Key findings

Long-Term Finance Provision: National Development Banks VS. Commercial Banks.

World Development, 158.

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Finance in Common

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Despite its practical significance in promoting long-term economic growth, long-term finance is often in short supply, especially in developing countries. Governments in both developed and developing countries have established national development banks (NDBs) to provide much-needed long-term loans.
We have built the first database on NDBs worldwide to systematically examine whether NDBs lend longer than commercial banks in deciding the maturity of their loans.
We find that long-term loans constitute a larger proportion of the total loan portfolio in NDBs than that in commercial banks in general and privately owned commercial banks in particular.
This result is statistically significant after controlling for country- and bank-level factors. Our study contributes to the literature on loan maturity because we are the first to use a comprehensive panel data to systematically examine whether NDBs—an understudied but important financial intermediary—play a maturity-lengthening role in filling the financing gap.

Objectives and research questions

In the wake of the recent global financial crisis that erupted in 2008, reversing the prolonged decline in the supply of long-term funding tops the agenda of policy makers worldwide. One key way for governments to overcome the scarcity of long-term finance is to establish development banks with the official mission of providing long-term capital to fill the market gaps. However, little systematic research has been conducted to examine whether NDBs have provided that much-needed long-term finance. Anecdotal evidence has suggested mixed findings. Our paper is the first empirical paper that examines whether NDBs on average lend longer than commercial banks.

Methods

We econometrically examine whether the proportion of long-term loans in the total loan portfolio of NDBs is on average larger than that in commercial banks. Matching our list of NDBs with bank-level data from BankFocus, we can build a large international data set for 1,253 banks, of which 58 are NDBs, 112 are state-owned commercial banks (SCBs), 695 are privately owned domestic commercial banks (PCBs), and 388 are foreign commercial banks (FCBs) from 106 countries during the 2011–2018 period. We use the panel analysis to examine the relationship between bank type and loan maturity after controlling for bank-level and country-level factors.

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Results

We find that long-term loans constitute a larger proportion of the total loan portfolio in NDBs than that in commercial banks. The proportion of long-term loans (longer than 5 years) by NDBs is on average larger by 4.9 percentage points than those by commercial banks. The proportion of short-term loans provided by NDBs is on average smaller by 16 percentage points than that provided by commercial banks. In summary, NDBs, on average, are more likely to lend longer than commercial banks in their choices of loan maturity.

Recommendations

First, policy makers should not dismiss the role of NDBs in providing long-term finance simply based on anecdotal evidence. Although it is true that not all NDBs have been successful and some NDBs have failed miserably in the past, this does not mean that NDBs cannot play a maturity-lengthening role. There are sound theoretical rationales behind the belief that NDBs are well positioned to provide long-term finance to fill the financing gap. Relying on a comprehensive panel data set of NDBs worldwide, our empirical analysis demonstrates that NDBs on average lend longer than commercial banks. Given the fact that NDBs are prevalent worldwide, we should shift the policy debate from whether governments should establish NDBs to how to make NDBs work better.

Second, NDBs need to focus on long-term finance to fill the financing gap and avoid unfair competition with commercial banks. NDBs are initiated and steered by governments to fulfill public policy objectives; accordingly, NDBs often enjoy government support, such as sovereign guarantee, preferential tax treatment, and concessional borrowing. NDBs should not provide short-term loans to firms that could have access to credits from commercial banks. Otherwise, NDBs would create distortions in credit markets and crowd out commercial banks. Recently, there has been a worrying trend that a few NDBs decide to take household deposits because they lack alternative funding sources. Because taking household deposits may create the maturity mismatch problem, it would undercut the comparative advantage of NDBs in providing long-term finance.

Access the paper
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