Financial Times

**Guest post: assessing Brazil’s BNDES**

Jun 6, 2014 1:27pm [by guest writer](http://blogs.ft.com/beyond-brics/author/guestwriter/)

*By Aldo Musacchio and Sergio Lazzarini*

On May 28 [Márcio Garcia posted an article](http://blogs.ft.com/beyond-brics/2014/05/28/guest-post-time-to-wean-brazilian-companies-off-the-bndes/) (1) here arguing that there is scant evidence of the impact of the BNDES, the government-owned development bank, on the Brazilian economy. He provided a chart showing that, in the last decade, the bank has substantially expanded its credit activity while country-level investment to GDP has barely moved above 18 per cent. Luiz Carlos Ferraz of the BNDES [replied on June 2](http://blogs.ft.com/beyond-brics/2014/06/02/guest-post-bndes-and-brazilian-development/) (2) with a different chart depicting an apparent association between investment and BNDES disbursements. Ferraz wrote that “evaluations, assessments, and opinions must be made on technically sound analysis.” In this post we would like to contribute to this virtual debate by presenting some results of our own work, summarised in our latest book, [*Reinventing State Capitalism*](http://www.hup.harvard.edu/catalog.php?isbn=9780674729681). (3)

We concur with Ferraz that the BNDES had an important role in the industrialisation of Brazil, especially during the 1960s and 1970s. In fact, in our book, we provide a historical account of the role of BNDES and then present the results of a series of quantitative studies using firm-level data on the impact of recent BNDES activities.

A [paper](http://amj.aom.org/content/early/2013/03/05/amj.2012.0406.abstract) (4) that we wrote with Carlos Inoue, for instance, shows that equity investments by BNDESPAR, the investment arm of the BNDES, improved the performance and investment activity of firms during the 1990s. We found that firms subject to what we call constrained opportunity – that is, firms with a valuable market opportunity but that, at the same time, were constrained in their ability to use their cash to fund new projects – used funds received from BNDESPAR to increase capital expenditures and showed higher profitability in the long run. Yet these positive effects disappeared when we restricted our sample to the period 2002 to 2009.

In [another paper](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1969843) (5), we collected fine-grained data on BNDES loans to and equity investments in large firms during the period 2002-2009. We looked exclusively at large publicly-traded firms because, under bank secrecy laws, the BNDES does not disclose detailed, firm-level data on loans.

Using data for over 300 firms we did not find any effect of BNDES loans or equity investments on firm-level profitability or investment. The only consistent effect we found is that firms that get BNDES loans faced significantly lower cost of capital due to the subsidies that accompany such loans. Thus, our micro-level data provides support to Garcia’s claim that large Brazilian firms are getting subsidies without necessarily increasing investment. In this same paper, however, we found that the BNDES is not systematically lending to underperforming firms; thus, the BNDES is not a “hospital for ailing corporations”. On the contrary, the bank appears to be targeting the most profitable firms in Brazil.

These results unveil a paradox. By targeting firms with sufficient cash to repay their credit, the BNDES sharply reduces its rate of non-performing loans. Yet those are precisely the firms that are supposed to be less financially constrained because they can get loans or issue equity abroad.

We are aware that our research is not representative of the entire Brazilian economy. In fact, large, publicly-traded corporations are expected to depend less on BNDES credit than smaller firms. As independent researchers, we would love to get access to a more comprehensive database that allows us to look at the effect of BNDES loans on smaller firms, but the bank refuses to share its data. Still, our findings raise the question: Why does the bank continue to support large firms that are not apparently constrained in their ability to get capital? Around 60 per cent of BNDES credit targets large firms, more or less similar to the firms that are in our database of publicly listed enterprises.

It is likely that the BNDES is having an impact on smaller, credit-constrained firms that were not part of our study; and that its loans and equity are generating other externalities that we have not been able to measure. However, this still has to be demonstrated with rigorous research. For the moment, one thing is clear: the BNDES is not following selective criteria guaranteeing that only those companies facing harsh credit constraints are the ones getting subsidised loans.

The late Alice Amsden, one of the leading global authorities on industrial policy, wrote in her book *The Rise of the Rest* that “the major weakness of development banks… was not to spend on the wrong industries but to spend *too much overall.*” For the time being, we have reason to believe that the recent expansion of the BNDES may well be another illustration of the concern raised by Professor Amsden.

*Aldo Musacchio is an associate professor at Harvard Business School. Sergio Lazzarini is a professor at Insper, Brazil.*

(1)

**Guest post: time to wean Brazilian companies off the BNDES**

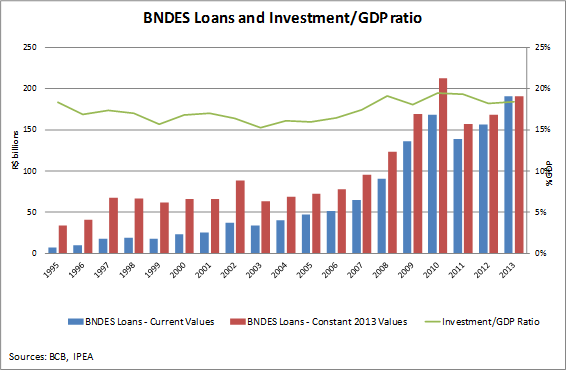
May 28, 2014 3:36pm [by guest writer](http://blogs.ft.com/beyond-brics/author/guestwriter/)

*[](http://blogs.ft.com/beyond-brics/files/2012/09/Marcio-Garcia.jpg)By Márcio Garcia of PUC Rio*

Another R$30bn ($13.5bn) in long-term loans will be given this year by Brazil’s National Treasury to the BNDES, the government-owned National Bank for Economic and Social Development. These transfers are made at a highly subsidised interest rate, called the TJLP, currently 5 per cent a year, while the central bank’s base rate, the Selic, is currently at 11 per cent. The Treasury’s transfers to government-owned banks, initiated in 2008, currently amount to almost 10 per cent of GDP, of which R$414bn has gone to the BNDES. These resources are lent by the BNDES to corporations, also at subsidised rates.

Nonetheless, Brazil’s investment to GDP ratio remains anaemic.

As the chart shows, in spite of the BNDES’s hyperactivity, the national investment rate remains below 20 per cent of GDP. This low investment to GDP ratio is one of the main explanations for Brazil’s mediocre average GDP growth for the 2011-2014 period, probably of less than 2 per cent a year.

[](http://blogs.ft.com/beyond-brics/files/2014/05/BNDES-loans-and-GDP-to-investment.png)

Source: Márcio Garcia

One may argue that the level of investment would have been even lower had the BNDES not taken steroids. But there is no evidence of this being the case. After all, in stark contrast to its initial mandate, BNDES loans go mostly to large corporations – 67.9 per cent of them, according to the bank’s 2012 Annual Report, the most recent available on its website. Yet large companies have access to financial and capital markets, in Brazil and abroad. They only resort to the BNDES because of the substantial subsidy on offer.

[](http://blogs.ft.com/beyond-brics/files/2014/05/breastfeeding1.png)

Honoré Daumier : La République. 1848. Paris, musée d'Orsay

Estimates put the cost of such transfers at more than 0.6 per cent of GDP, more than the 0.5 per cent of GDP spent on Brazil’s acclaimed *Bolsa Família*, a conditional cash transfer programme for poor families. And the cost is growing. Even if it were successful in boosting investment, it would not be feasible to maintain the growth of BNDES subsidised loans for much longer.

The big expansion of the BNDES’s parallel budget has been used do mask the true, lax position of fiscal policy. The National Treasury, which has a very high cost of capital (higher than the Selic’s 11 per cent a year), lends to the BNDES at a subsidised rate (the TJLP’s 5 per cent, or lower). The BNDES, in turn, lends to corporations adding a small spread. This generates (fictitious) profits for the BNDES, a share of which is passed back to the Treasury in the form of dividends. In other words, on the operation’s general reckoning, the Treasury incurs a high loss but, in the fiscal accounts, its primary fiscal revenues increase! This is an accounting trick that, in spite of repeated promises, the government refuses to give up.

In 2015, whoever he or she is, the next president of Brazil should heed calls to reverse the growth of subsidised loans. As the BNDES lends over the long term, the best policy would be to make the change gradually, reducing the volume of loans while steadily raising the TJLP towards the Selic rate, in order to prevent harm to long-term investment projects in progress. It would be unwise to go on raising lending until a fiscal crisis emerges. But the non-cooperative game of politics can end up leading to the worst outcome.

Recently, business leaders have reacted fiercely to criticism of the BNDES’s subsidies. One executive from the automotive sector, speaking off the record, was quoted in the newspaper [Valor Econômico](http://www.valor.com.br/politica/3540474/setores-da-industria-reagem-critica-de-aecio-creditos-subsidiados):

Brazil has big problems of competitiveness, generated partly by the cost of capital and the lack of a strong and dynamic capital market… I think it is justifiable to give loans solely for productive investment at incentivised rates to support competitiveness, for as long as the big reforms that the country needs, such as tax and social security reform, are not carried out.

So, instead of fighting for reforms that could actually help to solve the problems of Brazil’s high cost of capital and low competitiveness, this executive prefers to go for a rather selfish logic. First, the reforms should be carried out. Then, and only then, may the subsidies be withdrawn!

If part of Brazil’s business elite has such a non-cooperative attitude to reform, why should other beneficiaries of government programmes behave any differently? The next president’s job will certainly not be an easy one!

*Márcio Garcia is associate professor (Vinci Chair) at the economics department, PUC-Rio, Brazil.*

(2)

## Guest post: BNDES and Brazilian development

Jun 2, 2014 12:10pm [by guest writer](http://blogs.ft.com/beyond-brics/author/guestwriter/)

*[](http://blogs.ft.com/beyond-brics/files/2014/06/Jo%C3%A3o-Carlos-Ferraz.jpg)*By João Carlos Ferraz of the BNDES

The debate about Brazilian development has reached a consensus: investment is the key to a rebound. This is an interesting and very welcome phenomenon as economic analysts very seldom come to similar conclusions. However, when discussing development financing and the contribution of the country’s development bank, the BNDES, this debate has been largely characterised by shallow analysis, with extensive use of expressions with minimum substance, yet very conclusive in defining a negative role for the BNDES in pulling investment upwards. This has resulted in unproductive and even unfair attacks on one of the country’s institutions that has most effectively contributed to Brazil’s development.

At every moment of its 62-year history, the BNDES has well served the various stages of Brazil’s development and the priorities laid down by its governments. All this is well documented.

Criticising BNDES support for Brazilian business by using caricatures and derogatory terms, such as “the BNDES only supports big business” (the so-called “national champions”) may lead many to close their eyes, cover their ears and block their analytical capabilities to substantive assessments of its effective contributions.

I want to focus on one recurring issue – does the BNDES make a difference to investment? – by comparing different ways of assessing its recent performance. I hope that this simple and straightforward exercise may contribute to a more substantive reflection on the role of the BNDES in Brazilian development.

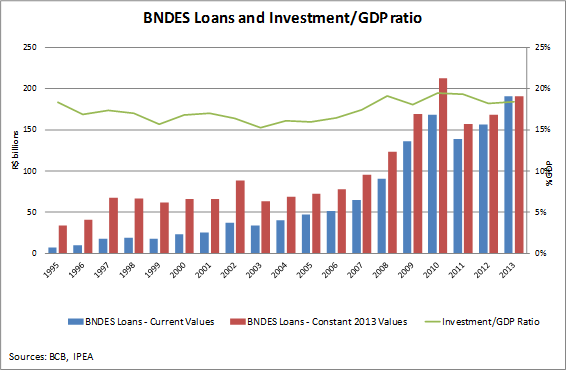
First, however, I must note that investment in Brazil is well short both of expectations and of the country’s needs. Despite the fact that, over the past 10 years, Brazil’s investment to GDP ratio has posted a stepwise recovery from 15.3 per cent in 2003 to 18.4 per cent in 2013, in recent years investment has stalled around that level and great challenges must be overcome to advance to higher levels.

And the BNDES? Its mission is to leverage investment, which must grow more quickly than GDP so that jobs are created and productive capacity expands ahead of demand, thus inducing systemic efficiencies and mitigating inflationary pressures. Even if inflationary pressure is created by the effects of BNDES lending on aggregate demand, these effects are temporary and should disappear in the long term, given the structural impact investment has on the economy.

So, what is the evidence on the relation between investment and BNDES lending? Please compare the three following charts:

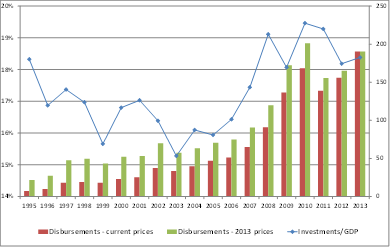
###### **BNDES disbursements (constant and current R$ billion) and investments (% of GDP)**

###### **Chart 1**

[](http://blogs.ft.com/beyond-brics/files/2014/05/BNDES-loans-and-GDP-to-investment.png)

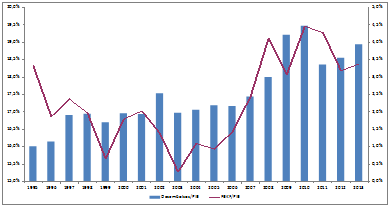
Source: Márcio Garcia

###### **Chart 2**

[](http://blogs.ft.com/beyond-brics/files/2014/06/BNDES-2.png)

Source: BNDES

###### **Chart 3: BNDES disbursements and investments (both as % of GDP)**

[](http://blogs.ft.com/beyond-brics/files/2014/06/BNDES-3.png)

Source: BNDES

Chart 1 reproduces the one presented by Márcio Garcia in a beyondbrics guest post on May 28, 2014. On the right axis, Garcia plotted investment to GDP on a scale from 0 to 25 per cent. On the left axis, BNDES disbursements are plotted, also starting from R$0, in both current and constant values. What is one led to conclude? That BNDES disbursements grew systematically, while the increase in investment was minimal.

On chart 2, I present a similar exercise with one difference: the rate of investment is plotted starting from 15 per cent, which is the minimum level reached in 2003. The graphic message is radically different from Garcia’s. But, as in the previous chart, there are technical glitches there, as two different variables are shown side by side. This calls for a third exercise.

The third chart presents both BNDES disbursements and investment as percentages of GDP. This is done to make the two variables comparable. The message here is similar to that of chart 2 and different Garcia’s exercise and the message he tried to convey. In both charts the BNDES is shown to be an institution that evolves in line with Brazilian development: disbursements and investments follow almost the same trajectory. Can this “visual dispute” demonstrate that BNDES makes a difference to investment? Can BNDES be considered not as the vanguard or the rearguard of Brazil´s development but rather as its “co-guard”? Each reader can draw her/his own conclusions.

The contribution of the BNDES to Brazilian development is not limited to the issue discussed here, given its role in financing infrastructure, capital goods, the expansion of industrial capacity, innovation, environmental sustainability, exports, culture, SMEs, etc. Given its overarching and sizeable influence on Brazilian development and as a public institution, the effective contribution of the BNDES and its relevance to Brazilian development must and should be monitored and evaluated.

If it is indeed an adaptable and learning institution, as history has demonstrated, much can be gained from internal and external evaluation carried out from different angles. But one pre-requisite is absolutely necessary: evaluation, assessments and opinions must be based on technically sound analysis. The BNDES needs them, the country needs them. Any discussion of the challenges of Brazilian development and the role to be played by the BNDES must be placed in a proper framework: less opinion-based, less ideologically biased. For the good of Brazil.

(3)

# Reinventing State Capitalism

## Leviathan in Business, Brazil and Beyond

### [Aldo Musacchio](http://www.hup.harvard.edu/results-list.php?author=17193)

### [Sergio G. Lazzarini](http://www.hup.harvard.edu/results-list.php?author=17194)

368 pages

The wave of liberalization that swept world markets in the 1980s and 90s altered the ways that governments manage their economies. *Reinventing State Capitalism* analyzes the rise of new species of state capitalism in which governments interact with private investors either as majority or minority shareholders in publicly-traded corporations or as financial backers of purely private firms (the so-called “national champions”). Focusing on a detailed quantitative assessment of Brazil’s economic performance from 1976 to 2009, **Aldo Musacchio** and **Sergio Lazzarini** examine how these models of state capitalism influence corporate investment and performance.

According to one model, the state acts as a majority investor, granting the state-owned enterprise (SOE) financial autonomy and allowing professional management. This form, the authors argue, has reduced many agency problems commonly faced by state ownership. According to another hybrid model, the state uses sovereign wealth funds, holding companies, and development banks to acquire a small share of equity ownership in a corporation, thereby potentially alleviating capital constraints and leveraging latent capabilities.

Both models have benefits and costs. Yet neither model has entirely eliminated the temptation of governments to intervene in the operation of natural resource industries and other large strategic enterprises. Nevertheless, the longstanding debate over whether private ownership is superior or inferior to state capitalism has become irrelevant, Musacchio and Lazzarini conclude. Private ownership is now mingled with state capital on a global scale.

(4)

# Leviathan as a Minority Shareholder: Firm-Level Implications of Equity Purchases by the State

1. [Carlos Inoue](http://amj.aom.org/search?author1=Carlos+Inoue&sortspec=date&submit=Submit),
2. [Sergio Lazzarini](http://amj.aom.org/search?author1=Sergio+Lazzarini&sortspec=date&submit=Submit)[⇓](http://amj.aom.org/content/early/2013/03/05/amj.2012.0406.abstract#corresp-1) and
3. [Aldo Musacchio](http://amj.aom.org/search?author1=Aldo+Musacchio&sortspec=date&submit=Submit)

[+](http://amj.aom.org/content/early/2013/03/05/amj.2012.0406.abstract) Author Affiliations

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## Abstract

In many countries, firms face institutional voids that raise the costs of doing business and thwart entrepreneurial activity. We examine a particular mechanism to address those voids: minority state ownership. Due to their minority nature, such stakes are less affected by the agency distortions commonly found in full-fledged state-owned firms. Using panel data from publicly traded firms in Brazil, where the government holds minority stakes through its development bank (BNDES), we find a positive effect of those stakes on firms' return on assets and on the capital expenditures of financially constrained firms with investment opportunities. However, these positive effects are substantially reduced when minority stakes are allocated to business group affiliates and as local institutions develop. Therefore, we shed light on the firm-level implications of minority state ownership, a topic that has received scant attention in the strategy literature.

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* Revision received February 22, 2013.
* Accepted March 2, 2013.

(5)

<http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1969843>