	Mongolia	Government	20

Source: Exim Bank of India (2013a).

Box 3.1 The Exim Bank's role in Government of India regional focus programmes

Other Government of India programmes administered by the Exim Bank are Focus Africa, Focus Latin America and the Caribbean and Focus Commonwealth of Independent States (CIS).

Focus Africa programme

On 31 March 2002, the Government of India (GOI) announced its Focus Africa programme along with its 2002–07 EXIM policy. The Programme was initially meant to target seven sub-Saharan countries – South Africa, Nigeria, Mauritius, Tanzania, Kenya, Ghana and Ethiopia – and to be later extended to all sub-Saharan African countries where India has diplomatic missions – i.e. Angola, Botswana, Côte d'Ivoire, Madagascar, Mozambique, Senegal, Seychelles, Uganda, Zambia, Namibia and Zimbabwe – and North African countries – i.e. Egypt, Libya, Tunisia, Sudan, Morocco and Algeria.

A process of country risk evaluation is undertaken by the Export Credit Guarantee Corporation of India (ECGC). The ECGC periodically reviews the grading of the perceived risk of each country and, wherever this improves, signals the change to the GOI and the Exim.

(Cont'd)

Box 3.1 (cont'd)

The objective under this programme – worth US$550m[18] – is to enhance commercial relations between India and African countries. The Exim Bank has been appointed as the implementing institution and administrator of export subsidies to Indian companies, including SMEs trading with African nations and LOCs to African governments tied to the purchase of Indian products (Fuchs and Vadlamannati 2013). Products traded under these arrangements are industrial manufactures, consumer durables and capital and engineering goods. The role of the Exim Bank in this context is that of an intermediary that mitigates the repayment risk for the Indian exporters. In fact, while part of the contract value (15–20 per cent) is paid in advance by the overseas importers, the rest (80–85 per cent) is paid directly by the Exim Bank to the Indian exporters on the shipment of goods (Government of India 2012a).

So far, the Exim Bank has contributed to India-Africa trade relations by offering US$6bn in LOCs to 45 African countries in order to promote their import of Indian equipment and services on deferred credit terms. Looking at the evolution of LOCs to Africa, there has been a significant increase in the volume of LOCs offered. In 2004/05, LOCs to Africa amounted to US$304m but had reached US$4.3bn in 2011/12 (Taraporevala and Mullen 2013).

The Indian LOCs to Africa have gone towards infrastructure and development projects, such as one hydroelectric project in the DRC; a housing project in Gabon; the development of the sugar industry in Ethiopia; the Gaza electrification project in Mozambique (Jones 2013); agriculture, ICT and potable water in Sierra Leone (US$74.45m); and a solar street-lighting project in ECOWAS (US$20m) (World Trade Organization 2013).

In Central Africa, the Exim Bank has supported Indian companies' exports of power transmission equipment and other industrial machinery into the DRC through a LOC of US$168m linked to the Ketende hydro-electric project (WTO 2013).

In East Africa, the Exim Bank has financed projects in textile, agribusiness and in natural resources sectors. For example, in Ethiopia Indian firms have invested heavily in agriculture and mining, and the bank contributed to the development and rehabilitation of the sugar industry by offering four concessional LOCs of US$213m, US$122m, US$166m and US$91m (WTO 2013; Schellhase 2013).

Table 3.4 Sector allocation of credit lines extended to African countries

Projects/sectors	Countries
Agriculture	Burkina Faso, Cameroon, Chad, Côte d'Ivoire, Gambia, Ghana, Madagascar, Mali, Senegal, Sierra Leone, Sudan and Tanzania
Construction	Gabon, Gambia and Ghana
Irrigation	Lesotho, Malawi, Mozambique and Senegal
Power generation	DRC, Equatorial Guinea, Ethiopia, Mali, Mozambique, Niger and Sudan
Power transmission and distribution, rural electrification	Burkina Faso, Ghana, Mali, Mozambique and Senegal
Railway rehabilitation	Angola, Benin, Ghana, Mali and Senegal
Road transportation	Central African Republic, Côte d'Ivoire, Ghana, Niger and Senegal
Technology (parks and training)	Côte d'Ivoire, DRC, Mozambique and Senegal
Sugar industry rehabilitation	Ethiopia and Sudan

Source: Exim Bank of India (2011).

(Cont'd)

[18] Value relating to the 2002–07 period.

Box 3.1 (cont'd)

Focus Latin American and Caribbean programme

India has demonstrated an interest in the trade growth potential of the Latin American and Caribbean (LAC) countries. The total merchandise exports of Latin America were US$1,097.207bn in 2011. Over the same period, India imported US$18.61bn from LAC. The total LAC imports in 2011 were US$1038.245bn, of which US$13.64bn was India's export to LAC.

Table 3.5 Top Indian trade partners in LAC in 2011–12 (in US$m)

Country	Exports	Imports	Total trade
Brazil	5,769.28	4,315.25	10,084.54
Venezuela	249.6	6,666.62	6,916.22
Chile	521.83	2,057.83	2,579.66
Bahamas	2,243.52	3.49	2,247.01
Argentina	473.45	1,052.61	1,526.07
Colombia	887.34	559.13	1,446.47
Peru	563.86	470.16	1,034.02
Panama Republic	232. 17	163.19	395.36
Ecuador	231.55	62.42	293.97
Trinidad	82.46	205.25	287.72

Source: Government of India (2012c).

Table 3.6 Top items of Indian exports to LAC in 2011–12 (in US$m)

Commodity	Apr–Mar 2011	Apr–Mar 2012	% Growth	% Share in 2011–12
Petroleum (crude and products)	3,852.56	5,035.12	30.70	41.04
Transport equipment	792.07	1,078.52	36.16	8.79
Drugs, pharmaceuticals and fine chemicals	682.11	71.49	4.81	5.83
Machinery and instruments	449.39	615.48	36.96	5.02
Plastic and linoleum products	219.68	628.18	185.95	5.12
Manmade Yarn, fabrics, madeups	514.86	566.09	9.95	4.61
Inorganic/organic agro chemicals	404.82	555.43	37.21	4.53
Cotton yarn, fabrics, made-ups	421.65	464.66	10.2	3.79
Manufactures of metals	193.66	251.84	30.04	2.05
Primary and semi-finished iron and steel	246.76	219.16	-11.18	1.79
RMG cotton incl. accessories	112.78	206.65	83.23	1.68
Rubber manufactured products except footwear	126.87	189.14	49.09	1.54
Other ores and minerals	175.72	164.99	-6.1	1.34
Electronic goods	120.2	154.58	28.6	1.26
Dyes/intermediates and coal tar chemicals	124.06	153.47	23.7	1.25

Source: Government of India (2012c).

Despite the modest position of India in LAC trade, the country has shown great interest in the potential of the LAC region and bilateral relations have grown steadily over time as a result of GOI efforts in boosting commercial relations. In November 1997, the Ministry of Commerce launched the Focus LAC programme aimed at granting incentives for Indian exporters to operate in the Latin America region. Products targeted by the programme have been:

(Cont'd)

Box 3.1 (cont'd)

- Textiles, including readymade garments, carpets and handicrafts
- Engineering products (and computer software)
- Chemical products, including drugs/pharmaceuticals.

These three categories now constitute nearly half of India's exports to the region (Government of India 2012c). In the textile sector, the main products are readymade garments, made-up fabrics, yarn, carpets and handicrafts. Among the engineering products are automobiles, auto components, electrical appliances and machinery. In the last group, Indian exports concentrate on bulk drugs, pharmaceuticals, dyes and intermediate agrochemicals, plastic products, naphtha, resins, essential oils, molasses, tyres for buses, trucks and cycles.

Table 3.7 Lines of credit extended by the Exim Bank through the LAC programme (in US$m)

Borrower	Amount of credit	Purpose	Tenure
Banco de Comercio Exterior de Colombia S.A. (Bancoldex), Colombia	10.00	General purpose	Up to 5 years
Corporacion Andina de Fomento (Andean Development Corporation) (covering Bolivia, Colombia, Ecuador, Peru and Venezuela)	10.00	General purpose	Tranche a: up to 5 years Tranche b: up to 2 years
Banco Bradesco S.A., Brazil	10.00	General purpose	Tranche a: up to 5 years Tranche b: up to 2 years
Republic Bank Ltd., Trinidad & Tobago	8.00	General purpose	Up to 5 years
Government of Suriname	16.00	General purpose	Up to 15 years
Government of Guyana	19.00	Cricket stadium in Georgetown	Up to 20 years
Government of Honduras	30.00	Communications, health, transport and Air Force components from India to Honduras	Up to 20 years
Government of Guyana	2.10	Signalling system	Up to 20 years
Government of Jamaica	7.50	Export of water pumps	Up to 12 years
Government of Suriname	10.40	Water supply project	Up to 15 years
Government of Suriname	10.59	Purchases from Bharat Electronics, Hindustan Aeronautics and Ordinance Factory Board	Up to 15 years
Government of Suriname	4.3	Supply of ten crash fire tenders	Up to 15 years
Government of Suriname	5.76	Purchase of helicopters from Hindustan Aeronautics	Up to 15 years

Source: Government of India (2012c).

(Cont'd)

Box 3.1 (cont'd)

Focus Commonwealth of Independent States programme

Launched in 2003, the Focus on Commonwealth of Independent States (CIS) programme initially focused on seven CIS countries: Azerbaijan, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, Ukraine and Uzbekistan. Later, the scope was extended to the rest of the region, including the Russian Federation, Armenia, Belarus, Georgia and Moldova.

Currently, the bulk of India-CIS trade is with Russia (61.2 per cent of India's exports; 59.8 per cent of India's imports from the region) and Ukraine (25.8 per cent of total trade). India's major export products to CIS are: pharmaceuticals; coffee/tea/spices; readymade garments, iron and steel, and machinery. India's major import commodities from CIS are iron/steel/nickel, fertilisers, mineral fuel, cereals, and rubber (Government of India 2012b).

Table 3.8 Lines of credit to CIS countries

Institution	Country	Amount (US$m)
Vneshtorgbank	Russia	25
Vnesheconombank	Russia	10
Bank TuranAlem	Kazakhstan	10
Absolut Bank	Russia	10

Source: Government of India (2012b).

3.8 Financial performance

Selected financial indicators (as measured at 31 March 2012)

- Total assets: 655.63bn rupees (approx. US$10.9bn); (547.50bn rupees (approx. US$9.10bn) in 2010/11)
- Ratio of adjusted total equity to adjusted assets: 9.8 per cent in 2012; (16 per cent prior to 2005)[19]
- Total profits: 10.89bn rupees (approx. US$179.6m); (10.13bn rupees – approx. US$168.4m – in 2010/11,)
- Non-performing loan (NPL) ratio: 1.46 per cent in 2012 (1.04% in 2011)[20]
- Return on assets (ROA) ratio: 1.13 per cent (on average over 2010–12 period)[21]

In total, the amount of loan disbursements during 2012/13 amounted to 406.35bn rupees (approx. US $6.66bn) while for 2011/12 they reached 370.45bn rupees (approx. US$607m) (Exim India 2013a). Guarantees issued amounted to CR 47.44bn (approx. US$ 778m) during 2012/13 (as at 31 March) and to CR 13.61bn (approx. US$223.38m) in 2011/12.

3.9 Sources of finance

The Exim Bank raises capital through (i) the issue/sell of bonds and debentures; (ii) borrowing from the Reserve Bank of India; (iii) borrowing from the central government or other national authority, organisation or institution approved by the central government; and (iv) borrowing from the International Markets.

[19] Reuters (2012).
[20] *Ibid.*
[21] *Ibid.*

Table 3.9 Total loan disbursements and guarantees 2003/04 to 2013/14 (in rupees billions)

Year	Approvals	Disbursements	Loan assets (1)	Approvals	Issuance	Guarantee portfolio
2003/04	92.657	69.575	107.751	10.792	5.743	15.769
2004/05	158.535	114.352	129.104	15.887	16.602	23.727
2005/06	204.887	150.389	175.931	43.264	21.959	34.023
2006/07	267.622	220.760	228.862	49.978	16.972	35.360
2007/08	328.045	271.587	287.767	21.994	20.386	34.556
2008/09	336.285	289.327	341.564	16.184	10.315	35.401
2009/10	388.430	332.485	390.357	13.508	3.875	22.736
2010/11	477.984	344.233	456.558	32.165	11.535	30.557
2011/12	444.119	370.451	538.898	27.549	13.611	32.407
2012/13	419.185	406.349	643.530	58.075	29.378	47.440

Source: Adapted from Exim Bank India (2013a).

Table 3.10 Origins of the Exim Bank's resources from 2003 to 2013 (in rupees billions)

Financial year	Paid-up capital	Reserves	Borrowings*	Total resources
2003/04	6.500	14.933	119.206	155.192
2004/05	8.500	16.625	120.118	156.922
2005/06	9.500	17.703	160.090	201.401
2006/07	10.000	18.741	216.616	262.439
2007/08	11.000	21.064	317.163	373.006
2008/09	14.000	24.681	372.023	442.017
2009/10	17.000	28.316	405.088	470.715
2010/11	20.000	32.302	471.918	547.508
2011–12	23.000	37.003	546.546	636.730
2012–13	30.594	41.796	644.848	761.182

*Borrowings include deposits which are net of reciprocal deposits placed/investments made with counter-parties for the years 2004–05 to 2006–07
Source: Adapted from Exim Bank of India (2013a: 2).

Currently the paid-up capital of the Exim Bank is 30.6bn rupees (approx. US$511m) and total resources amount to 761.2bn rupees (approx. US$12.7bn). Most of the bank's resources come from market borrowing – 644.8bn rupees (approx. US$10.7bn), which is 84 per cent of the bank's total resources.

The Government of India (GOI) wholly subscribes the issued capital of the Exim Bank. In 2011/12, the GOI made an infusion of Cr300 (approx. US$50m) (Exim Bank India 2013a) and again in late 2013 provided an extra Cr700 (approx. US$117m) into the bank's equity capital (*Economic Times* 2013). This increment follows an amendment of the Exim Bank's act in 2011, which increased the authorised capital of the bank from Cr2,000 (approx. US$334m) to Cr10,000 (approx. US$1.6bn) and approved the 'option for the government to further increase the capital 'up to an amount that it may deem necessary from time to time' (Press Information Bureau Government of India Cabinet 2011).

The strategy underlined by these measures is to provide the Exim Bank with the resources to take higher export credit exposures in a changing context where India needs to increment its presence in international markets.

Among its 2012/13 operations, the Exim Bank issued five-year US$500m and ten-year US$750m Eurodollar bonds, five-year Singapore dollar-denominated bonds of SGD250m, and five-year AU$200m Australian dollar-denominated bonds through its London Branch (Exim Bank of India 2013a). According to its 2012/13 financial statement, in 2013 the Exim Bank managed to raise about US$3.97bn in foreign currency resources from various sources.

3.10 Instruments deployed

The Exim Bank of India has different forms of support depending on the borrower and the nature of the project financed.

Under the Overseas Investment Finance Programme, it provides **term loans** to:

- Indian companies up to 80 per cent of their equity investment in overseas joint ventures/wholly-owned subsidiaries
- Indian companies towards up to 80 per cent of the loan extended by them to the overseas joint ventures/wholly-owned subsidiaries.
- Overseas joint ventures/wholly-owned subsidiaries for (i) capital expenditure towards acquisition of assets, (ii) working capital, (iii) equity investment in another company, (iv) acquisition of brands/patents/rights/other intellectual property rights, (v) acquisition of another company, and (vi) any other activity that would otherwise be eligible for finance from the Exim Bank had it been an Indian entity.[22]

Exim Bank also provides **guarantees** to the overseas joint ventures/wholly-owned subsidiaries, sustaining them in raising term loans/working capital. These guarantees amounted to 29.38bn rupees (approx. US$486m) in 2012/13 and were extended for overseas projects related to power generation, transmission and distribution, infrastructure development, and export obligation guarantees (Exim Bank of India 2013a).

The Exim Bank provides deferred credit on a medium- or long-term basis for project exports from India through buyers' credit under the **National Export Insurance Account** (NEIA). Access to this facility is restricted to a list of 40 countries approved by the Export Credit and Guarantee Corporation of India (ECGC), and belonging to SAARC or ASEAN, or in Africa, Central Asia, Eastern Europe, Latin America and the Caribbean. Exim Bank obtains credit insurance cover under the NEIA, a trust set up by the Ministry of Commerce. The beneficiaries of this facility are sovereign governments and government-owned entities in need of medium- and long-term deferred credit to import Indian goods and services (Exim Bank India 2013c). For example, the bank has provided US$248m for projects related to the functioning of a water treatment plant in Sri Lanka (Exim Bank of India 2013a: 38).

Lines of credit (LOCs) extended to overseas financial institutions, regional development banks, sovereign governments and other entities overseas act as intermediaries and lend to overseas buyers for the import of Indian equipment, goods and services on deferred credit terms. This instrument represents by far the most important one instrument, both in monetary terms – it makes the largest share of the bank's operation – and in strategic terms – it is the primary instrument employed to promote the economic, commercial and political interests of the Indian government overseas. As at 31 March 2013, the Exim Bank has provided US$8.6bn in the form of export credits, the largest share of which went for projects in Africa (US$5bn) and the second largest to Asia (US$3.1bn) (Exim Bank of India 2013a: 38). LOCs have been a key element in support of India's small and medium-sized enterprises (Chaturvedi 2012).

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[22] See www.eximbankindia.in/?q=oif.

3.11 Financing terms

3.11.1 Interest rates and other terms of lending

Table 3.11 Countries receiving loans from the Exim Bank – terms and conditions

Class of country	Names of countries	Interest	Period	Grace	Grant element
HIPC Heavily indebted poor countries declared under the Paris Club Initiative	Angola, Bolivia, Burkina Faso, Burundi, Cameron, Central African Republic, Chad, Comoros, Republic of the Congo, Democratic Republic of Congo, Côte d'Ivorie, Ethiopia, Gambia, Ghana, Guinea Bissau, Guyana, Honduras, Lao PDR, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Myanmar, Nicaragua, Niger, Yemen, Rwanda, Sierra Leone, São Tomé and Principe, Senegal, Somalia, Sudan, Tanzania, Togo, Uganda, Zambia, Vietnam	1.75% (fixed)	20	5 years	41.25%
LIHD Countries having low income and medium to high levels of debt*	Armenia, Azerbaijan, Bangladesh, Belize, Bhutan, Cambodia, Ecuador, Equatorial Guinea, Eritrea, Haiti, Georgia, Indonesia, Jordan, Kyrgyzstan, Lebanon, Lesotho, Madagascar, Moldova, Mongolia, Nepal, Nigeria, Pakistan, Panama, Papua New Guinea, Peru, Solomon Islands, Syria, Tajikistan, Ukraine, Uzbekistan, Yugoslavia, Zimbabwe	LIBOR + 0.5% (floating)	15	5 years	35.11%
MILD Countries having middle-level income and low levels of debt	Argentina, Brazil, Bulgaria, Colombia, Chile, Croatia, Dominica, Estonia, Gabon, Grenada, Hungary, Jamaica, Kazakhstan, Latvia, Malaysia, Philippines, Russia, Samoa, Slovakia, St Kitts and Nevis, St Vincent and Grenadines, Thailand, Tunisia, Turkey, Turkmenistan, Uruguay	LIBOR+0.5 % (floating)	8–10	2–3 years	17.11%–24.56%
MIHD Countries having middle-level income and medium to high levels of debt*	Albania, Algeria, Barbados, Belarus, Bosnia and Herzegovina, Botswana, Cape Verde, Costa Rica, China, Czech Republic, Djibouti, Dominican Republic, Egypt, El Salvador, Fiji, Guatemala, Iran, Lithuania, Macedonia, Maldives, Malta, Mauritius, Mexico, Morocco, Oman, Paraguay, Poland, Seychelles, Romania, South Africa, Sri Lanka, St Lucia, Swaziland, Trinidad and Tobago, Tonga, Vanuatu, Venezuela	LIBOR + 0.5% (floating)	12	4 years	28.75%

*According to the World Bank Statistical Appendix 2003
Source: Government of India (2014).

3.11.2 Currency

Rupee loans and advances accounted for 40 per cent of the total loan assets as at 31 March 2013, while the balance (60 per cent) was in foreign currency.

3.11.3Maturity

Table 3.12 Length of maturity of loans (in rupees billions)

Items	Less than or equal to 1 year	More than 1 year up to 3 years	More than 3 years up to 5 years	More than 5 years up to 7 years	More than 7 years	Total
Rupee assets	240.67	144.26	127.33	121.42	131.20	764.88
Foreign currency assets	217.18	147.01	132.25	63.87	138.50	698.81
Total assets	457.85	291.27	259.58	185.29	269.70	1463.69
Rupee liabilities	240.12	140.93	42.73	31.20	203.48	658.46
Foreign currency liabilities	215.79	146.80	11.716	53.47	161.15	694.37
Total liabilities	455.91	287.73	159.89	84.67	364.63	1352.83

Source: Exim Bank of India (2013a).

3.11.4Exposure norms

The Exim Bank complies with the norms set by the Reserve Bank of India relating to the exposure limit. The bank's exposure to a single industry sector cannot therefore surpass 15 per cent of the overall bank's credit exposure to all industry sectors.

3.12 Conditionality

The Exim Bank of India operates without conditionality, i.e. the bank provides credit while leaving the recipient countries free of deciding which projects to finance and the modalities (Chaturvedi 2012). No conditionality is attached in terms of political, social or environmental matters.

Lines of Credit (LOCs) provided by the Exim Bank have been interpreted as 'tied' in the sense that they are often bound to the requirement that 80–85 per cent of the goods and services procured for the realisation of the financed project is purchased from Indian companies.

3.13 Environmental and social policies and practices

Box 3.2 The Exim Bank's approach to green growth

The Exim Bank of India does not provide information on its environmental and social practices. There is also no publicly available indication as to whether or not some environmental and social appraisals have been undertaken before extending financial assistance to domestic export-oriented companies and/or overseas governments.

The bank interest in financing eco-friendly and energy efficient projects is proved by its participation in the 18th Annual Meeting of the Asian Exim Banks Forum held in Cebu, Philippines during November 2012. The forum discussed the role played by Exim Banks in the areas of co-financing of green projects, resource raising and training (Exim Bank of India 2013a).

More recently, on 9 May 2013, the Exim Bank of India signed an agreement for a 20-year €150m loan from the European Investment Bank (EIB) that will enable it to finance projects contributing to climate change mitigation. This EIB facility is the second of its type provided to the Exim Bank of India (the first was granted in December 2008) and is meant to support renewable energy projects (e.g. wind, solar, and biomass) and energy efficiency enhancement (e.g. fuel switching and plant modernisation), as well as projects that would reduce greenhouse gas emissions and contribute to a cleaner environment and afforestation.

3.14 Debated issues

LOCs vs ODA. Some have argued that LOCs could qualify as a form of Official Development Assistance (ODA) given that they satisfy the criteria of a grant element of at least 25 per cent. Nevertheless, Sinha and Hubbard (2011) and Fuchs and Vadlamannati (2013) point out that LOCs are extended for the purpose of export promotion, tied to the purchase of Indian products and services. LOCs therefore meet the criteria of officially supported export credits rather than ODA.

4 South Africa Country Profile: The Development Bank of Southern Africa

4.1 Summary key features

- The Development Bank of Southern Africa (DBSA) is one of four state-owned development banks in South Africa.
- It is wholly-owned by the Government of the Republic of South Africa and reports regularly to its National Treasury.
- The DBSA has two main objectives: (i) financial sustainability and (ii) development impact.
- It is a primary source of infrastructure financing in South Africa and in the Southern African Development Community (SADC). Almost three quarters of its overall budget goes to domestic operations, while approx. 25 per cent of funding goes to infrastructure projects in other African countries.
- The bulk of its activities are in support of municipalities. It provides finance to over 500 municipalities and to a wide range of public utilities and private firms.
- The institution is committed to public consultation and therefore maintains an open dialogue with its stakeholders.
- In the 2008 financial crisis, the DBSA struggled to play the role of countercyclical lender as it suffered the impact of the crisis and the NPLs increased substantially.

4.2 Background

With the 1994 elections, South Africa entered a complex political and constitutional transformation that led to a complete restructuring of the financial system and to the creation in 1996 of five separate development financing institutions (DFIs) in charge of facilitating the development of the country (Thomas 2001):

- The Industrial Development Corporation (IDC), with the mandate of providing finance for large-scale industrial development projects
- The Khula Enterprise Finance, dedicated to the development of small and medium-sized enterprises
- The National Housing Finance Corporation, with the mandate to provide financial assistance for housing
- The Land Bank, which deals with agricultural and rural development.
- The Development Bank of Southern Africa (DBSA)

In 1996, the DBSA stopped receiving annual funds from the government and was required to become self-sustainable, while contributing to the development of the country's infrastructure. Like the DBSA, all the DFIs were required by the government to be self-sustainable, while each ensuring the accomplishment of their own mandates.

The IDC[23] and DBSA both operate on a large scale in South Africa. The IDC was established in 1940 to support the development of domestic industrial capacity when trade between Europe and South Africa was disrupted due to the Second World War. The IDC has focused on the implementation of South Africa's industrial policy, mainly by providing financial support to the development of large industrial projects related to the petrochemical and mineral industries. The bank has also operated in favour of other industrial sectors – such as fabricated metals, agro-industries, clothing and textiles. Until the 1990s, the IDC operated

[23] With 112,230m rand (approx. US$10.6bn) total assets; 91,862m rand (approx. US$8.7bn) capital and reserves; and 3,410m rand (approx. US$324.7m) profit before taxation.

mostly within South Africa's borders, but since then has extended its operations to the rest of Africa. Its first venture was an aluminum smelter in Mozambique (IDC 2013). The IDC and DBSA have jointly participated in capacity-building initiatives such as the Pan-African Capacity Building Programme (PACBP) in 2010, which the Agence Française de Development (AFD) also contributed to. This programme obtained joint support of 55m rand devoted to the setting up of a capacity-building fund to support the development of competences for infrastructure development in Africa (DBSA, IDC and AFD 2010). Another field of cooperation between the two institutions, alongside the government's primary priority areas, has been funding via public–private partnerships (PPPs) to improve hospitals and provide finance for health projects (PPP Quarterly Online 2010).

The DBSA also has a longstanding partnership with the African Development Bank (ADB). With the aim of promoting broad-based economic growth, job creation, poverty reduction, regional integration and prosperity, in 2011 the ADB extended a fifth line of credit to the DBSA of US$300m for infrastructure development projects in the SADC region. The eligible sectors are: energy, transport, information and communications technology, health, housing, ports, roads, and water and sanitation; infrastructure and related sub-projects in resource-based industries such as agribusiness and mining; and manufacturing and infrastructure relating to tourism (ADB 2011).

The DBSA has cooperated with other financial institutions and private and public entities for both its domestic and external operations. For the development of the North-South Corridor, for instance, the DBSA has engaged with various African governments, as well as the South African government, regional development finance institutions and other international stakeholders. Projects in the North-South Corridor programme (linking Durban to the copper belt in the Democratic Republic of Congo and Zambia, and Dar es Salaam and the copper belt and Durban to Malawi) have been financed via a tripartite trust account managed by the DBSA with funds from the UK's Department for International Development (DFID) funded TradeMark Southern Africa (TMSA) programme. The projects have benefited from the tripartite alliance between the SADC, the Common Market for Eastern and Southern Africa (COMESA) and the East African Community (EAC) (DBSA 2013).

4.3 Origin and mission statement

The DBSA was established in 1983 by the South African government. The vision of the bank is 'to be a leading change agent for socio-economic development in southern Africa'. The mission of the bank is 'to contribute to development by providing finance and expertise to improve the quality of life of the people of southern Africa mainly through the provision of infrastructure'.

The main objects and mandate of the bank are provided for in the 1997 DBSA Act. Article 3 (1) notes that:

> The main objects of the Bank shall be the promotion of economic development and growth, human resources development, institutional capacity building (by mobilizing financial and other resources from the national or international private and public sectors) and the support of (sustainable) development projects and programmes in the region.
> (DBSA Act No. 13 of 1997)

4.4 History

At the time of its establishment in 1983, the DBSA received an initial capitalisation of 200m rand. Until the end of the apartheid regime in 1994, the DBSA operated in a credit risk-free environment (Thomas 2001), with the government providing annual transfers to the Bank.

With the political transformation following the 1994 elections, the government ceased fiscal transfers to the DBSA making it necessary for the bank to find alternative sources of funding in order to be financially self-sustaining (Musasike 2004). Since then, the DBSA has raised capital both domestically and internationally through the issuance of market-related debt-instruments (including Eurobonds).

Since 2007, the DBSA capital base has been eroded and has generated an estimated growth gap of 2.4bn rand in shareholders' equity (DBSA Integrated Annual Report 2012/13). At the end of the 2013 fiscal year, the DBSA reported losses of 825.9m rand (approx. US$89.3m) (Global Credit Research 2014).

The DBSA's negative performance led to it being downgraded by the rating agency Moody. The reasons for this were given as the progressive deterioration of the DBSA asset quality, its increasing credit concentrations and pressure on earnings. The deterioration of the quality of the bank's assets – apparent from an increase in the NPL ratio which reached 7.3 per cent from 4.9 per cent at year-end March 2012 – has been interpreted as a consequence of large exposures to the private sector, which in turn was negatively affected by the 2012/13 slowdown in economic growth in South Africa, and by labour unrest in the mining sector (Global Credit Research 2014). As for the increasing credit concentrations, the DBSA's top 20 exposures make around 67 per cent of total loans as at September 2013 (58 per cent in March 2013). This creates a great risk for the solidity of the bank in case of default by any of its large borrowers (Global Credit Research 2014).

As a consequence of its capital erosion, the government intervened by injecting 2.4bn rand in June 2013 as part of a total capital commitment of 7.9bn rand to be provided over three years and increasing the 'callable capital' (Global Credit Research 2014).

4.5 Mandate and strategy

The DBSA aims at financing strategic infrastructure projects and promoting the capacity to deliver infrastructure whilst achieving long-term financial sustainability.

Along with financial support to municipalities, the DBSA has played a part in institutional capacity building through a series of actions/programmes aimed at enhancing institutional ability to plan, implement and manage large-scale infrastructure projects – for example, the Siyenza Manjie programme entailed knowledge transfer and skills development in municipalities through the deployment of young professionals specialised in finance, engineering, project management, and town planning, etc. (Gumede *et al.* 2011).

According to what the DBSA itself states, it plays a triple role in the pursuit of its mandate, as quoted in its annual reports:

1. the 'financier', as it contributes to the delivery of basic services and the promotion of economic growth through infrastructure financing. It has also committed to play the role of market facilitator crowding-in rather than crowding-out private finance (National Treasury of South Africa 2011)
2. the 'adviser' as it provides development solutions and builds institutional, financial and knowledge capacity for development
3. the 'partner', working together with private, public and community stakeholders in the development process.

Table 4.1 The DBSA's triple role

Financier	Partner	Adviser
Making grants	Training	Providing development information
Lending	Acting as development catalyst	Providing policy analysis and advice
Investing	Leveraging funds and expertise	Advocacy
Underwriting	Facilitating development	Providing technical assistance
Arranging	Providing agency services	Research, monitoring and evaluation

Source: NDB-Kgarimesta (2004).

4.5.1 Domestic operations

The DBSA conforms to the government's priority national mandates. So far, special emphasis has been given to green energy, hospital and school infrastructure and water and sanitation (IDFC 2011). It has been appointed as the implementing agent for the National Infrastructure Plan, adopted by the government in 2012 to transform the country's economic landscape.[24] The DBSA is responsible for developing the business plan and for programme management of some strategic integrated projects (SIPs), in particular Integrated Municipal Infrastructure and Electricity Transmission and Distribution for All. These projects are intended to support economic development and address service delivery in the poorest provinces (DOE 2014).

4.5.2 External operations

The DBSA seeks to be a leading change agent for sustainable socioeconomic development in the SADC region as well as a strategic partner across sub-Saharan Africa (Musasike 2004). It focuses on financing large infrastructure cross-border projects to solve blockages around the delivery of infrastructure, thereby promoting regional integration and more equitable development, as part of its mandate to enhance trade and economic growth and foster regional integration.

4.6 Organisational structure

The Financing Operations Division supports both the South Africa Financing Division and International Financing Divisions by assessing and preparing projects, providing expertise and managing the DBSA portfolio.

The Infrastructure Delivery Division is responsible for the delivery of important infrastructure programmes, for example, in the education and health sectors.

The Risk Division was created in 1996, following the government's expectation of a self-sustaining DBSA, with the objective of providing a proper assessment of the risks involved in infrastructure project financing. The ultimate responsibility for risk management, however, remains with the Board of Directors.

4.6.1 Domestic operations

The South Africa Financing Division is responsible for all lending operations in South Africa.

4.6.2 External operations

The International Financing Division is responsible for investment and project development operations outside of South Africa (in Angola, Botswana, Democratic Republic of Congo, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Swaziland, Tanzania,

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[24] This focused on the assessment of the country's (i) basic needs, (ii) economic opportunities, (iii) state of existing infrastructure, (iv) required infrastructure, and (v) unlocking economic opportunities.

Zambia and Zimbabwe). It manages the funds of other international cooperating partners from both multilateral and bilateral institutions. To better evaluate and manage the risk associated with the investments in the SADC region, the DBSA monitors the country risk ratings of the countries that it deals with and respects country lending limits. Country risk ratings and limits are reviewed at least annually.

4.7 Sector focus

Prior to1994, the bank funded projects in all sectors, including agriculture, industrial development and small and medium-sized enterprises. In the period between 1994 and 1996, the government streamlined the entire development funding system. As a result, the five national DFIs refocused on their core sectors: the DBSA on infrastructure; the Landbank on Agriculture; the Industrial Development Corporation on industry; Khula Enterprise on small and medium-scale lending and the National Housing Finance Corporation on housing.

4.7.1 Domestic operations

Within the SIPs, of which the DBSA is the coordinator, the focus sectors are:

- Sewerage, bulk water and water reticulation
- Residual new build backlog maintenance and upgrade of water and sanitation
- Electricity distribution network builds and upgrades
- Maintenance and fixing of roads under the S'Hamba Sonke programme
- New road construction
- Boreholes in rural communities to provide access to water
- Revitalising clinics and hospitals
- Digital migration/access to digital TVs
- Solar water heaters
- Schools revitalisation programme.

Table 4.2 Disbursements and non-performing loans by sector (in 1,000 rand)

Sector	Disbursements				Non-performing loans			
	2012		2013		2012		2013	
	n	(%)	n	(%)	n	(%)	n	(%)
Commercial infrastructure	4,743,527	11	4,557,437	10	787,065	39	1,111,909	34
Communication and transport infrastructure	5,099,177	12	3,845,136	9	368,449	18	1,070,560	33
Energy	8,295,086	20	13,951,864	31	326,129	16	321,236	10
Human resources development	1,189,987	3	1,099,243	2	20,114	1	41,638	1
Institutional infrastructure	16,057	0	12,462	0	–	–	–	–
Residential facilities	2,334,863	6	2,193,949	5	112,221	6	253,452	8
Roads and drainage	9,087,516	22	9,988,235	22	50,571	2	61,667	2
Sanitation	1,429,999	3	1,375,748	3	86,928	4	90,677	3
Social infrastructure	4,259,678	10	3,988,656	9	160,574	8	214,538	7
Water	4,923,605	12	3,943,634	9	114,187	6	104,718	3
Total	41,379,495	100	44,956,364	100	2,026,238	100	3,270,395	100

Source: Adapted from DBSA Integrated Annual Report (2013).

For the electrification programme in rural areas, 205m rand were disbursed as part of a total of 2bn rand allocated by the DBSA and the Department of Energy to the Electrification Programme over a period of three years (Odendaal 2013).

Regarding the performance of loans by sector, two sectors – namely, the commercial infrastructure sector and the communication and transport infrastructure sector – cover the largest share of the NPL portfolio. Their joint contribution went from 57 per cent in 2012 to 67 per cent in 2013. The energy sector also records a large share of NPL; in 2012 this share equalled 16 per cent, while in 2013 it went down to 10 per cent.

4.7.2 External operations

In the SADC, the DBSA has focused on providing finance not only to infrastructural projects but also to economic growth sectors considered drivers for the economic development plans of those countries. The bank, through its International Financing Division approved projects for 2.9bn rand (approx. US$44.6m) in strategic energy and transport sectors in Angola, Mozambique and Zambia (DBSA 2013).

As at 31 March 2013, the DBSA reports the following loan exposure by sector:

- 34 per cent transportation
- 28 per cent energy
- 15 per cent financial services
- 6 per cent health
- 5 per cent manufacturing
- 5 per cent information and communications technology
- 7 per cent other.

The large exposure of the DBSA in the transportation sector refers to the activities related to the development of the North-South Corridor. Projects financed under this programme serve the goal of regional integration and development, and encompass various sub-sectors such as road, rail, ports, and one-stop border posts.

4.8 Geographic focus

About one-fifth of the DBSA's loans go for development in the SADC region, excluding South Africa. This region also accounts for more than half of the DBSA's non-performing loans.

4.8.1 Domestic operations

The bulk of the DBSA's domestic lending has gone to the Gauteng and KwaZulu-Natal districts. Gauteng recorded among the lowest share of NPLs, while KwaZulu-Natal accounts for a low but still substantial share of the NPL total during the last two years.

4.8.2 External operations

Within the realms of its mandate, the DBSA operates in other countries in the SADC region.

The government has recently issued a draft DBSA Amendment Bill that will extend the scope of authorised DBSA operations to African countries (beyond the SADC region) and the continent's oceanic islands following its enhanced engagement and relationship within the BRICS block (National Treasury 2013).

The DBSA's largest loan exposure to a single country is for Zambia (32 per cent), then Zimbabwe (12 per cent), Mozambique (9 per cent), Lesotho (8 per cent) and Angola (7 per cent) (DBSA 2013).

Table 4.3 Disbursements and non-performing loans by geographical region in South Africa and other SADC countries (in 1,000 rand)

Geographical region	Disbursements				Non-performing loans			
	2012		2013		2012		2013	
	n	(%)	n	(%)	n	(%)	n	(%)
Eastern Cape	1,667,787	4.0	1,895,894	4.2	256,070	6.5	154,916	2.4
Free State	570,997	1.4	660,933	1.5	86,812	2.2	996,011	15.7
Gauteng	13,433,450	32.5	15,053,541	33.5	33,531	0.9	46,447	0.7
KwaZulu-Natal	7,946,658	19.2	7,437,554	16.5	187,641	4.8	215,910	3.4
Limpopo	1,004,072	2.4	1,076,897	2.4	50,674	1.3	355,464	5.6
Mpumalanga	1,344,687	3.2	1,606,530	3.6	317,264	8.1	322,194	5.1
North West	910,386	2.2	639,902	1.4	83,392	2.1	9,250	0.1
Northern Cape	446,295	1.1	1,550,590	3.4	183,334	4.7	217,958	3.4
Western Cape	3,793,787	9.2	3,459,887	7.7	714,030	18.1	759,061	12.0
Multi-regional South Africa	7,614	0.0	5,913	0.0	–	–	–	–
SADC (excluding South Africa)	10,253,762	24.8	11,568,723	25.7	2,026,238	51.4%	3,270,395	51.5
Total	41,379,495	100	44,956,364	100	3,938,986	100	6,347,606	100

Source: Adapted from DBSA Integrated Annual Report (2013).

Table 4.4 Disbursements and non-performing loans by country (in 1,000 rand)

Geographical region	Disbursements				Non-performing loans			
	2012		2013		2012		2013	
	n	(%)	n	(%)	n	(%)	n	(%)
Angola	178,011	1.7	174,344	1.5	–	–	–	–
Botswana	57,573	0.6	43,412	0.4	57,573	8.1	43,412	5.7
Democratic Republic of Congo	70,780	0.7	86,342	0.7	–	–	–	–
Lesotho	949,179	9.3	889,767	7.7		0.0		0.0
Malawi	177,411	1.7	125,416	1.1	117,490	16.5	84,282	11.1
Mauritius	184,936	1.8	194,840	1.7	–	–	–	–
Mozambique	1,086,484	10.6	1,060,258	9.2	146,531	20.5	158,368	20.9
Namibia	644,229	6.3	545,821	4.7	–	–	–	–
Swaziland	202,578	2.0	215,174	1.9	126,734	17.7	136,804	18.0
Tanzania	377,717	3.7	374,544	3.2	–	–	–	–
Zambia	3,754,217	36.6	3,714,006	32.1	122,303	17.1	154,605	20.4
Zimbabwe	559,026	5.5	1,418,338	12.3	–	–	–	–
Other	2,011,621	19.6	2,726,461	23.6	143,399	20.1	181,590	23.9
Total	10,253,762	100	11,568,723	100	714,030	100	759,061	100

Source: Adapted from DBSA Integrated Annual Report (2013).

Table 4.5 Other financial indicators

	2008/09	2009/10	2010/11	2011/12	2012/13
Financial position (rand million)					
Cash and cash equivalents	2475	2707	1180	2113	1252
Financial market assets	5321	5521	4159	4842	4859
Investment in development activities (1)	31997	36133	41323	44432	47075
Other assets	589	695	736	950	754
Total assets	40382	45056	47397	52337	53940
Financial market liabilities (2)	22405	26327	28588	33612	36159
Other liabilities	741	943	957	1198	1075
Total liabilities	23146	27270	29546	34810	37234
Total equity	17236	17786	17851	17528	16706
Financial performance (rand million)					
Interest on development loans	2784	3077	3119	3514	3631
Interest on investments	677	525	469	468	437
Total interest received	3461	3602	3588	3982	4068
Interest expense	1705	1971	1945	2286	2442
Net interest income	1756	1631	1642	1697	1626
Operating income (3)	1857	1751	1794	1950	1938
Operating expense (4)	669	716	758	779	948
Sustainable earnings/(loss) (5)	871	807	808	677	-615
Profit/(loss) for the year	1426	518	29	-371	-826
Financial ratios (%)					
Total capital and reserves to development loans	59	54	47.20	43.40	39.20
Long-term debt to equity	131	149	161.60	193.80	217.40
Debt/equity (including callable capital) (6)	131	118	127.40	152.20	169.50
Cash and cash equivalents to total assets	6	6	2.50	4	2.30
Total capital and reserves to assets	43	40	37.70	33.50	31
Financial market liabilities to investment in development activities	70	73	692	75.60	76.80
Non-performing book debt as a % of gross book debt	5	5	4.20	4.90	7.30
Return/(loss) on average total equity	9	3	0.20	-2.10	-4.80
Return/(loss) on average total assets	4	1	0.10	-0.70	-1.60
Interest cover (times)	2	2	1.80	1.70	1.70
Net interest income margin (7)	51	45	45.80	42.60	40
Cost-to-income ratio	36	41	42.20	39.90	48.90

(1) Development activities, development loans and equity investments.
(2) Financial market liabilities comprise debt securities, lines of credit, funding under repurchase agreements, and derivative assets held for risk management.
(3) Operating income excludes net foreign exchange gain/(loss), net gain/(loss) from financial assets and liabilities, and impairments.
(4) Operating expense comprises personnel expenses, general and administration expenses, and depreciation.
(5) Sustainable earnings/(loss): Net profit/(loss) before grants, and adjustments to foreign exchange and revaluation of financial assets and liabilities.
(6) Measure includes 4.8bn rand callable capital.
(7) This ratio is calculated as net interest income (interest income less interest expense) over interest income.
Source: DBSA Integrated Annual Report (2013).

4.9 Financial performance

Selected financial indicators[25] (as measured at the end of 2012)

- Total liabilities: 37,234m rand (approx. US$3.5bn)
- Total equity: 16,706m rand (approx. US$1.5bn)
- Total assets: 53,940m rand (approx. US$5.1bn)
- Tot. Profits: 826m rand (approx. US$78.2m)
- Non-performing loan (NPL) ratio: 7.30 per cent
- Return on assets (ROA) ratio: 1.60 per cent
- Return on equity (ROE) ratio: 4.80 per cent

4.10 Sources of finance

The DBSA is a self-funded development finance institution. Its capital comes from:

- Internally generated sources
- Bond issues, private placements with select investors – in domestic and international capital markets
- Lines of credit with supranational and major bilateral financial institutions as well as commercial banks – e.g. the African Development Bank (ADB), the Korea Eximbank, the European Investment Bank (EIB).
- 'Callable capital' that the DBSA could draw at any time and implicitly guarantees the intervention of the Southern African government in case of need.

Table 4.6 DBSA capital structure (in rand thousands)

	2012	**2013**
Debt securities	25,808,711 (approx. US$2.4bn)	25,790,079 (approx. US$2.4bn)
Held at fair value through profit or loss (1)	7,876,593	8,390,655
Held at amortised cost (2)	17,932,118	17,399,424
Lines of credit – Held at amortised cost	7,705,306 (approx. US$733.6m)	10,081,507 (approx. US$960m)
Funding under repurchase agreements (3) – Balance at the end of the year	–	201,752 (approx. US$19.2m)
Capital authorised	5,000,000 (approx. US$476m)	5,000,000 (approx. US$476m)
Permanent government funding (4) – Balance at the end of the year	3,792,344 (approx. US$361m)	3,792,344 (approx. US$361m)
Revaluation reserve on land and buildings (5)		
Balance at the beginning of the year	245730	255088
(Loss)/gain on revaluation of land and buildings	9358	–1601
Balance at the end of the year	255088 (approx. US$24.2m)	253487 (approx. US$24.1m)

(1) Debt securities designated at fair value through profit or loss consists of DV bonds and private placements listed and unlisted.
(2) Debt securities carried at amortised cost consist of Euro rand bond issues, Money Market Issuance (bridging bonds).
(3) Investments under resale agreements. In the ordinary course of business, the bank raises short-term funding through the repurchase market. This entails the sale of financial assets in such a way that all or part of the assets do not qualify for

[25] Compiled according to the official data provided by the DBS. See www.DBSA.com.cn/english/NewsInfo.asp?NewsId=4448 (accessed 27 January 2014).

derecognition cost. The essence of such a transaction is to raise short-term funding through the repo market. The financial instruments thus transferred include government bonds, corporate bonds and municipal bonds. The bank retains substantially all of the credit risks and rewards associated with the transferred assets, and continues to recognise these investments within investment securities, whilst the corresponding financial liability considerations received are recognised in funding under repurchase agreements. At 31 March 2013, the fair value of the financial assets used as collateral is 202m rand (2012: Rnil).
(4) This represents capital provided by the South African government and remains part of the permanent capital of the bank. No funds have been received since March 1994.There are no repayment terms and this funding is interest free. To date, no cash repayments have been made and the full amount initially received is equal to the residual amount and is thus allocated to equity.
(5)This reserve represents the valuation surplus recognised on the revaluation of the land and buildings.
Source: DBSA Integrated Annual Report (2013: 97).

4.11 Instruments deployed

The instruments used by the DBSA can be classified in two categories:

- **financial:** lending/investment, guarantees, grants
- **non-financial products and services:** advisory services – e.g. preliminary project assessments (feasibility and pre-feasibility studies) to determine if a project is viable, technical assistance and capacity building, research (Hagerman 2012).

Table 4.7 Services provided by the DBSA, its operations and types of client served

Type of service	Operations	Clients
Project development advisory services	• Project identification • Feasibility assessments • Technical assistance • Financial structuring • Project preparation funds	• Municipalities • Public–private partnerships • Public–public partnerships • Regional integration
Project finance	• Debt • Mezzanine finance • Limited and non-recourse lending • Guarantees	In South Africa • Municipalities • State-owned enterprises • Public–private partnerships • Public–public partnerships • Private sector intermediaries Outside South Africa • No municipalities and sovereign
Accelerating infrastructure delivery	Managing the design and construction of key projects in the education, health and housing sectors	National and provincial government departments
Programme implementation	Project management support, including to the jobs and green funds	National and provincial government departments

Source: Coetzee (2013).

The DBSA is predominantly a debt provider, but also invests in equity instruments and, more recently, has started providing investment banking products such as arranging syndication and performing underwriting roles (Musasike 2004).

Box 4.1 The DBSA Development Fund

In 2001, the DBSA established the Development Fund to promote sustainable capacity-building at municipal level and to enhance service delivery and local economic development in support of municipalities. Aside from grants to development projects, the fund has provided a series of non-financial services, in the form of expertise, agency management services, sharing of knowledge and best practices.

The fund has provided its services through four programmes:

1. **National Provincial Implementation Support Programme:** in support of education, housing and health. In the education sector, the DBSA was appointed to support the construction of school infrastructure (689m rand was allocated to the construction of 49 schools in the 2011–12 period and the planning of another 70 schools to be constructed between 2013 and 2015).
2. **Municipal Capacity Building and Implementation Programme** which financed infrastructure and housing programmes in various under-resourced municipalities
3. **The Operations and Maintenance Programme:** providing capacity support to municipalities to run infrastructure maintenance activities
4. **The Jobs Fund:** a 9bn rand fund in support of job creation through the co-financing of public, private and NGO projects. By 31 March 2013, grants amounting to 4.3bn rand had been allocated to 17 public projects (1.4bn rand), 18 private projects (1.2bn rand) and 31 NGO projects (0.8bn rand) with an estimated impact of 100,524 new jobs created and 56,194 people employed in existing jobs.

4.12 Financing terms

The bank diversifies its portfolio in terms of country/sector spread and applies single obligor limits in order to mitigate risks. For its project finance, financing terms also vary depending on the nature of the project and its risk assessment.

4.12.1 Interest rate policy

The Board of Directors approves the DBSA interest rate policy, which interest rates applied to project finance (cost of funding plus a margin for risk and an internal overhead charge) are based on. Interest can be fixed rate or floating rate.

4.12.2 Maturity

Long-term debt can have a maturity up to 20 years if debt is issued in rand (Musasike 2004), and up to ten years for US$ and Euro debts (Mthembu 2012).

4.12.3 Repayment

Capital grace during construction.

4.12.4 Single obligor limits

The public sector single obligor limit varies for domestic and external operation:

- For South Africa, it is set at 10 per cent of shareholders' interest including the callable capital.
- For outside South Africa, it is 10 per cent of shareholders' interest excluding callable capital.

Also, no more than ten per cent of shareholders' interest may be invested in equity/quasi-equity in aggregate (Musasike 2004).

4.13 Conditionality

All programmes and projects proposed to the DBSA for financial support are subjected to an environmental appraisal (DBSA 2010).

The environmental conditionalities are incorporated in the legal agreements with its borrowers.

Before any fund can be disbursed, the DBSA may require proof of the acquisition of an environmental authorisation or permit. The bank can also act when the non-compliance with certain requirements would affect the environmental risks of a project to a certain extent. All these conditions are called 'suspensive' (DBSA 2010).

There may be further conditionality included in the agreement under the header 'further terms and conditions' and these are envisaged to ensure compliance with the environmental conditions identified in the loan agreement (e.g. the preparation of an environmental mitigation and management plan) (DBSA 2010).

4.14 Environmental and social policies and practices

The DBSA's environmental policy was approved by the Board of Directors in 2005 and designed in compliance with national and regional environmental policies, legislative and regulatory requirements, and international obligations and commitments (e.g. the United Nations Environment Policy Finance Initiative to which the DBSA is a signatory).

The DBSA's environmental policy requires all operations to be carried out in an environmentally and socially responsible manner, deriving the maximum environmental and social benefits (DBSA 2010). For this reason environmental conditionality applies to all projects funded by the DBSA. The DBSA will not provide funding for projects recognised as having a high environmental risk even after mitigation.

An environmental appraisal is an integral part of the project assessment and approval and must be carried out by an environmental analyst. Also an environmental specialist in the Advisory Unit must review all appraisal reports for high-risk and SADC programmes and projects.

Four types of risks are considered within the environmental appraisal:

- the environmental impact of the project, e.g. the risks of groundwater pollution associated with the establishment of a waste disposal site, road fill contamination with heavy metals, etc.
- non-compliance with legislative requirements, e.g. planning authorisation, EIA approvals, water permits, etc.
- the capacity of an institution to fulfil environmental requirements throughout all phases of project implementation
- reputational risks and public and political concerns.

The environmental appraisal takes place at all phases of the project cycle – project screening, site visit, environmental impact assessment, throughout implementation, and during the monitoring, completion and evaluation phases.

1. Application: an environmental analyst is assigned to the team assessing the application. He or she will determine the environmental risk category of the project and may require further information on the project.
2. Mobilisation of project resources and information: while the project team works together with the borrower to design the project, the environmental analyst will assess

the information provided and assist the client in fulfilling the environmental requirements.

3. Recommendation: the project team undertakes a detailed appraisal of the sustainability of the project, issues a recommendation on whether the DBSA should provide investment assistance and, if so on which terms and conditions.
4. Investment decision: Depending on the type and value of the project, the Development Intervention Committee, the Corporate Credit Committee or the Board Investment Committee decides about support for the project.
5. Contract: At the point of negotiation and agreement on the terms and conditions of the contract, environmental requirements suggested in the appraisal phase are included.
6. Implementation: all projects under implementation are monitored to ensure full compliance with the terms and conditions of the agreement, including environmental conditions.
7. Project completion: the DBSA monitors the project for the whole duration of the loan term.

Box 4.2 The Green Fund

The Green Fund was established in 2011 by the Government of South Africa/Department of Environmental Affairs, which made available 800m rand over three years to initiate the fund. The DBSA was then appointed as the implementing agent.

The Green Fund objectives are:

- Promoting innovative and high-impact green programmes and projects
- Reinforcing climate policy objectives through green interventions
- Building an evidence base for the expansion of the green economy
- Attracting additional resources to support the development of South Africa's green economy.

The fund operates in support of the 'green cities and towns', providing grants and concessional finance as well as assistance in project preparation. The sectors covered by this initiative are waste management and recycling; water demand management; public transport; municipal buildings and infrastructure; and urban greening. The applicants are municipalities and municipal entities and, to a small degree, other organisations.

The Green Fund promotes the shift to a low-carbon economy, focused on climate mitigation, renewable energy, energy efficiency, cleaner production, sustainable transport, and biofuels. Applicants to these schemes are private companies, research organisations, small to medium-sized enterprises and NGOs.

A third scheme through which the Green Fund provides support is the Environmental and Natural Resource Management scheme. This scheme focuses on biodiversity and ecosystem management, sustainable agriculture, fisheries and rainwater harvesting. Applicants are farmers and community-based organisations, research organisations, private companies and NGOs.

The instruments deployed by the Green Fund range from project development grants to capital development grants, research and policy development grants, and concessional project development loans (DBSA-DEA 2012).

In order to ensure the 'additionality' of financed interventions, the Green Fund supports only those projects that would not have been implemented without its support.[26]

[26] See www.sagreenfund.org.za/Pages/About.aspx.

Box 4.3 DBSA support to the green and renewable-energy sector

The DBSA's engagement in South Africa's transition to a green economy has been large, both in financial and political terms.

In the framework of the 2011 National Strategy for Sustainable Development and Action Plan (NSSD3) – whose priorities have been identified as providing effective responses to climate change, building sustainable communities and sustaining ecosystems through the efficient use of natural resources – the DBSA provided US$2.5bn for the industrial development green economy initiatives. These funds were accompanied by a further US$10bn raised from the private sector and US$80m from the National Treasury (Kaggwa *et al.* 2013).

The DBSA has been appointed as the implementing agent for the Renewable Energy Market Transformation Project (REMT), a GEF/World Bank-funded project aimed at reducing barriers to renewable energy development in South Africa, thus enabling the country to reduce its greenhouse gas emissions and develop its renewable energy sector.

In comparative terms, the DBSA's financial support to the green economy is similar to that of other domestic banks such as the IDC, which provided 25bn rand (approx. US$2.8bn) over the 2011/2012 to 2014/15 period (Montmasson-Clair 2013). Also, with respect to the Renewable Energy Independent Power Producer Procurement Programme, the DBSA's loan facilities of 6.2bn rand (approx. US$0.7bn) in the first bid window (Vermeulen 2012) came along with the IDC contribution of 7.5bn rand (approx. US$0.8bn) extended over the first two phases in 2011 and 2012 (Montmasson-Clair 2013).

In 2012, the DBSA announced another round of loan facilities amounting to 9.6bn rand (approx. US$0.9bn), mostly targeting solar projects and including one wind energy project (see Table 4.8) (DBSA-DEA 2012).

Table 4.8 Loan facilities for renewable energy projects (in rand millions)

Province	Project name	Technology (sector)	Capacity (MW)	Total DBSA exposure
Northern Cape	De Aar Solar	Solar PV	483	647
Northern Cape	Droogfontein	Solar PV	483	650
Northern Cape	Abengoa KaXu	Solar CSP	100	1.300
Eastern Cape	Jeffrey's Bay	Wind	1.339	1.057
Northern Cape	Bokpoort	Solar CSP	75	1.900
Northern Cape	Abengoa Khi	Solar CSP	50	600
Northern Cape	Herbert	Solar PV	20	1.605
Northern Cape	Scatec	Solar PV	75	350
Northern Cape	Greefspan	Solar PV	10	110
Free State	Lesedi	Solar PV	75	400
Northern Cape	Letsatsi	Solar PV	75	400
Western Cape	Touwsrivier	Solar CPV	36	470
Northern Cape	Khathu	Solar PV	75	521
Northern Cape	Kalahari	Solar CSP	75	1103
Total			896.5 MW	9.668.50bn

Source: DBSA (2012).

5 Russia Country Profile: The Vnesheconombank

5.1 Summary key features

- The Vnesheconombank (VEB) is a 100 per cent state-owned policy bank.
- The VEB's mandate limits its operations to targeted sectors and to the regions of the Russian Federation.
- The VEB does not pursue profitability. On the contrary, it is meant to provide financial support to sectors characterised by high uncertainty and long-term pay-off.
- The VEB aspires to overcome infrastructural barriers and obstacles to national development and to foster the competitiveness and diversification of the Russian economy.
- Under the general objectives of its mandate, VEB is meant to foster specific development drivers such as the high-tech industrial sectors, small and medium-sized enterprises (SMEs) and exports.
- The VEB's external operations mainly take the form of export support activities and support to exporting SMEs via the Entrepreneurship Fund or the SME's bank.

5.2 Background

With the fall of the Berlin Wall and the dissolution of the Soviet Union, the former USSR territories – now belonging to the Russian Commonwealth of Independent States (CIS) – started a process of economic modernisation that revealed several shortcomings in the financial system. It became clear that the undeveloped financial, industrial and infrastructure facilities, along with a lack of long-term funding (Maidan 2012), were major challenges to the rapidly changing political and economic context in the CIS. Against this background, the mainstream literature has considered that the establishment of development financing institutions (DFIs) – both financial and non-financial – would be one viable solution to overcoming such structural deficiencies.

From the end of the 1990s and throughout the 2000s, a number of DFIs were created, especially between 2006 and 2008 (Maidan 2012). As a consequence, Russia now has a considerable variety of DFIs, which are ineffective and which do not coordinate with other peer institutions. The VEB stands out as the most important DFI in the whole of the Russian Federation, with total assets representing over 5 per cent of Russia's GDP.

The VEB is characterised by wide international cooperation with other financial institutes, especially DFIs. With their shared objective of supporting large infrastructural investment projects, the VEB and International Bank for Reconstruction and Development (IBRD) have established several joint financing programmes.[27] Their joint investment programme entitles the VEB to access IBRD funds – from a minimum of US$500m up to US$1bn – for a 15–30-year period at a below-market interest rate for infrastructure and industrial development projects. The programme includes the possibility of getting technical assistance from the World Bank and other DFIs in preparing project documentation. Another programme related to financing energy-efficiency projects in Russia provides access to a US$300m IBRD loan for a period of 18 years against a full sovereign guarantee from the Russian Federation.[28] In

[27] More details are available on the VEB website: www.veb.ru/en/strategy/pmfi/vebmbrd/.
[28] More details are available on the VEB website: www.veb.ru/en/strategy/pmfi/vebmbrd1/.

February 2011, the VEB and IBRD signed a memorandum of understanding setting up the Partnership for Modernisation Initiative, with the objectives to sustain the modernisation of the Russian economy and to promote mutually beneficial cooperation between Russia and the European Union. Priority is given to financing energy efficiency, transport, innovation initiatives related to small and medium-sized enterprises (SMEs), and the commercialisation of innovations in a number of sectors.

The VEB has engaged in intensive relations with the German Kreditanstalt für Wiederaufbau (KfW). This relationship has been fostered by the periodic German-Russian intergovernmental consultations that have been taking place annually since 2009. Within this framework, several agreements have been signed between the VEB and KfW. In May 2012, the VEB, the KfW and the Permanent Secretariat of the Council of the Baltic Sea States (CBSS) signed the so-called Baltic Memorandum to support SME financing in Russian territories adjacent to the Baltic Sea. A long-term US$110m loan agreement followed in November 2012 and, later, the International Fund for Entrepreneurship Support was founded with US$150m to introduce long-term foreign investments for SMEs in Russia.

The VEB belongs to the Montreal Group, a non-profit organisation comprised of the VEB, BDC (Canada), BNDES (Brazil), CDB (China), NAFINSA (Mexico), OSED (France) and SIDBI (India), which exchanges ideas and best practices on the challenges facing SMEs.

The VEB is also part of the Long-Term Investors Club comprised of important development financial institutes such as the European Investment Bank (EIB), the CDB, Cassa Depositi e Prestiti, KfW, Caisse des Dépôts et Consignations (CDC) and others. The club's principal objective is to develop a joint investment and enhance cooperation between major global investors.

5.3 Origin and mission statement

The Vnesheconombank (VEB) – the state corporation Bank for Development and Foreign Economic Activity – is a wholly state-owned bank with the mandate of 'fund(ing) major investment projects aimed at removing economic growth infrastructure restrictions'.[29] The VEB fills a gap in financing as it 'does not compete with commercial credit institutions and participates only in those projects that are not capable of receiving private investors' financing'. Along with these functions, the VEB:

- participates in funding investment projects aimed at modernising mono-cities
- provides support for small and medium-sized enterprises
- supports Russian exporters on world markets
- assists in raising direct foreign investments for Russia.[30]

5.4 History

The VEB traces its origins back to 1922, when it was established as the Russian Commercial Bank. In 1924, it was renamed the Bank for Foreign Trade of the USSR (Vneshtorgbank USSR). At the time, the bank was one of only three state-controlled banks and the only financial institution entrusted with servicing export-import transactions and foreign currency transactions.

Following new banking regulations introduced in 1987, the Vneshtorgbank was assigned broader duties and named the Bank for Economic Affairs of the USSR – Vnesheconombank of the USSR.

[29] See www.veb.ru/en/strategy/.
[30] See www.veb.ru/en/strategy/.

Between 1997 and 1999, after the fall of the USSR, the VEB was recognised as the legal successor of the USSR Vnesheconombank, and is responsible for restructuring the former USSR's liabilities due to foreign banks and financial institutions, the London Club and the Paris Club. The VEB played the role of intermediary between London Club creditors and the Russian Government for the rescheduling of the outstanding London Club debt (approx. US$31,700m as at 31 March 2000), which in 2000 was converted into new Eurobonds issued by the Russian government with maturity in 2010 and 2030.

In 2003, the VEB was appointed as the agent for managing Russian State Pension Fund assets. This task role, as the state trust management company for pension savings, is due to last until 1 January 2019.

In 2007, the bank underwent a profound transformation into a state bank for development, taking the German KfW model for both its mandate and internal procedures.

With the outbreak of the 2008 economic crisis, the VEB acted as a countercyclical lender, providing anti-crisis support to the Russian economy in line with Russian government policies and strategy. Once it had completed anti-crisis measures in 2010, the VEB refocused on its development mandate, dedicating resources to large infrastructure development projects.

In 2011, the VEB established the first Russian export credit agency (EXIAR), with a charter capital of approx. US$1bn, and the Russian Direct Investment Fund (RDIF). The fund – a 100 per cent VEB-owned subsidiary endowed with US$10bn – was created to encourage investments in high-tech sectors of the Russian economy.

In 2013, the VEB Asia Ltd was registered in Hong Kong. This is a 100 per cent VEB-owned subsidiary in charge of liaising with Hong Kong financial institutions and supporting Asian investors willing to finance large-scale projects in Russia.

5.5 Mandate and strategy

The VEB's official mandate is: 'to diversify the Russian economy, boost its competitive edge and encourage the inflow of investments'.[31]

According to the federal law 'On Bank for Development', the purpose of the VEB is:

> To promote competitiveness of the Russian Federation economy, its diversification, encouragement of investment activity through investment, foreign economic, insurance, consultancy and other activity contemplated hereby in order to implement projects in the Russian Federation and abroad, including projects involving foreign capital, aimed at development of infrastructure, innovations, special economic zones, environmental protection, support of export of Russian goods, works and services, as well as small and medium business support.[32]

The VEB helps to implement state economic policy aimed at overcoming infrastructural barriers to national development; boosting the development of the high-tech industrial sector, promoting the innovation and production potential of small and medium-sized enterprises; supporting industrial production and service export; and upgrading efficiency in the use of natural resources.

[31] See www.veb.ru/en/strategy/.
[32] See www.veb.ru/en/about/normpr/law.

Under these provisions, the VEB operates as a driver for economic development and private investment in Russia. It does so by operating in the following areas:

a. Investments and development in
   - top priority strategic industries for Russia
   - national infrastructure projects
   - other Russian banks
   - Small and medium enterprise development
   - Equity funds.

b. Export support in the form of:
   - Export credit finance, insurance and guarantees (heavy machinery, high tech equipment, etc.)
   - Cooperation agreements with other export credit agencies and export-import banks.

c. Agent of the state
   - Government debt management (London Club and Paris Club)
   - Government financial asset management
   - Pension fund management
   - Anti-crisis measures.

5.6 Organisational structure

As stated in its statute, the VEB group comprises: the state corporation 'Bank for Development and Foreign Economic Affairs (VEB), Russian banks, CIS-based banks, and Russian and foreign companies (collectively, the "Group")'.

The federal law on the 'bank for development' establishes the governing bodies of the VEB: the Supervisory Board, the Management Board and the Chair of the VEB.

The Supervisory Board is a collegial organ and represents the VEB's supreme governing body, responsible for defining the policy orientation of the bank within the framework set by the federal law. In particular, the Supervisory Board:

i. defines the major areas of the bank's activities,
ii. approves the bank's revenues/expenditures plan (budget)
iii. issues the annual report and other basic internal documents
iv. approves an independent external auditor to perform a mandatory annual audit of the bank's annual financial statements,
v. approves the head of the bank's internal control service and, lastly,
vi. makes decisions on approving transactions in compliance with the documents regulating the Bank's activities.

The board consists of eight members appointed by the Government of the Russia Federation and the chair of the VEB. The chairman of the Russian Federation Government, Dimitry Medvedev, is also the chair of the VEB's Supervisory Board, as a sign of the strong political connection between the government and the VEB.

The Management Board is a collegiate executive body of the VEB. It consists of the VEB's chairman (*ex officio*) and eight Management Board members appointed by the VEB's Supervisory Board.

The Chairman of the VEB heads the board and is in charge of its activities. It acts as the sole executive body managing the bank's everyday operations.

The VEB's headquarters are in Moscow and there are Foreign Representative Offices in London, Frankfurt, Milan, Paris, New York, Beijing, New Dehli, Mumbai, Johannesburg and Zurich.

The bank comprised of 33 standalone structural divisions and 17 representative offices in Russia and abroad.

The VEB is at the head of several subsidiaries operating in the same sector, which complement the bank and share the same mission and strategy.

Table 5.1 Operating segments of the VEB group

Segment	Criteria of classification/ division	Banks
Segment 1	Major banks within the group	VEB, SME Bank, Eximbank of Russia
Segment 2	Banks purchased in 2007 and 2008 (to recover their financial stability)	Sviaz-Bank, CJSC 'Globexbank'
Segment 3	Group's bank in Ukraine	PSC Prominvestbank
Segment 4	Group's bank in Republic of Belarus	Bank BelVEB OJSC
Segment 5	Subsidies and fund in which the Group holds a controlling ownership interest	OJSC 'VEB-Leasing', LLC 'VEB Capital', 'VEB Engineering' LLC, FCPF, Closed-endMutual Hedge Fund 'MRIF', Closed-end Mutual Equity Fund 'MRIF-II', OJSC 'Development Corporation of North Caucasus', RDIF Management Company, LLC, EXIAR, Mutual Fund RDIF, OJSC 'The Far East and Baikal Region Development Fund' and other subsidiaries

Source: Compiled from information provided in the Memorandum on Financial Policies, Vnesheconombank 2012 Annual Report.

5.7 Sector focus

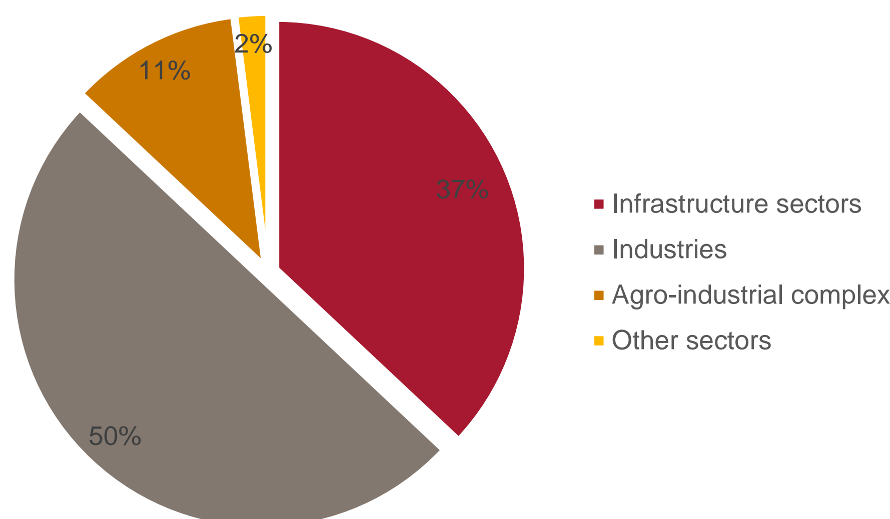
The VEB's sector priorities are set out in the Memorandum on financial policies of state corporation Bank for Development and Foreign Economic Affairs (Vnesheconombank) (No. 1007-r, July 27, 2007). As established there, VEB operates in those sectors characterised by lack of private capital investments, mainly due to large investments and a long-term pay-off, and high uncertainty of investments.

In compliance with its mission and strategy VEB is engaged in financing investment projects in the following sectors: aircraft construction, rocket and space complex, shipbuilding, electronics industry, atomic industry including nuclear power engineering, heavy, transport, special and power engineering machine-building, smelting industry (production of special steels), timber processing industry, defence industrial complex, agro-industrial complex, strategic computer technologies and software, information-communications systems, medical equipment and pharmaceutics.

Loans extended to finance 33 projects in priority lines of economy modernisation amounted to RUB 159.7bn (approx. US$4.47bn), the majority of which were designed to increase power efficiency.

In terms of external operations, the VEB's export support primarily targets aircraft engineering and space and rocket complex; electronics; transport; special-purpose and power engineering; and the defence industry (Vnesheconombank 2013).

Figure 5.1 The VEB's loan portfolio (as at 31 December 2012)



Source: Adapted from Vnesheconombank Annual Report (2012:13).

5.8 Geographic focus

In line with its mission and objectives aimed at developing infrastructure and fostering innovation projects, the VEB has a relatively narrow geographic interest, focusing its financial operations almost exclusively on Russian Federation territory.

Such a tendency is more evident with respect to investment projects as compared to other operations. Indeed, only three investment projects have been financed outside the Russian Federation during the whole period. With regard to distribution within the Russian Federation, the VEB is engaging in investment projects throughout the Federation.

5.9 Financial performance

Table 5.2 Selected financial indicators (as measured at end of 2012)

Total equity	RUB 531.1bn (approx. US$17.2bn)
Total assets	RUB 2,919.1bn (approx. US$95bn); (RUB 2,531.9bn, approx. US$2.4bn 2011)
Total profits	RUB 17,488m (approx. US$566m; (RUB 7,480m, approx. US$247m in 2011)
Total disbursements	RUB 720.2bn (approx. US$20.7bn; (RUB 505.4bn, approx. US$14.1bn in 2011)
Non-performing loan (NPL) ratio**	n/a
Return on assets (ROA) ratio	0.0059%
Return on equity (ROE) ratio	0.032%

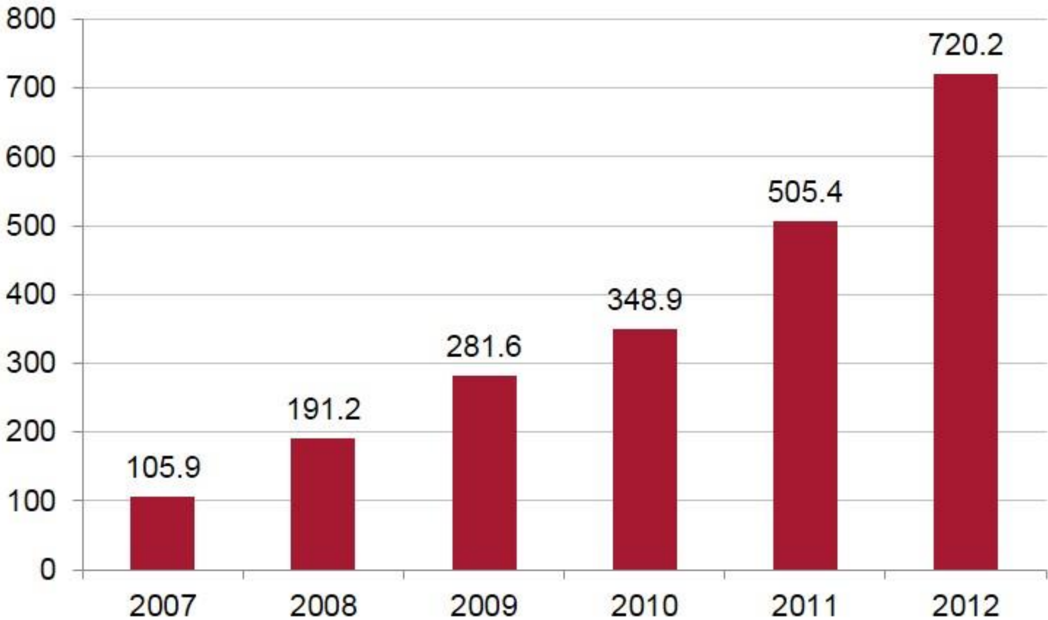
Source: Based on data from Vnesheconombank (2012).

As shown in Figure 5.2 below, the VEB's loan portfolio in 2012 was more than seven times bigger than in 2007, passing from about RUB 100bn (approx. US$4.05bn) in 2007 to more than RUB 720bn (approx. US$20.7bn) in 2012. This growing dynamic reflects the VEB's continued focus on its core business activities and the related provision of significant

financing for several large-scale infrastructure and investment projects, as well as strategic investments in Russian banks and corporates.

Since its peak in 2007/08, borrower concentration[33] has been reduced from 43 per cent to just 16 per cent at the end of 2012 (Vnesheconombank 2014).

Figure 5.2 Loan portfolio[34] (as at 31 December 2012 in RUB bn)



Source: Adapted from Vnesheconombank (2012).

5.10 Sources of finance

Given the bank's legal status as a state corporation, the Russian Federation and Ministry of Finance contributed continuously to the charter capital and paid-in capital of the VEB in the period 2007–11. The VEB's equity attributable to the Russian government for the year 2012 equalled RUB 531,177bn (approx. US$14.8bn). In order to ensure an appropriate resource base to fund its activities, the VEB also relies on other sources of finance. More specifically, in addition to traditional borrowing from other banks, the VEB can raise funds through placement of debt securities in the domestic and foreign capital markets, including Eurobonds, for a term of not less than one-year maturity.

The total amount of financial resources gathered in the capital market steadily increased year by year during the 2007–13 period, reaching RUB 527.8bn (approx. US$14.7bn) in 2012, of which almost 76 per cent have over five-year maturity. Financial resources gathered in 2011 amounted to about RUB 400bn (approx. US$11.2bn), of which 72 per cent had maturity of over five years.

Borrowing from other international financing institutions represents the main source of funding for the VEB. Recently, the bank has been particularity active in signing 19 individual loan agreements, including agreements with China, the US and Europe. With the China Development Bank, the VEB signed an agreement of US$1.43bn (with maturity of 14 years) to finance a project for the construction of Taishet aluminium plant in the Irkutsk Region (the biggest bilateral deal in 2012) (Vneshekonombank 2013: 48).

[33] Borrower concentration is measured as the ratio between the amount of the three biggest borrowers and gross loans.
[34] Portfolio of loans extended by the VEB to non-credit institutions, public executive bodies and municipalities for investment projects and export support, excluding loans extended using the funds of the Central Bank and the National Wealth Fund.

As a rule, funds obtained through bilateral agreements are bound to the realisation of specific investments, or destined to specific beneficiaries, i.e. SMEs. During 2012, the total amount of funds obtained through bilateral agreements amount to the equivalent of RUB 65.7bn to be destined to specific interventions (Vneshekonombank 2012).

5.11 Instruments deployed

The bank combines a wide range of financial instruments:

a. **Loans:** comprising a series of traditional financing products ranging from commercial loans, to project finance, pre-export finance, claims under letters of credit, etc. These items count for almost half of the VEB's total assets (Vnesheconombank 2012).
b. **Guarantees and securities:** mostly deployed for: (i) supporting large investment projects, or exports, (ii) supporting exports by guaranteeing exporters' obligations to foreign buyers, (iii) supporting businesses willing to invest in the Russian Federation
c. **Participation on equity:** the bank also provides financial support by purchasing shares, particular bonds and other kinds of financing participation instruments in the equity of investment projects, under a pay-back period of over five years, and for financing amounts of over RUB 2bn.
d. **Leasing transactions:** in favour of either investment projects or SMEs.

The VEB provides the following types of assistance:

- **Commercial loans:** the most important financial instruments for investment projects reaching RUB 746.33bn (approx. US$20.9) at the end of 2012
- **Loans to SMEs:** supporting SMEs' needs for capital
- **Project finance:** for the implementation of large infrastructural or energy projects through the acquisition of shares/participation on equity or bonds. For these operations, the VEB uses a special purpose vehicle (SPV), whose core activity is the realisation and management of the project over a long period. As a rule, the project and cash flows deriving from it once it is fully operative constitute the only guarantee for loan payback. Project finance is the second most deployed instrument following commercial loans
- **Export finance:** includes: export credits to foreign banks and non-banking institutions, pre-export financing of manufactured products to be delivered to foreign markets, guaranteed support for Russian high-tech exporters (worth approximately US$7bn for the 2007–13 period). As at 31 December 2013, the export finance portfolio amounted to approximately US$3.7bn (Vneshekonombank 2013).

5.12 Financing terms

As a general rule, the VEB offers credits and guarantees for projects with payback periods exceeding five years and for a total value higher than RUB 2bn. As stated in the Memorandum of the Bank's Financial Policies, the VEB complies with the following rules.

Box 5.1 The SME Programme

Financial support to small and medium-sized enterprises (SMEs) has entered the strategic priorities of the Russian Ministry of Economic Development which launched a public SME development programme, managed by a specialised development bank – the SME Bank – fully owned by the VEB. This VEB subsidiary provides loans at preferential terms through a network of partner banks to which the SMEs apply for funding. The SME Bank has had 247 partner banks and 202 partner organisations since the start of the programme, and has offered them funds containing a subsidy element and subject to capped interest rates. This financial support is intended to promote investments for the modernisation of production facilities or the creation of technological innovations. While SME Bank-funded enterprises still only make up about 1.5 per cent of the total banking sector, the SME Bank's portfolio has experienced a sharp increase, growing by over 120 per cent in 2011 (IPC GmbH 2013).

Table 5.3 Details of the VEB's SME programme

Size	RUB 98.59bn (approx. US$2.7bn) the total amount of support provided to SMEs (as at 1st quarter 2014)
Sector focus	Manufacturing sector, innovation-driven SMEs, entrepreneurs in regions with a difficult socioeconomic situation
Geographical focus	82 regions of the Russian Federation
Terms of lending	12.7% is the average rate on the portfolio loans; 65% of the loans with a maturity up to one year, 20% from 1 to 3 years, 15% over 3 years.

Source: IPC GMbH (2013).

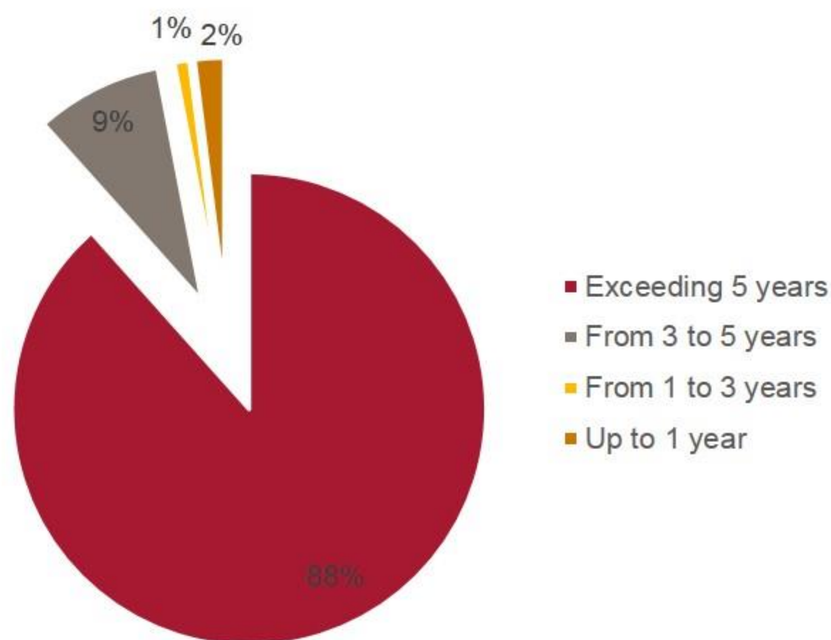
Table 5.4 Rules governing the VEB's credits and guarantees

Financial instrument	Beneficiary	Pay-back period	Project total value	Amount
Extending credits or loans	Investment projects aimed at developing infrastructure and implementing innovation projects	5 years or more	No less than RUB 2bn	More than Rub 1bn
	Credit institution and legal entity which provide financial support to small and medium sized enterprises	More than 2 years		Less than Rub 1.5m
Issuing or (and) extending guarantees and sureties	Industrial production exporting companies and Opened Joint Stock Company[35]	n/a		Less than 30% of the total value exported
Extending credit and providing guarantees and sureties	Organisations engaged in implementing state defence orders and targeted federal programmes in defence and security	Does not apply the general rules		Does not apply the general rules
Participation in the capital, through shares or other instruments	Investment projects aimed at developing infrastructure and implementing innovation projects.	5 years or more	No less than RUB 2bn	More than RUB 1bn

Source: Government of the Russian Federation (2007).

[35] A company established by the VEB which arranges insurance for export credits and investments against entrepreneur and political risk.

Figure 5.3 Loans to customers (by maturity) (as at 31 December 2013)



Source: Adapted from Vnesheconombank (2012: 22).

5.13 Conditionality

The Memorandum on the financial policies of the VEB clearly defines 'the core business and indicators of investment and financial activity' of the bank, restricting its operations from a qualitative and quantitative perspective. As a result, investment projects should fulfil several requirements to be eligible for support. Needless to say, such limitations in the VEB's mandate reflect its mission and strategy.

In particular, the projects are subject to sector restrictions. Only investment projects in the pre-established sectors (see Section 5.7) are considered. This restriction can be understood in terms of the Russian economy's high dependence on raw materials, from which derives the need to diversify the economy and foster new drivers for competitiveness. For this reason, oil projects, for example, are not supported.

Moreover, investments are subject to size restrictions. Indeed, only projects with a total cost of more than RUB 2bn are considered for financing support. In the same way, the minimum participation share of the VEB in each operation amounts to half of the total investment value or RUB 1bn.

Another restriction regards the ownership, provenance and situation of projects. Companies receiving financial support from the VEB should be owned or controlled by Russian companies. Investment projects are generally located within the Russian Federation.

5.14 Environmental and social policies and practices

Social responsibility has gained special attention in the VEB's operations. As a matter of fact, the VEB's Board has adopted a corporate social responsibility (CSR) strategy for the period 2012–15. According to the strategy document, CSR is an integral part of all the banks activities rather than a separate business line. This implies that the VEB is fully responsible for the social and environmental impact resulting from its decisions. By adopting a sustainability approach, the bank is expected to contribute to (Vnesheconombank 2012):

- increasing the bank's contribution to social, economic, and environmental sustainability
- raising the efficiency of managing the social and environmental impacts of the bank's activities
- developing the system of corporate governance
- improving the management quality of nonfinancial risks
- making the bank more attractive to investors
- positioning the bank as a modern development institution of international significance
- promoting stakeholder relations and increasing stakeholders' confidence in the bank
- building up corporate culture and enhancing employee loyalty towards the bank
- promoting corporate social responsibility in the business community.

In 2012, the VEB adopted guidelines for evaluating the social and economic impact of all of activities conducted with the bank's support.

Annex 1 Summary of results

	CDB	BNDES	EXIM INDIA	DBSA	VEB
Mandate	To provide medium- to long-term financing for the development of a robust economy and a healthy, prosperous community	To foster sustainable and competitive development in the Brazilian economy, generating employment, while reducing social and regional inequalities	To enhance exports and to integrate the country's foreign trade and investment with overall economic growth	To contribute to development by providing finance and expertise to improve the quality of life of the people of southern Africa mainly through the provision of infrastructure	To fund major investment projects aimed at removing economic growth infrastructure restrictions
Strategy	• Countercyclical lender • Domestic strategy: CDB has used Local Government Financing Vehicles (LGFVs) – companies set up by local governments – to finance infrastructure development through low interest asset-backed loans. • International Strategy: CDB engaged in cross-border energy and natural resources deals to implement the national government's 'going global' strategy, thus financing the expansion of Chinese firms abroad and securing long-term access to natural resources for China	• Countercyclical lender • Since the 1990s a founding agent promoting the internalisation of Brazilian companies • Financial support to large companies	• Not a countercyclical lender • Promotes India's political, economic and commercial interests: through lines of credit (LOCs) extended to overseas governments, Indian companies to gain access to overseas markets, and to foster Indian investment abroad • LOCs extended to African governments seem to have focused on oil-rich nations	• Not a countercyclical lender • Pursues financial sustainability • The bulk of DBSA activities have been in support of municipalities. DBSA operates as: • 'financier' as it contributes to the delivery of basic services and the promotion of economic growth through infrastructure financing • 'adviser' – i.e. it builds institutional, financial and knowledge capacity for development • 'partner' – working together with private, public and community stakeholders	• Countercyclical lender • Participates in funding investment projects aimed at modernising mono-cities • Provides support for small and medium-sized enterprises • Supports Russian exporters in world markets • Assists in raising direct foreign investments for Russia

(Cont'd)

Annex 1 (cont'd)

		CDB	BNDES	EXIM INDIA	DBSA	VEB
Size						
	Equity	US$79.8bn	US$24.9bn	US$1.06bn	US$1.5bn	US$17.2bn
	Assets	US$1,205bn	US$329bn	US$10.9bn	US$5.1bn	US$95bn
	Profits	US$10.2bn	US$3.6bn	US$179.6m	US$78.2m	US$ 0.566m
	NPL	0.30%	0.14%	1.46%	7.30%	–
	ROA	0.92%	0.46%	1.13%	-1.60%	0.0059%
	ROE	13.37%	6.96%	–	-4.80%	0.032%
Main funding sources		The main source of funds is the low-interest bonds with long-term maturities up to 30 years purchased by national commercial banks. Since 2000, CDB has also been selling in the international bond market.	• 1/3 from FAT/PIS-PASEP (workers' assistance fund) • 1/2 from National Treasury • Fundraising abroad only 3.3% BNDES borrows from the government at TJLP rate (subsidised rate now equal to 5%)	• Market borrowing is the main source – equal to 84% • Exim India also borrows from the Reserve Bank of India and from the Indian government	• Debt securities – approx. US$2.4bn • LOCs credit – approx. US$960m • Capital authorised – approx. US$476m	• Russian government (equity attributable to it approx. US$14.8bn). • Borrowing from other banks, debt securities in the domestic and foreign capital markets (approx. US$14.7bn of funds raised in 2012, of which almost 76% have over five-year maturity).

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Annex 1 (cont'd)

	CDB	BNDES	EXIM INDIA	DBSA	VEB
Instruments	• Asset-backed loans (e.g. land-backed) • Energy-backed loans • Loans and LOCs to support Chinese state-owned enterprises 'going global' • Equity funds	• Financing (e.g. project finance, export credits, etc.) • Non-reimbursable resources (e.g. grants to the Amazon Fund, etc.) • Subscription of securities: (e.g. subscription of shares, debentures, mutual fund shares and other securities to support publicly-listed and private companies like Petrobras, Vale, Odebrecht)	• Main instruments used are LOCs	• Financial: lending/investment, guarantees, grants; • Non-financial products and services: advisory services – e.g. preliminary project assessments, technical assistance and capacity building, research	• Commercial loans • Loans to SMEs • Project finance • Export finance

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Annex 1 (cont'd)

	CDB	BNDES	EXIM INDIA	DBSA	VEB
Terms of lending	• Long terms (up to 20 years) • Commercial interest rates (no concessional rates) • Off-taker agreements – i.e. the obligation to buy Chinese goods correspondent to a certain percentage of the loan received (e.g. 60% of the loan amount in the case of Ghana)	• Long terms • 1997–2007 30% was concessionary credit • Local content conditionality • Direct operations: financing cost (TJLP) + BNDES fee + risk premium = interest rate • Indirect operations: financing cost (TJLP) + BNDES fee + financial intermediation tax + financial institution spread = interest rate	• No political and/or environmental conditionality attached to LOCs • 80–85% of goods and services procured for the realisation of the financed project is purchased from Indian companies Terms depend on the country class. • HIPC interest rate = 1.75% (fixed); maturity = 20; grace period = 5 years; grant element = 41.25% • LIHD interest rate = LIBOR+0.5% (floating); maturity = 15; grace period = 5 years; grant element = 35.11% • MILD interest rate = LIBOR+0.5% (floating); maturity = 8–10; grace period = 2–3 years; grant element = 17.11–24.56% • MIHD interest rate = LIBOR+0.5% (floating); maturity = 12; grace period = 4 years; grant element = 28.75%	• Environmental conditionality applies to all projects funded by the DBSA. • Maturity up to 20 years if debt is issued in rand, up to ten years for US$ and € • Grace period during construction • Single obligor limits (10%)	Credits and guarantees for projects payback periods generally exceeds 5 years (88%) and for a total value higher than RUB 2bn.

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Annex 1 (cont'd)

	CDB	BNDES	EXIM INDIA	DBSA	VEB
Sector allocation	The first three sectors are: • Public infrastructure (20.6%) • Roads (17.2%) • Power (energy and natural resources) (11.4%)	Share of disbursements: • Industry 30% • Infrastructure 33% • Agribusiness 10% • Trade and services 27% BNDES corporate shares: • Oil and gas 47.4% • Electric energy 10.9% • Mining 19.8% BNDES offers large support to the renewable energy sector (e.g. biofuels, hydroelectric energy)	The first three sectors are: • Ferrous metal and metal processing (10.41%) • Engineering, procurement and construction (EPC) services (9.41%) • Textiles and garments (8.06%)	The first three sectors are: • Transportation (34%) • Energy (28%) • Financial services (15%)	VEB sector exposure: • Infrastructure (37%) • Industry (50%) • Agro-industrial projects (11%) The majority of VEB's investments in modernisation projects focused on increasing energy power efficiency

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Annex 1 (cont'd)

	CDB	BNDES	EXIM INDIA	DBSA	VEB
Country allocation	Geographic allocation of CDB funds: Domestic operations: • Eastern China 46.10% • Central China 17.02% • Western China 20.85% • Overseas 16.03% External operations: • Loans to Africa US$13.7bn as of July 2012 • Loans to Latin American countries from 2005–11 US$62bn • Reported loans to Russia and Central Asia US$28bn	International operations: Earlier engagement in Latin America and the Caribbean (LAC) than in Africa • 2000–10 US$3.6bn to LAC of which 49.2% to Argentina and 19.8% to Venezuela • In Africa BNDES has engaged prevalently in energy, mining, construction, infrastructures; Brazilian companies operating in Angola, Mozambique and South Africa received most of BNDES financing. Domestic operations: Nearly half of disbursements goes to the south-eastern region of the country.	• Africa received 59% of LOCs in 2013 • Asia received 36% of LOCs in 2013 • LAC countries received 2% of LOCs in 2013 • Target countries in Africa: Burundi, Mozambique, West Africa, ECOWAS, Mali, Senegal, Togo, Nigeria, South Africa, Zambia, Chad, DRC, Republic of Congo, Central African Republic • Target countries in Asia: Nepal, Maldives, Sri Lanka, Mongolia • Target Latin American countries: Colombia, Corporacion Andina de Fomento (Andean Development Corporation) (covering Bolivia, Colombia, Ecuador, Peru and Venezuela), Brazil, Trinidad & Tobago, Honduras, Guyana, Jamaica, Suriname	• Almost 75% of its budget goes to domestic operations • approx. 25% of funding goes to infrastructure projects in other SADC countries	• VEB operates within the Russian Federation territory

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	CDB	BNDES	EXIM INDIA	DBSA	VEB
Environmental/ social policies	• Environmental impact assessment (EIA) required to all loan applications • Not a signatory to the Equator Principles • CDB environmental assessment is undertaken along the whole loan cycle and is structured around two phases – pre- and post-lending	• EIA required (but there is not an independent evaluation when producing the EIAs) • Not a signatory of the Equator Principles • 2008 – BNDES signed a 'green protocol' with the Ministry of Environment • 2009 – created an environmental division • Manages the Amazon Fund and the Climate Fund	• No information available • Not a signatory of the Equator Principles • Exim India manages the funds coming from the European Investment Bank (EIB) to be devoted to climate change mitigation projects	• DBSA will not provide funding for projects having a high environmental risk even after mitigation. • Environmental appraisal is an integral part of project assessment and approval throughout all phases of the project cycle (i.e. project screening, site visit, environmental impact assessment, project implementation, monitoring, completion and evaluation).	• No information available • In 2012 VEB adopted guidelines for evaluating the social and economic impact of financed projects.

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