The role of Industrial Policy in Brazilian development

A seminar for CEPAL’s Summer School
August 2010

João Carlos Ferraz

BNDES Brazilian development bank
• Recent performance, growth prospects and challenges
• Development Policies
• A challenge: long term financing
• The role of BNDES
• Summary and implications
Recent performance, growth prospects and challenges
• Growth in check... for some time… New poles of dynamism.

• Negative externalities associated with climate change.

• Fierce competition.

• Acceleration of technical progress.

• States actively defending national interests.
**Domestic market explains 2004-2008 growth cycle and 2010 recovery...**

### Contribution to GDP

( in percentage points)

<table>
<thead>
<tr>
<th>Year</th>
<th>Domestic Demand</th>
<th>Net External Demand</th>
<th>GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>2.5</td>
<td>0.2</td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>1.7</td>
<td>-0.5</td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td>5.7</td>
<td>1.2</td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>0.7</td>
<td>0.5</td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td>5.0</td>
<td>3.2</td>
<td></td>
</tr>
<tr>
<td>2007</td>
<td>2.7</td>
<td>4.0</td>
<td></td>
</tr>
<tr>
<td>2008</td>
<td>5.3</td>
<td>6.1</td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td>7.5</td>
<td>5.1</td>
<td></td>
</tr>
<tr>
<td>2010*</td>
<td>7.4</td>
<td>0.1</td>
<td>9.1</td>
</tr>
</tbody>
</table>

* Forecast

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Source: Ipeadata
... as economic inclusion is on the making...

Social Groups (% of total population)

Group C: 26% growth 2003-2009

Social Groups monthly earnings

- A&B: US$ 2,700 +
- C: US$ 620 – 2,700
- D&E: up to US$ 620

* Values in December 2008

Source: FGV and Finance Ministry

GDP (2009): US$ 1.6 trillion
Per capita income: US$ 8,200
An average 5% p.a. growth is feasible over the next 5 years...

Brazil: GDP Annual Growth Rate (%)

Source: IBGE, BNDES
... with investment leading the way...

Source: IBGE, BNDES
... as corporate investment plans are robust and rising...

<table>
<thead>
<tr>
<th>Sectors</th>
<th>US$ billion</th>
<th>Growth 2010-13 (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2005-8 (observed)</td>
<td>2010-13 (forecast)</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>111</td>
<td>172</td>
</tr>
<tr>
<td>Industry</td>
<td>174</td>
<td>305</td>
</tr>
<tr>
<td>Housing</td>
<td>191</td>
<td>258</td>
</tr>
<tr>
<td>Total</td>
<td>476</td>
<td>736</td>
</tr>
</tbody>
</table>

Source: BNDES Forecast

Based on Corporate Investment Plans from 13 sectors – Last Forecast: April 2010
Sample: 10% of GDP; 52% of Gross Fixed Capital Investment; 60% of Manufacturing investments; 90% of Infrastructure investments
Challenge: strengthen innovation capabilities

R&D/Sales (most recent available data)

- Germany: 2.60%
- France: 2.20%
- UK: 1.25%
- Norway: 0.97%
- Spain: 0.87%
- Brazil: 0.66%
- Hungary: 0.50%
- Czech Republic: 0.42%
- Portugal: 0.37%
- Argentina: 0.21%
- Mexico: 0.09%

Source: Innovation Surveys, various countries
Despite 0.2% negative growth in 2009, almost 1 million jobs created
Development Policies
Beyond the short term: development policies in place

Development policies

- Education - PDE
- Industrial Policy PDP
- S&T & Innovation
- Infrastructure PAC
- Health
- Housing

Industrial Policy: focus on investment, innovation, exports, SMEs
### Planned investments - US$ billion

<table>
<thead>
<tr>
<th></th>
<th>PAC 1 2007-2010</th>
<th>PAC 2 2011-2014</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Logistics</td>
<td>49.4</td>
<td>52.3</td>
<td>101.7</td>
</tr>
<tr>
<td>Energy</td>
<td>151.8</td>
<td>232.8</td>
<td>384.6</td>
</tr>
<tr>
<td>Social &amp; Urban development</td>
<td>130.8</td>
<td>194.5</td>
<td>325.3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>332.0</strong></td>
<td><strong>479.6</strong></td>
<td><strong>811.6</strong></td>
</tr>
</tbody>
</table>

Effective management by Minister Chief of Staff of the Presidency

BNDES in PAC 1: 331 projects
Financing US$ 76 bn for US$ 138 bn of investments (70% energy)

Highlights

• **Political priority**: President leadership

• **Direct involvement & partnership with relevant actors**: Ministry of Industry and Trade, Ministry of Finance, Ministry of S&T, BNDES

• **Policy focus**: Investment, Innovation, Exports, SMEs

• **Main beneficiary**: capital goods producers & users

• **Systematic interaction with private sector**

• **Effectiveness**: over 95% of proposed measures are operational
A comprehensive policy framework for a complex productive structure

PDP programmes

Consolidating and Expanding Leadership
- Aeronautics
- Oil, Gas and Petrochemicals
- Bio-ethanol
- Meat
- Mining
- Steel
- Pulp and Paper

Strengthening Competitiveness
- Automotive Complex
- Capital Goods
- Textile & Garments
- Wood and Furniture
- Hygiene and Cosmetics
- Housing
- Services Complex
- Naval & Shipping Industries
- Leather & Footwear
- Agribusinesses
- Bio-diesel
- Plastics
- Wheat
- Electronics – consumer
- Toy Industry

Fostering Knowledge
- Industrial Health Complex
- Information and Communication Technologies
- Nuclear Energy
- Defense Complex
- Nanotechnology
- Biotechnology

Strategic Issues
- Expanding Exports
- Strengthening SMEs
- Productive Integration with Latin America
- Integration with Africa
- Regionalization and production decentralization
- Clean Production and Sustainable Development
Governance: hierarchical structure and well defined roles for relevant agencies

Coordination Industry and Trade (MDIC)

Ministerial Council
Chief of Staff, Finance, Planning, S&T, Education

Executive Secretariat
Industrial Development Agency (ABDI), BNDES, Finance Ministry (MF), S&T Ministry (MCT)

Systemic Actions
Coord.: MF
1 Executive Committee

Strategic Themes
Coord.: ABDI
6 Executive Committees

Fostering Knowledge
Coord.: MCT
6 Executive Committees

Strengthening Competitiveness
Coord.: MDIC
15 Executive Committees

Consolidating Leadership
Coord.: BNDES
7 Executive Committees

The challenge: coordinating 500 civil servants; over 60 public agencies
Instances for Public-Private interaction
Participation: Government representatives and Representative entities of the private sector

- Permanent interface and dialog with private sector
- Presentation of proposals and actions
- Propositions for fine-tuning goals, actions and measures
- Establishment / Negotiation with private sector on counterparts and responsibilities

Instances for deliberating policy
Participation: Institutions, organs and agencies of the Federal Government

- Technical assessment and fine-tuning of private sector propositions
- Consolidation of and Agreement on the Agenda for Actions
- Negotiation / validation of public-private
- Definition of Execution Plan (priorities, goals and specific actions)
- Dispatch for Implementation
- Follow up
• The agenda of productive development has gained priority

• “Refreshing”, updating, upgrading the public debate over the “where to Brazilian industry?”

• Effectiveness: most measures are operational

• Intra-State interaction, especially between PDP and S&T policies

• Public-Private interaction: a growing recognition of the role each one has to play

• Recognition of the need for a permanent PDP
Credit Growth
(September 2008 = 100)

Contribution to Credit Growth
(Sept/08-Jan/10)

During the recent crisis, State-owned banks sustained credit expansion

Source: Bacen.
BNDES daily disbursements for Capital Goods procurement
Direct and 2nd tier operations (US$ million)

PSI: Interest rate equalization program for investments designed by Finance Ministry and operated by BNDES

Source: BNDES
• **Executive Committees**
  - Public servants of varied expertise
  - Limited participation of government institutions
  - Agendas for Action of varied quality
  - Limited experience in similar initiatives

• **Public-private relations**
  - Variance of private-sector representation
  - Private preference for “own channels” to expose needs
  - Difficulty in overcoming traditional negotiations of “complaints” and “support” agendas
  - Difficulties in defining “contrapartidas” to benefits
### A new PDP on the manking

<table>
<thead>
<tr>
<th>Sustainable and competitive development</th>
<th>Innovate &amp; invest to strengthen competitiveness and sustain growth</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ex-post Competitiveness (at markets)</td>
<td>Expand market share in world exports</td>
</tr>
<tr>
<td></td>
<td>Increase share of knowledge &amp; engineering intensive activities in economy’s valued added</td>
</tr>
<tr>
<td></td>
<td>Strengthen SMEs</td>
</tr>
<tr>
<td>Ex-ante Competitiveness (Eficiência)</td>
<td>Increase labour productivity</td>
</tr>
<tr>
<td></td>
<td>Increase capital efficiency and clean production</td>
</tr>
<tr>
<td>Learning and competences</td>
<td>Strengthen skills of labour force</td>
</tr>
<tr>
<td></td>
<td>Increase private R&amp;D</td>
</tr>
<tr>
<td></td>
<td>Expand Fixed Investment</td>
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</table>
A challenge: long term financing
BNDES is important for investment financing

Financing sources for Investment in Manufacturing & Infrastructure (2004-2009) (%)
But credit stock held by Brazilian largest banks is focused on the short term

Distribution of credit stock by duration
Reference dec/09, 50 largest Banks

- up to 3 months: 214,1 (20%)
- 3 to 12 months: 272,3 (25%)
- 1 to 3 years: 275,5 (25%)
- 3 to 5 years: 111,5 (10%)
- 5 to 15 years: 74,0 (7%)
- 15 years +: 143,0 (13%)

Short term prevails...
Up to 12 months: 45% - Above 5 years: 20%

Source: SPE/MF
Banks’ revenue from loan portfolio with duration of over 5 years (% of total revenue)

BNDES is practically alone in providing (and profiting from) long-term loans

Source: SPE-MF
Capital Market offerings are expanding but they are pro-cyclical

BNDES disbursements and Capital Markets offerings (% GDP)

* 12 months may 2009/10 ** Stocks, bonds, commercial papers, asset backed securities

BNDES & Capital Markets: complementarity rather than substitution

Source: SPE - MF
The role of BNDES
BNDES priorities follow Brazil’s economic momentum and policy priorities

BNDES priorities in time

1950s
Infrastructure (Energy and Transport)

1960s
Infrastructure (Energy and Transport) - Consumer Goods

1970s
Industrial Commodities - Capital Goods

1980s
Exports - Agribusiness

1990s
Privatization

Today
Infrastructure - Productive Structure - Exports

Upcoming Agenda
Above + Innovation & Sustainability
BNDES: main features

- Main provider of long-term financing in Brazil
- 100% State-owned company under private law
- Institutional funding
- 2,500 employees

BNDES 2009 – US$ billion

<table>
<thead>
<tr>
<th></th>
<th>Assets</th>
<th>Equity</th>
<th>Loans</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>222.0</td>
<td>15.9*</td>
<td>68.8</td>
</tr>
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</table>

Source: BNDES.  * Book value

Delinquency rate 2009 0.20%

**Instruments**

Direct operations | Indirect operation | Exim | Grants | SME | Project Finance | Equity investments

According to VneshEconomBank (Russia), in 2007-08, among ten largest development banks in the world, BNDES is:

Among ten largest in assets; 1st in return to capital; 1st in return to assets;
Recent expansion of demand required more support from National Treasury.

Institutional Funding (Workers’ Assistance Fund)

Prudential behavior is an asset of credibility

Source: BNDES
2009: BNDES financed US$ 46.8 bi for US$ 93 bi of fixed investments. These generated or maintained 4.5 million jobs (direct/indirect and income effects)

Source: BNDES. R$/US$: average exchange rate for each year
BNDES supply of credit is anti-cyclical

Source: BCB

BNDES share in total credit: in crisis, higher; in good times, lower

Source: BCB
BNDES contribution to GFKF is relevant

Disbursements*/GFKF 1995-2009 (%)

(*) excludes exim; support for internationalization; capital market operations, working capital and M&A

BNDES is contributing to the recent investment drive

Source: BNDES
Summary and implications
Drivers of a 5% p.a. growth (2010-2015)

Domestic market

✓ Consumption: emerging middle class
✓ Investments: oil & gas, renewable energies, agribusinesses, logistics, large scale events (World Cup, Olympic Games), housing

Foreign markets

✓ Trade and investment for food and energy security
Challenges for policy making

- Strengthen long term planning capabilities
- Improve macro performance: Savings/GDP
- Build up a financial industry oriented to the long term
- Adequate finance/guarantee/insurance for complex infrastructure projects
- Innovation focused on sustainability
- Priority for human resources: more and better jobs
Each nation has its own structure, history & aspirations. Hence, singular institutions. But, some features of Brazilian “PDP DNA” may serve as “food for thought” for others:

- **Flexibility**: learning and adaptation to change
- The spirit of serving the **public interest**
- Technical **competence** to be effective and efficient
- **Negotiating** skills: the capacity to interact with stakeholders
- **Opportunity**: to be on the right place, at the right time
- **Obsession** with investment
- **Political leadership**
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ANNEX – Tables and Figures

João Carlos Ferraz
80% of BNDES loans to industry and infrastructure

Disbursements by business sector (%)

Source: BNDES
Half of disbursements are through commercial banks.

Disbursements by type of operation (%):

- Direct Operation
- Indirect Operation

Source: BNDES
BNDES and size of firms: number and value of operations: a contrast

Number of operations and disbursement by size of firms

12 months up to April 2010 (accumulated values)

Source: BNDES
A large and diversified equity portfolio

Sectoral distribution of BNDES equity portfolio (%)

BNDES Equity Investment Portfolio:
US$ 47.5 billion (dec-09)
The role of Industrial Policy in Brazilian development

ANNEX – Tables and Figures

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