UNITED NATIONS

ECLAC

FOR PARTICIPANTS ONLY
REFERENCE DOCUMENT

LC/PLEN.36/DDR/1
21 November 2021

ENGLISH
ORIGINAL: SPANISH

21-00848

COMMITTEE OF THE WHOLE
Thirty-sixth session

New York, 3 December 2021

DEVELOPMENT BANKS' RESPONSE TO COVID-19 AND THEIR ROLE IN A SUSTAINABLE RECOVERY[*]

[*] This document is a translation of a Spanish original which did not undergo formal editing.

1. Introduction

Strengthening the lending and response capacity of multilateral, regional, subregional and national development banks and regional cooperation and coordination among them is one of the central pillars of the response to the challenges of financing for development posed by the coronavirus disease (COVID-19) pandemic.

The short-, medium- and long-term effects of COVID-19 have underscored the need to address the problem of financing for development in middle-income countries such as those in Latin America and the Caribbean —a region characterized by the increasing decoupling of per capita income and the ability to mobilize domestic and external resources—, and the trend in multilateral cooperation increasingly oriented towards lower-income countries.

The countries of Latin America and the Caribbean require multilateral and, above all, regional cooperation in order to foster a sustainable recovery and advance their economic and social development. This will address the region's medium- and long-term challenges, including declines in productivity and investment, which are key to reconfigure the development model towards productive transformation with sustainability and equality.

Regional, subregional and national development banks have played a central role in the countercyclical response to the economic and social effects of the pandemic. In 2020, Latin America faced the worst crisis on historical record and the sharpest economic contraction in the developing world (GDP declined by 6.8%).

The financial effort of regional, subregional and national development banks exceeded that of multilateral banks. The response of these institutions was not only directed towards the government sector but also, especially in the case of national banks, towards the productive sector and in particular towards safeguarding the productive and job-creating capacity of micro-, small and medium-sized enterprises (MSMEs). This was achieved in part through instruments such as loans and also in some cases by expanding the use of guarantee systems with a number of advantages in terms of low costs and liquidity relative to more traditional instruments.

The role of development banks is also central to achieving a sustainable recovery in the long term. The pandemic has deepened the gaps and structural problems in Latin America and the Caribbean, which, together with a low base of comparison with 2020, partly explains why the rebound in growth expected in the region in 2021 (5.9%) is likely to be temporary.

Reversing the downward trend in the regional GDP growth rate and in gross fixed capital formation since 2014, which the pandemic has worsened, will require expanding the capacity to mobilize and channel resources for public and private projects in strategic productive sectors and in areas that foster economic complementarity. One of the central challenges for development banks is exploring the various existing mechanisms such as increased capitalization and flexible lending criteria to develop their potential to mobilize resources for productive development.

At the same time, higher levels of investment must be accompanied by a change in the composition of investment in order to address one of the greatest challenges facing the region in terms of its economic and sustainable development: climate change. This in turn requires a change in the composition of the loan portfolio and a significant percentage of this portfolio being channelled towards green investments and climate change-related projects.

In order to implement a coherent strategy for green financing in the development banking system, coordination and cooperation mechanisms between multilateral, regional, subregional and national development banks must be strengthened. In particular, subregional and national banks must have the support of multilateral banks to access low-cost financing, long-term capital and the technical capacity to access funds and design projects for progressive and environmentally sustainable structural change.

2. Stylized facts about development banks in the region

Financing for development in Latin America and the Caribbean is channelled through multilateral banks (World Bank), regional banks (Inter-American Development Bank (IDB)), subregional banks (Development Bank of Latin America (CAF), Central American Bank for Economic Integration (CABEI), Caribbean Development Bank (CDB) and FONPLATA Development Bank) and more than 100 development finance institutions operating at the national level.

An analysis of these institutions shows that there is no predetermined development bank model. Rather, different models coexist, which creates significant potential for cooperation and coordination among development banks.

The size, financial and institutional profile, and regional coverage of these institutions is heterogeneous. An analysis of selected balance sheet indicators, including capital, net worth, assets, liabilities and loan portfolio shows that they vary substantially across institutions. The same applies to the other balance sheet components, including the loan portfolio volume and the capital-to-loans ratio. This applies to multilateral, regional and subregional banks as well as to national banks.

By way of example, a comparison between multilateral, regional and subregional banks shows that the World Bank accounts for the largest volume of assets, followed by IDB, CAF, CABEI and CDB. IDB is the largest lender in Latin America and the Caribbean. The greater diversification of the World Bank and IDB implies that these two development banks have greater leverage capacity relative to CAF, CABEI and CDB. The leverage of the World Bank and IDB is estimated at 5 and 3, respectively, while and that of CAF and CABEI is 2. In terms of regional coverage, the World Bank, IDB and CAF target Latin America and the Caribbean as a whole. The activities of CABEI are focused on Central America, while those of CDB are oriented to the Caribbean. Geographic diversification is one of the determinants of institutions' credit ratings. Thus the World Bank and IDB have a triple A credit rating.

A significant difference between the World Bank, IDB, CAF and CABEI is the composition of shareholders. Voting power in the World Bank is essentially dictated by the non-borrowing countries (e.g. the United States). In the case of IDB, the borrowing countries control approximately half of the voting power, while for CAF and CABEI, they account for the majority of the voting power. This largely determines the volume and orientation of the loans, as well as their capitalization.[1]

[1] See Fleiss (2021).

Table 1
Multilateral, regional and subregional development banks in Latin America and the Caribbean: selected financial indicators 2019–2020
(Billions of dollars, leverage and credit rating)

	World Bank	Inter-American Development Bank (IDB)	Development Bank of Latin America (CAF)	Central American Bank for Economic Integration (CABEI)
Committed financing (billions of dollars)	9 723	12 961	13 010	2 638
Disbursements (billions of dollars)	6 265	10 574	10 043	1 934
Total assets (billions of dollars)	496 276	140 248	42 294	11 611
Equity (billions of dollars)	208 558	35 703	12 797	3 443
Paid-up capital (billions of dollars)	259 377	13 684	9 370	1 102
Callable capital (billions of dollars)	269 968	164 901	1 590	3 662
Leverage	5	3	2	2
Credit rating	AAA	AAA	A+	AA

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of P. Fleiss, "Multilateral development banks in Latin America: recent trends, the response to the pandemic, and the forthcoming role", *Studies and Perspectives series-ECLAC Office in Washington, D.C.*, No. 21 (LC/TS.2021/62-LC/WAS/TS.2021/2), Santiago, ECLAC, 2021.
Note: Data for the World Bank include the International Bank for Reconstruction and Development (IRBD) and the International Development Association (IDA).

National financial institutions also differ significantly in terms of their financial structure, mandates and institutional framework. The group of development finance institutions includes the National Bank for Economic and Social Development of Brazil, whose assets (US$ 181 billion) exceed those of IDB, CAF, CABEI and CDB, along with smaller institutions such as the National Popular Housing Fund (FONAVIPO) in El Salvador (US$ 66 million in assets) and the Saint Lucia Development Bank (with assets equivalent to US$ 36 million).

Similarly, some of these banks have mandates for specific economic sectors and regions, while others operate in a wider range of sectors and at the national level. A sample of 63 national financial institutions in Latin America and the Caribbean reflects mandates to serve MSMEs (33%), the agricultural sector (12%), the housing sector (10%), export development (6%) and local development. The remaining 36% have a broader mandate. Evidence also shows that 19 of these institutions (28%) operate only at the regional level.

Notwithstanding their differences and heterogeneity, the functions of development banks can be classified under three broad objectives. The first is to mobilize and channel public and private savings for public and private projects in the economic, social and environmental areas identified in the strategic vision.

This objective corresponds to the more traditional mandate of development banks to provide financing for productive investment in strategic productive sectors and in areas that promote economic complementarity. This includes the role of identifying, evaluating, promoting and financing investment projects.

This objective also highlights the fact that a modern development institution works with the public and private sectors in terms of resource mobilization and also in terms of projects. In some emerging market economies, development banks have become one of the providers (if not the main one) of long-term credit in agriculture, housing and infrastructure.

The second objective is to contribute to the development of the financial sector and capital markets. This represents a key area of indirect support for private sector development. It complements the first objective, in which the development of the financial sector and capital markets greatly facilitates the mobilization of savings. It can also be seen as a complement to government efforts to promote sound financial sector institutions and policies. Finally, strengthening domestic financial intermediaries is crucial to efforts to alleviate financial constraints and to promote the financial inclusion of households and businesses.

For obvious reasons, this objective may depend on a variety of variables and factors, including good macroeconomic performance and credible government institutions, regulations and laws. With respect to laws, a sound financial regulatory and supervisory framework is key to ensure that financial sector activities are geared towards social and economic development.

These objectives are reflected in greater sectoral diversification of the subregional bank loan portfolio, with emphasis on productive infrastructure (29%, 28% and 30% for CABEI, CAF and CDB, respectively), energy (28%, 23% and 15% for CABEI, CAF and CDB, respectively) and financial development (5%, 12.8% and 15% for CABEI, CAF and CDB, respectively.

The third objective is to provide financing for small and medium-sized enterprises (SMEs). It reflects the importance of the SME sector, which in Latin America and the Caribbean accounts for 20% of GDP and more than 40% of private sector employment, and represents more than 90% of all businesses. This sector accounts for 13% of the total CDB portfolio.

To fulfil their functions in addition to lending, development banks also offer a variety of financial and non-financial products. The financial products include loan guarantees, leasing and factoring services, microcredit, seed capital and financial support for entrepreneurship, education, health and insurance services. The non-financial products include advisory services, capacity-building and training programmes.

Following the current trend of development banks, these function as first- and second-tier banks. First-tier banks mainly lend to small and medium-sized enterprises, while second-tier banks help to meet the objective of mobilizing long-term savings for investment and to develop the financial sector and capital markets.

3. COVID-19 has strengthened the role of regional, subregional and national development banks in financing Latin America and the Caribbean

The response of multilateral, regional, subregional and national development banks to the economic and social impact of COVID-19 was countercyclical. In total, between January 2020 and February 2021, these development banks together allocated US$ 150.4 billion in financial resources for Latin America and the Caribbean to address the effects of the pandemic.

However, their response has been heterogeneous. Multilateral development banks have responded less forcefully to the impact of COVID-19 than in other systemic crises. During the global financial crisis (2008–2009), the World Bank's financing commitments to developing economies increased by US$ 28.1 billion. In comparison, during the COVID-19 crisis, these commitments were roughly 40% lower, at US$17.3 billion. Between 2009 and 2010, gross disbursements from the World Bank (US$ 80 billion) exceeded those of the International Monetary Fund (IMF) (US$ 67 billion) and other international financial institutions (US$ 56.4 billion).[2]

Moreover, most of the committed funding went to regions with the highest proportion of low- and lower-middle-income countries, such as Africa and South Asia. These two regions accounted for 56% and 57% of the financing committed by the World Bank in 2020 and 2021, respectively. This contrasts with the regional composition of funding committed in 2009, which benefited regions composed mostly of middle-income countries. That year, Latin America and the Caribbean received 29%, of the financing committed and disbursed by the World Bank, which represents roughly double the amount of financial support received in 2020 and 2021 (see table 2).

Table 2
Developing regions: World Bank financing commitments
(Billions of dollars and share of total in percentages 2017–2021)

	Billions of dollars					Share of total				
	2017	2018	2019	2020	2021	2017	2018	2019	2020	2021
Africa	11 842	16 531	15 007	20 820	27 069	28	35	33	36	41
East Asia and the Pacific	7 107	4 612	5 302	7 270	7 868	17	10	12	12	12
Europe and Central Asia	5 308	4 507	4 332	7 196	5 874	13	10	10	12	9
Latin America and the Caribbean	5 876	4 326	6 139	7 776	10 233	14	9	14	13	15
Middle East and North Africa	5 880	6 375	5 483	3 622	4 634	14	14	12	6	7
South Asia	6 061	10 661	8 860	11 657	10 873	14	23	20	20	16
Total	42 074	47 012	45 123	58 341	66 551	100	100	100	100	100

Source: World Bank, *The World Bank Annual Report 2021: from Crisis to Green, Resilient, and Inclusive Recovery*, Washington, D.C., 2021.
Note: Years refer to fiscal years (June–July).

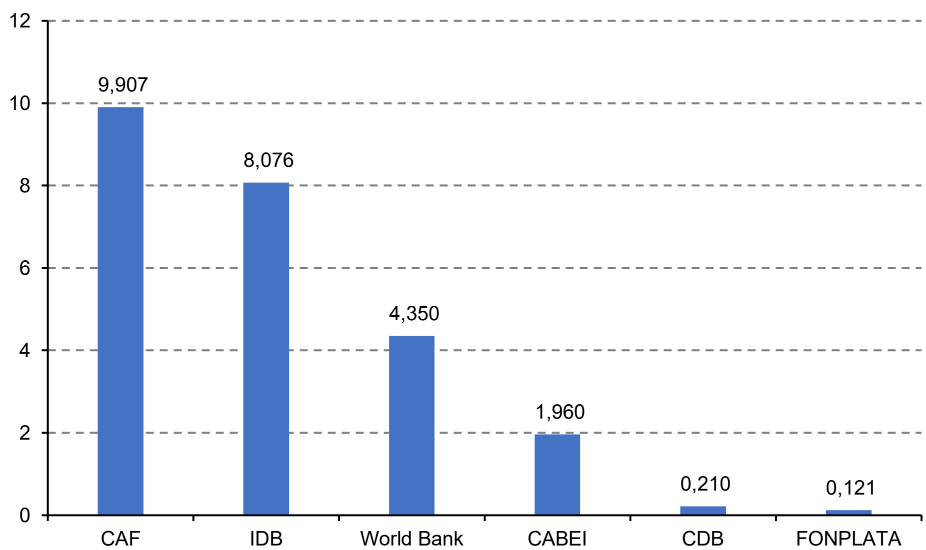
Owing to the prevalence of upper-middle-income countries in Latin America and the Caribbean, most World Bank financing for the region is not concessional. The countries of Latin America and the Caribbean that are eligible for concessional financing include low-income (Haiti), lower-middle-income (El Salvador, Honduras, Nicaragua and the Plurinational State of Bolivia), and upper-middle-income countries that are classified as vulnerable (Dominica, Guyana, Saint Lucia, Saint Vincent and the Grenadines). This is also the case for IDB, whose concessional loans in 2020 went to Guyana, Honduras and Nicaragua.

[2] See Independent Evaluation Group (2011).

Between April 2020 and October 2021, the World Bank disbursed US$ 4.6 billion in financing related to COVID-19, representing just under half of the total committed financing for the region. This focused on minimizing loss of life, strengthening health systems and disease surveillance, mitigating the economic impact of the pandemic, and working with partners and the private sector to address supply chain and delivery issues (World Bank, 2021c).

As multilateral banks have refocused their efforts on regions with a higher proportion of low- and middle-income countries, regional, subregional and national banks have assumed a more prominent role in financing for Latin America and the Caribbean (figure 1).

Figure 1
Latin America and the Caribbean: total amounts assigned by multilateral, regional and subregional banks in relation to COVID-19, January 2020–February 2021
(Billions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information from development banks, press clippings and G. Cipoletta Tomassian and T. Abdo (2021), "Financiamiento de la banca de desarrollo en el marco de la crisis del COVID-19 en América Latina y el Caribe", *Financing for Development series*, No. 272, Santiago, Economic Commission for Latin America and the Caribbean (ECLAC), 2021, forthcoming.

IDB and subregional development banks (CAF, CABEI and CDB) have provided around US$ 8 billion and US$ 12 billion, respectively, in financial support to fight the pandemic. This is equivalent to 0.45% of regional GDP and 1.9% of regional exports of goods and services. These funds were used to finance emergency programmes, including health-related measures, and to provide stand-by lines of credit.

IDB Group's response to the pandemic totalled US$ 8.076 billion, representing 27% of the amount attributable to regional development banks. It focused on funding to meet urgent public health needs, safeguards for vulnerable populations, economic productivity and employment, and fiscal measures to help mitigate economic impacts. The increase in IDB lending to address the effects of COVID-19 in the region actually exceeds that following the 2008–2009 global financial crisis. In 2020, IDB approved 82 loans with sovereign guarantees, with total financing of US$ 12.64 billion. The sovereign guaranteed loan programme included 57 investment projects for US$ 6.38 billion, 19 policy-based loans (PBLs) for US$ 4.96 billion, and 5 special development lending (SDL) projects for US$ 1.23 billion.

In 2020, with a lending portfolio directly targeting the COVID-19 crisis that approached US$ 10 billion (representing 35% of its total lending portfolio in March 2021), CAF became the leading provider of finance to the region, surpassing not only the World Bank, but also the US$ 8 billion in loans provided by IDB. The financial support provided for these purposes by subregional institutions that are relatively smaller than those mentioned above, such as CABEI, CDB and FONPLATA, amounted to US$ 1.96 billion, US$ 210 million and US$ 121 million, respectively (figure 2).

CAF was the main lender to the region, directing most of its efforts towards the government sector, thus alleviating budgetary restrictions with US$ 9.907 billion in lines of credit for the different countries of the region, in addition to non-reimbursable financing of US$ 400,000 for its member countries, thus accounting for 33% of the total extended by regional banks.

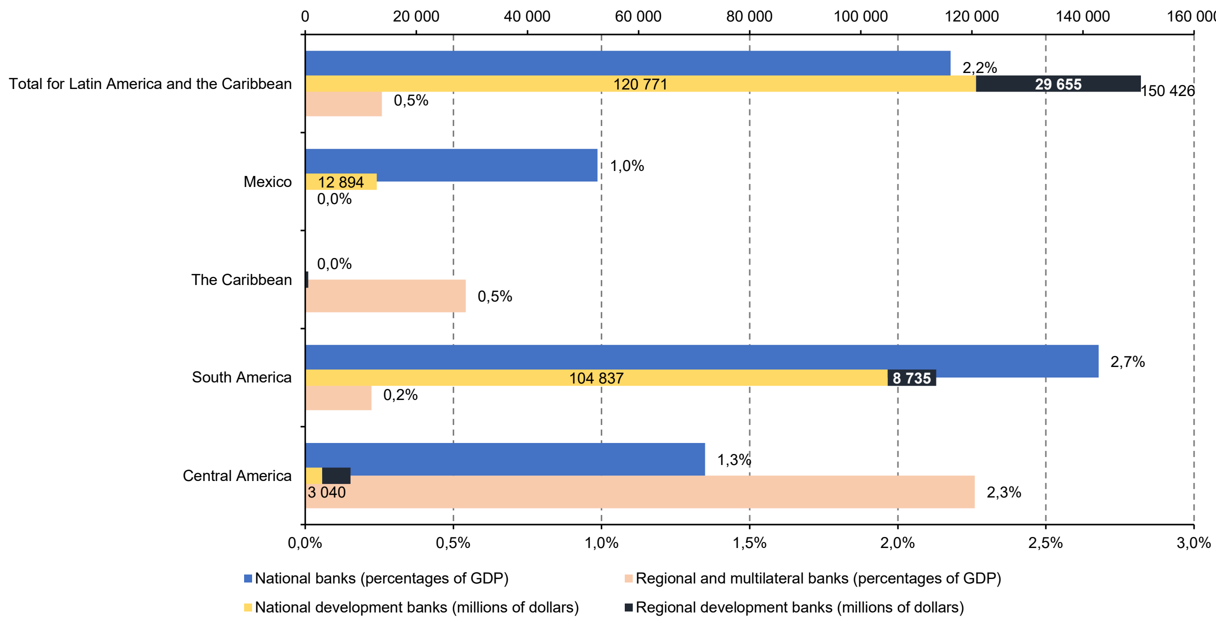
In response to the coronavirus pandemic, CABEI launched the Emergency Support and Preparedness Program for COVID-19 and Economic Reactivation, which aims to contribute to prevention and containment of the health emergency faced by CABEI member countries. The key priorities in the strategy focus on actions to strengthen the regional economy during the downturn caused by the suspension of activities and during the subsequent recovery phase.

The elements of the emergency COVID-19 pandemic support programme were based on:

1. Emergency support with non-reimbursable funds of up to US$ 8 million (resources extended to the countries of the Central American Integration System (SICA)).
2. Purchase and supply of medicines and medical equipment for early detection of COVID-19, with up to US$ 2.1 million available.
3. Financing for public sector operations for up to US$ 600 million (US$ 400 million for SICA countries and US$ 200 million for other countries). Under this initiative, eligible public sector operations would be financed in amounts not exceeding US$ 50 million per country.
4. Credit programme to support the liquidity management of central banks, a line of action for up to US$ 1 billion for founder and non-founder members of CABEI.
5. Support for the financial sector to contribute to the revival of economies through the use of different financial products with an emphasis on supporting MSMEs, for up to US$ 350 million.

At the time of writing of this report, the CABEI response to the pandemic in the region totalled US$ 1.960 billion.

Figure 2
Latin America and the Caribbean:
national development bank financial support by region, January 2020–February 2021
(Millions of dollars and percentages of GDP)



Source: Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information from development banks, press clippings and G. Cipoletta Tomassian and T. Abdo (2021), "Financiamiento de la banca de desarrollo en el marco de la crisis del COVID-19 en América Latina y el Caribe", *Financing for Development series*, No. 272, Santiago, Economic Commission for Latin America and the Caribbean (ECLAC), 2021, forthcoming.
Note: The total amount for Latin America and the Caribbean, in addition to the amounts that reached each individual country from national banks and regional or multilateral banks, also includes US$ 6.266 billion in regional joint packages from multilateral and regional banks (IMF and CAF) and an additional US$ 9.677 billion owing to reported amounts for IDB and CAF being updated in February 2021, without disaggregation by country.

A significant effort to provide financial resources has been made by national development banks, with financial support totalling more than US$ 120 billion (January–November 2020) including loans/credits, guarantees, refinancing, payment suspension and guarantees. This is concentrated among some of the larger economies in the region, including Brazil, Chile, Colombia, Mexico and Peru (US$ 73.4 billion, US$ 4.2 billion, US$ 4.5 billion, US$ 12.9 billion and US$ 21.9 billion, respectively). Nonetheless some smaller economies have also benefited from the financial support of national development banks. In El Salvador and Panama, the financial support provided by national banks represented 6% and 2.8% of GDP, respectively (see figure 2).

4. Development banks: regional and productive specialization

An analysis of multilateral, regional and national development bank financing to address COVID-19 by region shows that multilateral banks were the largest source of financing for the smallest economies in the region (Caribbean), accounting for 85.7% of the total to such economies. Regional and subregional banks provided 14.3%, and domestic banks did not provide financing for this group of economies (table 3).

The economies of South America and Mexico received the largest share of financing from national banks (54.4%). Regional and subregional banks contributed 23.9% and 21.8% of the total. Of the financial support extended by national development entities, 97% corresponds to five countries: Brazil (61%), Peru (18%), Mexico (11%), Colombia (4%) and Chile (3%).

Table 3
Proportion of COVID-19 financial support by multilateral, regional/subregional and national financial institutions, by subregion in Latin America and the Caribbean, 2021
(Percentages)

Region/subregion	Multilateral	Regional/subregional	National	Total
South America	23.9	21.8	54.4	100
Central America	40.5	18.8	40.7	100
The Caribbean	85.7	14.3	0.0	100
Mexico	0.0	0.0	100.0	100

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official COVID-19 information from development banks and press clippings.

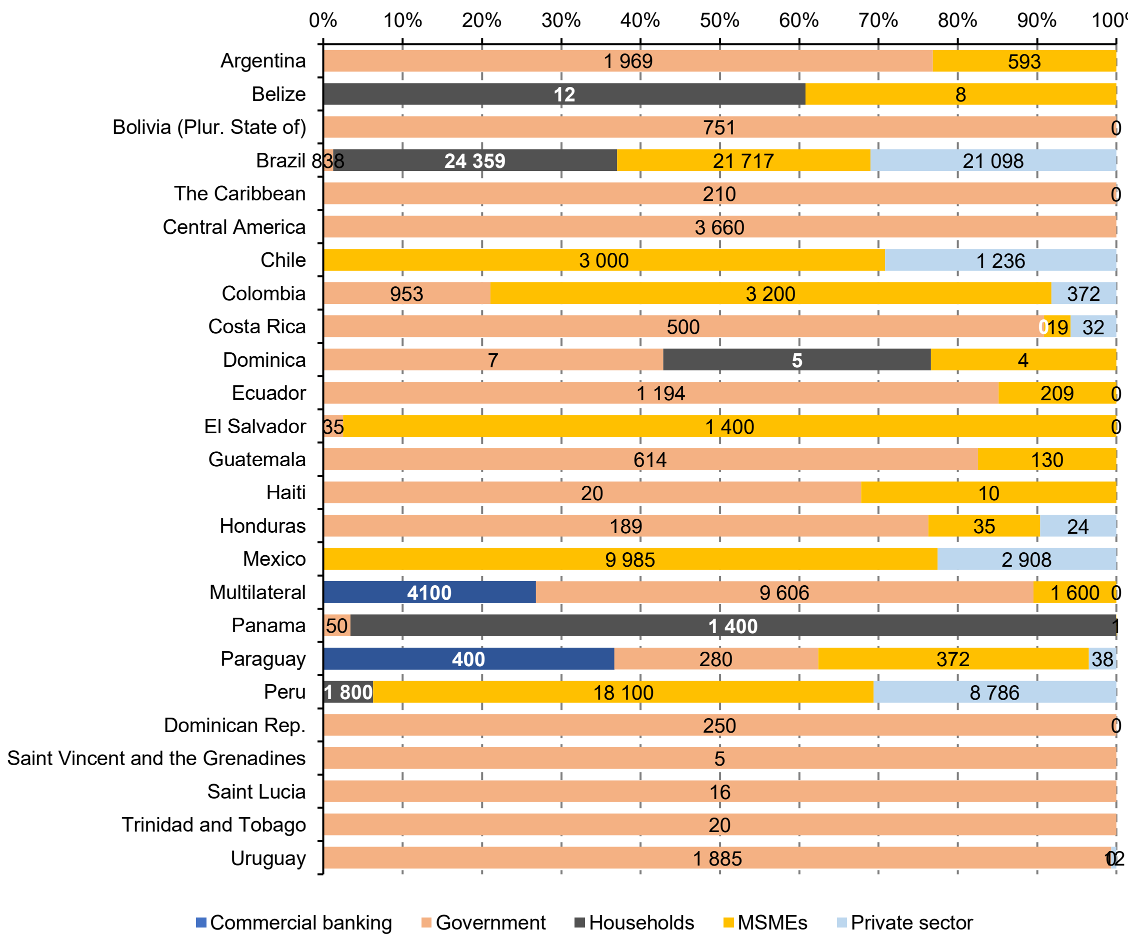
In general, the responses of national and regional development banks in Latin America and the Caribbean to the pandemic crisis focused on economic revival. The sectors of activity receiving the financial support extended by national development banks included most notably primary agriculture and services. Regional banks in Latin America have focused on helping to maintain countries' fiscal balances, allocating most of their funds directly to the government sector (the main recipient), with an emphasis on health.

The countries in which the funds were mostly directed towards government are those in which regional banks accounted for the majority of funds. This is the case in several Caribbean and Central American countries. Uruguay is a special case, as the funds from the national bank also alleviated the public sector.

In Colombia and Chile, development bank funds were primarily earmarked for MSMEs. In Brazil, funds were allocated almost equally, although with a greater share going to households, followed by the private sector and MSMEs, with the government sector receiving the smallest share. The Mexican national banking system focused its efforts solely on the private sector, and 77% of funds were exclusively for MSMEs. The only country where the national development bank offered direct financial support to commercial banks was Paraguay (US$ 400 million). The remaining 91% of contributions to commercial banks were made by regional banks.

In Central America, US$ 1.96 billion was allocated to governments through cooperation from the subregional banking system (CABEI). Of the total of US$ 8.133 billion disbursed by all development banks (national, subregional and regional) to the subregion, 62% was to the government sector, 20% to MSMEs and 17% to households.

Figure 3
Latin America and the Caribbean (selected countries and groupings): national, regional or multilateral development bank COVID-19 financial support provided by sector and country
(Percentages)



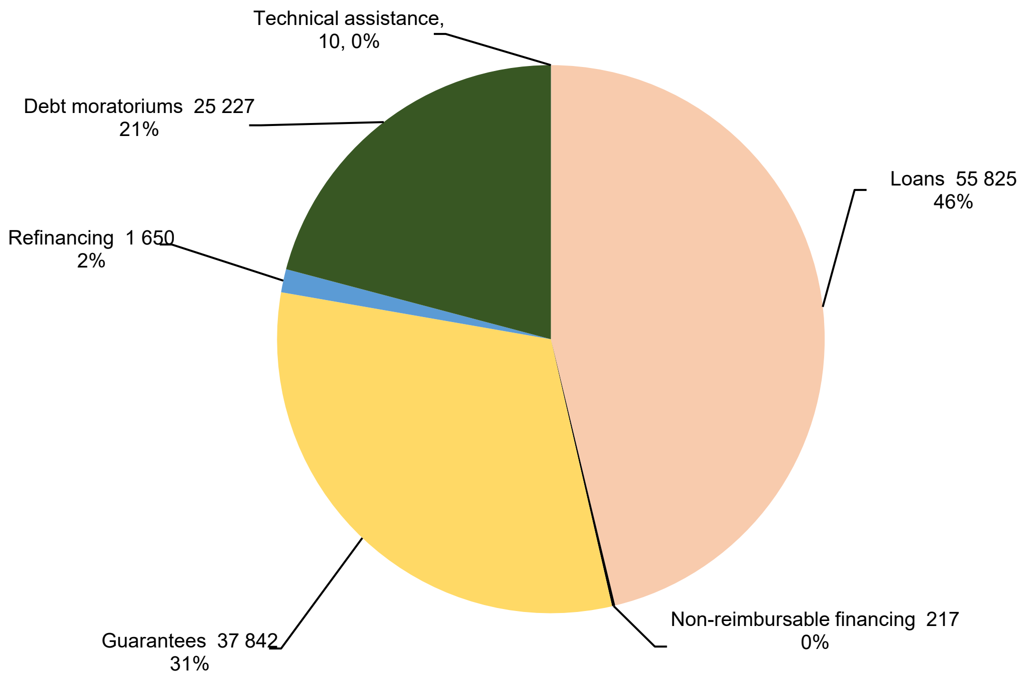
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information from development banks, press clippings and G. Cipoletta Tomassian and T. Abdo (2021), "Financiamiento de la banca de desarrollo en el marco de la crisis del COVID-19 en América Latina y el Caribe", *Financing for Development series*, No. 272, Santiago, Economic Commission for Latin America and the Caribbean (ECLAC), 2021, forthcoming.

During the crisis caused by the COVID-19 pandemic, national development banks' priorities have included reviving the economic sector, with emphasis on keeping the private productive sector (the main recipient) active, in different sectors of activity. The countries where funds mainly went to the government are those where regional banks accounted for the majority of funds. This is the case in several Caribbean and Central American countries. Regional banks tend to need an intermediary between themselves and the population.

5. Financial instruments to respond to the pandemic

Guarantee systems have become a very important to support MSMEs during the pandemic (see figure 4) and have been one of most used instruments by development financial institutions to support the productive sector in countering the effects of the pandemic. National development banks have provided liquidity support through various instruments. Of the amounts disbursed, 46% was for credit, 2% for refinancing plans, 21% for debt moratoriums and 31% for guarantees to enable producers to obtain new loans that allowed them to continue operating, the latter being the instrument to reactivate lending to SMEs that experienced the highest rate of growth.

Figure 4
Latin America: financial support provided by national development banks to address the effects of COVID-19, by type of instrument, 2020
(Millions of dollars and percentages of the total)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information from development banks, press clippings and G. Cipoletta Tomassian and T. Abdo (2021), "Financiamiento de la banca de desarrollo en el marco de la crisis del COVID-19 en América Latina y el Caribe", *Financing for Development series*, No. 272, Santiago, Economic Commission for Latin America and the Caribbean (ECLAC), 2021, forthcoming.

Many companies, especially MSMEs, have faced unprecedented liquidity constraints during the pandemic. Given their advantages, and despite their financial risks, guarantee systems have emerged as a potentially effective policy tool to address the liquidity gap that MSMEs are facing. This instrument is attractive for its speed (when it is already in place), and its low budgetary costs, especially compared to other tools such as loans and grants.

Credit guarantee systems have three important benefits. The first is the increase in the supply of credit from the financial system. With the support of the guarantees, financial institutions can expand their supply of credit for companies that are in suboptimal financing situations, because they are not able to offer sufficient guarantees but do have the capacity to administer a higher level of principal .

The second benefit is that with a guarantee system more companies can access the formal financial system. With the support of a guarantee instrument, companies that are not able to offer sufficient guarantees of their own accord, start-ups, new companies and firms with little experience in covering their borrowing needs would have access to financing.

The third benefit is the improvement in credit conditions. The interest rates, amounts and terms of loans can improve owing to the mitigation of risks provided by a guarantee mechanism.

Guarantees are mainly aimed at MSMEs. These enterprises are a priority because of their vulnerability to the impact of the pandemic and their effect on employment. However, in some cases (Chile, Colombia, Costa Rica, and Uruguay), guarantees have also benefited large companies.

Another important instrument that has been used by development banks to address the challenges of the pandemic is the loan. The 130 loans recorded in the database for which the amounts were given are estimated to total US$ 85.428 million. Loans are the most widely used development banking instrument globally (Griffith-Jones and others, 2020). The COVID-19 pandemic in Latin America and the Caribbean was no exception, as loan transactions accounted for 46% of the total financial support provided. While non-reimbursable financing was directed mainly to governments, loans primarily went to the private sector.

MSMEs received most of the loans, for a total of US$ 32.475 million, spread over 45 different transactions. The rest of the private sector received US$ 23.341 million, through 30 transactions. In terms of the supply of working capital, loans and grants are often subject to certain conditions, such as maintaining stable levels of employment and wages (Griffith-Jones and others, 2020), including during the pandemic crisis. Governments received US$ 22.108 billion through 49 lines of credit, in addition to a US$ 731 million debt moratorium from Brazil’s National Bank for Economic and Social Development (BNDES).

6. Development banks and economic recovery

After experiencing the worst contraction in its history due to COVID-19 (6.8%), Latin America and the Caribbean will see an uptick in economic growth in 2021 (5.9%), but this is unlikely to last. This growth is explained by the low basis of comparison relative to 2020 and is driven by consumption within a context of exacerbated structural problems. It will provide only temporary respite from the current economic situation and prove insufficient to reduce the region’s financing gap or improve its debt profile.

Tackling the region’s current challenges will require a major mobilization of resources and a resource-allocation logic based on financing for environmentally, socially and economically sustainable development. Economic criteria alone cannot suffice: environmental, social and corporate governance criteria must be integral elements of the guiding principles of productive financing.

Development banks can provide financing for sectors that generate significant social benefits and for those with risk-return profiles capable of attracting private capital and channelling it towards development objectives.

Regional, subregional and national development banks, in particular, can play a key role in spearheading investment recovery efforts by prioritizing medium- and long-run development objectives. One of the most important components for boosting growth with a strategic approach is green investment and climate-change-related projects.[3]

Increased financing in these areas should be accompanied by changes in the composition of lending portfolios. Regional and subregional development banks have taken a step in this direction. IDB has set a target of allocating 30% of its portfolio to climate investment, while CABEI and CAF have set targets of 35% and 30% of their total portfolios, respectively. Furthermore, CAF projects that it will devote 40% of its portfolio to climate investments by 2040 and 50% by 2050. In the case of national development banks, climate investment accounts for a much smaller share of the total loan portfolio. According to a 2017 IDB study, it averaged 1% in domestic banks in Brazil, Mexico and Chile.[4]

To boost investment and contribute to a transformative recovery, development banks can also explore alternative financing mechanisms such as social and sustainable bonds. This type of financial instrument has grown exponentially since 2012, with global issuances up from US$ 11.6 in 2013 to US$ 852 billion in 2021. In 2020, 63.6% of the social and sustainable bonds issued globally were aligned with the Sustainable Development Goals.

In the third quarter of 2021, sustainable bond issuances in Latin America and the Caribbean stood at US$ 15.5 billion, accounting for 7.8% of the global total (table 4).

Table 4
Sustainable bond issues for selected regions, third quarter 2021
(Millions of dollars and percentage of total)

Region	Millions of dollars	Percentage
Africa	883	0.4
Asia	29 169	14.7
Latin America and the Caribbean	15 513	7.8
Europe	103 504	52.2
Middle East	1 600	0.8
North America	42 478	21.4
Oceania	5 205	2.6
Total	193 147	100

Source: Environmental Finance, Environmental and Finance Bond Database [online] www.bonddata.org [accessed in 2021].

3 ECLAC has identified eight drivers of a new development model that can improve competitiveness and employment, lower the carbon footprint and reduce socioeconomic and gender inequalities. Four of these (sustainable tourism, the bioeconomy and ecosystem services, sustainable mobility in urban areas and the transition to renewable energies) are related to green investment and climate change.

4 See Abramskiehn and others (2017).

7. Future challenges

To mobilize more resources for investment in strategic areas, the lending capacity of development banks must be expanded and there must be greater coordination among development banks. Although there are spaces for dialogue, the region lacks coordination mechanisms between national development banks across countries and between national, subregional and regional development banks. Coordination and interlinkages are central to enhancing the development of production-oriented financing by these institutions and also green financing.

7.1 Lending capacity and capitalization

The lending capacity of development banks can be increased through two different means: increased capitalization and greater flexibility in their lending criteria. CABEI increased its authorized capital by 40% (US$ 2 billion) in April 2020, and IDB is considering the possibility of a capital increase that would enable annual lending to reach nearly US$ 20 billion (Martin, 2021).

In the case of IDB and the World Bank, the available capital could also be used more effectively by reducing the ratio of equity to loans to a level commensurate with that of commercial banks. Multilateral development banks take a conservative approach to capital adequacy: the major banks of this kind have an equity-to-loan ratio between about 20% and 60%, surpassing that of most commercial banks (10%–15%) (Humphrey, 2020).[5] In other words, multilateral development banks have US$ 2 – US$ 6 in equity for every US$ 10 in outstanding loans, whereas commercial banks have only US$ 1 –US$ 1.50 in equity per US$ 10 in outstanding loans. The equity-to-loan ratios of the World Bank and IDB stand at 22.6% and 38.2%, respectively.[6]

A recent study focused on the World Bank, the Asian Development Bank, IDB and the African Development Bank shows that by adopting more flexible criteria for lending and increasing their leverage, these banks could jointly triple their lending capacity from US$ 415 billion to US$ 1.3 trillion. According to the findings, the increase in leverage and risk would have a minimal effect on these multilateral development banks' credit ratings. In July 2021, the G20 drafted the terms of reference for an independent review of the capital adequacy frameworks of multilateral development banks.[7]

7.2 Coordination among development banks

Mobilization of more resources to bolster investment in strategic areas requires greater coordination among development banks. Not all development banks have the same lending capacity and access to the same financing conditions.

Constraints affect some institutions, particularly domestic banks. This includes the main barrier, access to low-cost long-term capital. A major related challenge is being able to lend to entities that do not

---

[5] Equity consists of paid in capital and accumulated reserves. Loans include loans, guarantees, and capital investments for development purposes.

[6] Capital includes paid in capital and accumulated reserves. Loans include loans, guarantees, and capital investments for development purposes.

[7] See Settimo (2019), Maasdorp (2021) and G-20 (2021).

have a clear guarantee from their government. This problem is especially significant when it comes to financing projects for highly indebted municipal entities and local governments. Another constraint is the difficulty of financing and obtaining imported equipment suited to specific needs.

Lastly, there are considerable technical capacity constraints, including a lack of capacity to identify and rank relevant green projects, difficulty in assessing the financial and technological risks of climate projects, and a lack of knowledge and experience in climate finance and innovative products.

These constraints and possible solutions are summarized in table 5, which presents the results of a 2019 ECLAC survey of national development banks, identifying the difficulties they face in mobilizing more resources and prioritizing sustainable development.[8]

Table 5
Summary of results of an ECLAC survey of the challenges faced by national development banks in efforts to promote sustainable development financing, 2019

Constraints	Solutions
Financing with unfavourable credit conditions	Establish funds and place them with appropriate credit terms
Limited maturity of formulation of projects that are potentially applicable to green finance or limited demand for projects that can be financed.	Increase the availability of reimbursable and non-reimbursable funds for pre-investment studies and technical assistance
Structuring	A dedicated department to support the structuring of sustainable development projects, such as in the Foreign Trade Bank of Colombia (Bancóldex)
Unfavourable credit conditions	Soft loans with long payback deadlines
Lack of knowledge	Adequate training
Lack of pre-investment studies	Institutional financing through reimbursable or non-reimbursable technical assistance in conducting of the relevant studies
High risk involved in financing green projects	Devise an impact fund to reduce risks in green projects
Low appetite for risk among financial institutions for this type of project	Allocate resources towards partial credit guarantees as a risk management mechanism
No technical support for access to credit lines	Support to increase access to lines of credit by financial intermediaries
No risk management mechanisms proposed by cooperation agencies	Cooperation agencies develop instruments to minimize risks
No technical support for project design	Structuring of projects
Sovereign guarantees	Other guarantees
Governments' tax quotas	Requisite prioritization of investments and financing alternatives such as public-private partnerships

Source: L. A. Zuleta Jaramillo, "Intercambio entre bancas de desarrollo en América Latina y el Caribe para un gran impulso ambiental", *Project Documents* (LC/TS.2020/93), Santiago, Economic Commission for Latin America and the Caribbean (ECLAC), 2020, on the basis of the responses to a survey on development banking and project financing conducted by ECLAC in 2019.

[8] See Zuleta Jaramillo (2020).

Possible areas of cooperation among financing institutions include technical support from multilateral banks to strengthen the internal organization of financial institutions involved in green financing, capacity-building and the design of green finance products. The International Finance Corporation, sister organization of the World Bank, has an important role to play in this area. Bank associations can also be key players in promoting voluntary green protocols that integrate financial institutions in green financing strategies.

Strategies to foster cooperation among development banks include the exchange of information through knowledge platforms and networks with a view to sharing and disseminating best practices in financial instruments and technological innovation, including green technologies. In this regard, IDB actively participates in knowledge transfer based on China's experience in green financing to Latin American banks.[9] Knowledge-sharing through technology platforms could give rise to the formation of a working group, composed of national development banks, to create a joint programme pooling expertise and forming strategic alliances between institutions that design and manage similar products (Zuleta Jaramillo, 2020). Another possible outcome of knowledge-sharing is the preparation of guides on good practices related to development bank financing in specific sectors.

To implement best practices, top management will have to commit fully to the design and execution of a specific strategy. In some cases, it may be advisable to revise the regulatory frameworks and mandates of development banks to provide for greater flexibility in the use of innovative financial instruments.

Conclusion

Regional, subregional and national development banks have played a central role in providing countercyclical financing to address the effects of the pandemic. The COVID-19 crisis also made it clear that the development bank system can leverage its complementarities to assist different sectors and to create instruments, such as the guarantee system that has been widely used by several development banks in the region.

The actions of development banks can also help to drive a sustainable recovery in the region. This means, first, expanding the lending capacity of these institutions. Proposed measures have included increased capitalization, more flexible lending criteria and, more recently, the potential use of special drawing rights (SDRs).

Second, development banks can foster economic growth by adopting a resource allocation logic based on financing for environmentally, socially and economically sustainable development. Environmental, social and governance criteria —not just economic factors— must be an integral part of the guiding principles of production-oriented financing. Increased financing must be accompanied by changes in the composition of lending portfolios.

To this end, a significant percentage of the loan portfolio should be channelled towards green investments and climate change-related projects. The evidence shows that development banks, and in particular regional and subregional development banks, have increased the share of financing in the total portfolio through specific targets. However, green financing continues to represent a small share of the

[9] See Zuleta Jaramillo (2020).

portfolios of national banks, although many could capitalize on their existing mandates for sustainable development financing to make a new push towards environmentally responsible investment.

In order to scale up climate financing and strengthen sustainable financing, domestic development banks must overcome financial, technical and institutional constraints. A major barrier to the expansion of climate financing by development banks is the limited access to low-cost sources of finance and a lack of long-term capital. Projects aimed at improving the environment, such as renewable energy and urban infrastructure, are large-scale projects requiring heavy up-front capital investment. Environmental improvement projects also have long gestation periods. Another obstacle is inexperience and insufficient technical capacity to access funds and to design projects that are in line with the supply of financing. A third obstacle is the lack of coordination between public and private institutions: institutional coordination is a fundamental precondition for the financing of environmental projects.

Overcoming these constraints will require strengthened cooperation mechanisms and coordination among development banks. Better coordination between national development banks and regional development banks would mean that the latter could provide important financial support to their subregional and national counterparts, reducing costs, mitigating financial risk and building technical capacity for drawing up and presenting projects to obtain green financing.

While there are spaces for dialogue, the region lacks mechanisms for coordination between national development banks in the different countries and between national, subregional and regional development banks. Promoting the use of information exchange tools such as online platforms to share experiences and best practices is the first step towards surmounting this deficiency.

Bibliography

Cipoletta Tomassian, G. and T. Abdo (2021), “Financiamiento de la banca de desarrollo en el marco de la crisis del COVID-19 en América Latina y el Caribe”, *Financing for Development series*, No. 272, Santiago, Economic Commission for Latin America and the Caribbean (ECLAC), forthcoming.

Climate Funds Update (2021), “Data Dashboard” [online] https://climatefundsupdate.org/data-dashboard/.

ECLAC (Economic Commission for Latin America and the Caribbean) (2021a), “Financing for development in the era of COVID-19 and beyond: priorities of Latin America and the Caribbean in relation to the financing for development global policy agenda”, *COVID-19 Special Report*, No. 10, Santiago, March.

_______(2021b), *Economic Survey of Latin America and the Caribbean, 2021* (LC/PUB.2021/10-P), Santiago.

Environmental Finance (2021), Environmental Finance Bond Database [online] www.bonddata.org.

Fleiss, P. (2021), “Multilateral development banks in Latin America: recent trends, the response to the pandemic, and the forthcoming role”, *Studies and Perspectives series-ECLAC Office in Washington, D.C.*, No. 21 (LC/TS.2021/62-LC/WAS/TS.2021/2), Santiago, Economic Commission for Latin America and the Caribbean (ECLAC).

Green Bank Design Platform (2020), *State of Green Banks 2020*, Rocky Mountain Institute.

Green Bank Network, “Prospective GBN Members” [online] https://greenbanknetwork.org/prospective-gbn-members/.

Green Climate Fund (2021), “FP098 DBSA Climate Finance Facility” [online] https://www.greenclimate.fund/project/fp098.

Griffith-Jones, S. and others (2020), “Matching risks with instruments in development banks”, *Research Papers*, No. 170, French Development Agency, October.

G20 (Group of 20) (2021), *Italian G20 Presidency. Third G20 Finance Ministers and Central Bank Governors meeting. Annex I: An Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks Terms of Reference*, July.

Humphrey, C. (2020), "All hands on deck: how to scale up multilateral financing to face the Covid-19 crisis", *Briefing Papers*, London, Overseas Development Institute, April [online] https://www.odi.org/publications/16832-all-hands-deck-how-scale-multilateral-financing-face-coronavirus-crisis.

IDB (Inter-American Development Bank) (2020), *Development Effectiveness Overview (DEO) 2020,* Washington, D.C.

Independent Evaluation Group (2011), *The World Bank Group's Response to the Global Economic Crisis: Phase 1*, Washington, D.C., World Bank [online] https://openknowledge.worldbank.org/handle/10986/2277.

Maasdorp, L. (2021), "Multilateral development banks can do more to aid the recovery: they have been held back by restrictive capital requirements and a desire to maintain AAA credit ratings", *Financial Times*, 7 September.

Martin, E. (2021), "Latin America bank needs $80 billion capital hike, head says", Bloomberg, 3 February [online] https://www.bloomberg.com/news/articles/2021-02-03/latin-america-bank-head-says-capital boost-needed-for-recovery.

Settimo, R. (2019), "Higher multilateral development bank lending, unchanged capital resources and triple-a rating: a possible trinity after all?", *Questioni di Economia e Finanza (Occasional Papers)*, No. 488, April.

World Bank (2021a), "World Development Indicators" [online] https://databank.worldbank.org/reports.aspx?source=world-development-indicators.

_______(2021b), *The World Bank Annual Report 2021: from Crisis to Green, Resilient, and Inclusive Recovery*, Washington, D.C.

_______(2021c), "World Bank's response to COVID-19 (coronavirus) in Latin America & Caribbean" [online] https://www.worldbank.org/en/news/factsheet/2020/04/02/world-bank-response-to-covid-19-coronavirus-latin-america-and-caribbean.

World Bank and others (2015), *From Billions to Trillions: MDB Contributions to Financing for Development* [online] https://documents1.worldbank.org/curated/en/602761467999349576/pdf/98023-BR-SecM2015-0233-IDA-SecM2015-0147-IFC-SecM2015-0105-MIGA-SecM2015-0061-Box391499B-OUO-9.pdf.

Zuleta Jaramillo, L. A. (2020), "Intercambio entre bancas de desarrollo en América Latina y el Caribe para un gran impulso ambiental", *Project Documents* (LC/TS.2020/93), Santiago, Economic Commission for Latin America and the Caribbean (ECLAC).