Journal Essays on Economic Policy (ESPE) - National Development Banks in Colombia

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In Colombia, the National Development Banks (NDBs) are organized as a system of four (initially five) specialized institutions. This system was adopted during the market reforms of the early 1990s, which eliminated the development functions of the central bank, liberalized the financial sector and privatized public banks, with the exception of Banco Agrario, but maintained the development bank system. The participation in terms of economic size of two of these entities, Findeter and Finagro, has increased or remained constant, while that of the other two, Bancóldex (including IFI, which it absorbed) and FDN (formerly FEN), has decreased. However, FDN is in a dynamic growth process after its recent restructuring.

This essay explores five areas of action in which NDBs should act to overcome market failures, including countercyclical financing, infrastructure development (long-term financing), financial inclusion, promotion of innovation and structural change, and green finance.

With regard to countercyclical financing, this function has been performed to a very limited extent. The portafolio of NDBs has tended to grow more moderately during credit booms, but has not increased significantly during crises.

With regard to the second function, the most important development has been the restructuring of FDN with a strategic focus on infrastructure development. The FDN aims to be a catalyst for investment and a source of financing for infrastructure projects developed as public-private partnerships, in particular the 4G fourth generation road concession program. However, it faces significant challenges in mobilizing resources from other investors and banks. It should broaden its focus, as it has begun to do, to include renewable energy projects or infrastructure and urban renewal, while avoiding competition with Findeter.

For its part, Findeter, the bank specializing in the promotion of urban and regional infrastructure, has been the most active since the turn of the century. It has played a fundamental role in the implementation of public programs with a strong regional component in social services, transportation, housing, and water and sanitation.

Two banks, Bancóldex and Finagro, are active in financial inclusion. As for the former, more than half of its disbursements in 2017 went to MSMEs;it also manages the country's financial inclusion program, Banca de las Oportunidades. The latter allocates a large share of its rediscount loans to medium and large agricultural producers. One of its challenges is how to prevent rediscount loans from depleting the Agricultural Development Bonds (TDA), which are intended for small producers. To this end, it would be advisable to adopt the proposal of the Mission for the Transformation of Rural Areas to earmark targeted credit exclusively for two objectives: promoting financial inclusion and encouraging investment in rural areas for all types of producers.

Among Bancóldex's traditional activities is the promotion of innovation and structural change, but these activities have not received the necessary attention. One of the government's main instruments in this area is the iNNpulsa program, which was managed by Bancóldex until last year, when was transferred to its trust company. With the exception of financial inclusion, it is necessary that the functions of this entitybe clearly defined, with a strong emphasis on promoting innovation, and not change depending on who is in charge.

In terms of green finance, all NDBs have been integrated into the green growth policies promoted by the national government. To avoid conflicts in this area, greater coordination between them is needed so that the projects they support are complementary. Although the leveraging of these investments is new, Bancóldex and Findeter have already done important work in terms of financial and non-financial support and leadership, assumed within the framework of the Green Protocol. Finagro should be much more active in this area, especially with regard to good land use and reforestation.

Currently, the role of NDBs enjoys the greatest support since the early 1990s market reforms. Consequently, the national government should maintain this system and allow the banks to continue to operate with clear policies defined under its guidance. However, it is crucial that they operate as a system and therefore interact and coordinate their activities, especially in areas where the mandates of two or more banks overlap. At present, there is no institutional coordination mechanism, which should therefore be established.

These banks should also actively exchange experience on financing issues, in particular to ensure that financing schemes are cost effective and consistent with a more competitive financial sector. Equally or more important is mutual support in the development of new instruments, in particular the promotion of private equity and debt funds as well as investment guarantee schemes. It is also crucial to increase the size of the system, at least to the level of the early 1990s, and that NDBs play a more active countercyclical role when needed. In terms of prudential supervision, although current practice should be maintained, it would be advisable to develop more specific rules for rediscount operations, as they face very different risks from those of first-tier financing.

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