The experience of development banking in Peru: 1990-2015

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Two basic processes (privatization and dollarization) transformed the Peruvian financial system in the 1990s:

1) the privatization of the strong public-enterprise sector, non-financial and financial, as well as the liquidation of almost all state development banking.

2) the credit expansion of the 1990s was an expansion of loans in foreign currency, which reached a peak above of 20% of GDP right before the banking crisis of 1998-99.
Peru: lending by commercial banks and state-owned financial entities (% GDP).

Source: SBS, INEI, and BCRP

Compiled by authors
Peru: lending by state-owned financial entities (% GDP).

Source: INEI and SBS
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Peru: dollarization of credit by financial entities (% GDP).

Source: SBS
Compiled by authors
These two processes (privatization and dollarization) that transformed the Peruvian financial system occurred in a context of macroeconomic stabilization, economic activity recovered and inflation dropped to below 10% per year in the 1990s, accompanied by an improvement in the external situation (capital inflows).
Perú: terms of trade, GDP per capita and inflation. (1951-2016)
Main market failures of the Peruvian financial system:

1) long-term financing in domestic currency

2) financing of small businesses

3) agricultural financing

Potential market failures: those related to financing the necessary diversification of the export economy of minerals as well as climate change mitigation. There is no national plan with these long-term goals.
Perú: credit funding mismatches in local currency (LC) and foreign currency (FC) and external debt.

Source: INEI and SBS
Compiled by authors
Peru: lending, deposit and policy interest rates and inflation.

Source: BCRP

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Four state-owned financial entities:

(+) Banco de la Nación (BN) was created in 1966 to provide the banking services required by the public sector.

(+) Corporación Financiera de Desarrollo (CFD) created in 1971, is a credit institution that lends mainly to other financial intermediaries.

(+) Fondo Mi Vivienda (FMV) was created in 1998 to facilitate the acquisition of social housing.

(+) Banco Agropecuario (BA), created in 2001, grants loans to the agricultural sector.
Banco de la Nacion (BN):

Since 2000, the financial operations that can be carried out by BN have been gradually expanded. Receiving demand deposits from individuals and private companies that acted as suppliers to the public sector, receiving savings deposits from the same entities in places where commercial banks had no branches, granting loans to public sector employees and pension-holders, to execute operations and services with entities that lend to small and micro enterprises, etc.
Banco de la Nacion (BN):

(+) sources of financing, there has been a sustained increase in the relative share of deposits raised from the public.

(+) resource usage, it maintains very high liquidity surpluses, which has diminished the potential aggregate yield on its assets.

(+) Despite this, since 2009 BN has maintained a favorable average differential of +460 basis points between the aggregate return on interest-bearing assets and the aggregate cost of interest-bearing liabilities.
Banco de la Nacion: differential between return and costs.
In 1981, it was ruled that the investment activities of CFD would be transferred, and CFD was transformed into a credit entity. In 1991, it was ruled that foreign funding attracted by CFD should be channeled through the commercial banks, with a few exceptions; and that CFD’s security issuances would lose the tax exemption to which they were entitled. In 1992, CFD was prevented from gathering deposits from the public and lending to non-financial private sector, with a few exceptions.
Corporacion Financiera de Desarrollo (CFD):

(+) sources of financing, CFD has a high proportion of external debts; in recent years, an explosive growth was recorded in the long-term securities issued abroad.

(+) resource usage, CFD has increased its loans since 2010 but its returns are very low due to the legal obligation to use another financial entity as intermediary. Its liquidity surpluses has also increased in recent years.

(+) CFD has an average differential of just +4 basis points between the aggregate return on interest-bearing assets and the aggregate cost of interest-bearing liabilities.
Corporacion Financiera de Desarrollo: differential between return and costs.
FondoMiVivienda (FMV):

Since 2000, the financial operations that can be carried out by FMV have greatly expanded. In 2001, it was established that it could guarantee the credit or securities of private financial intermediaries. In 2002, it was granted the power to administrate a fiscal subsidy for the acquisition of social housing.

In 2005, it was authorized to participate in the mortgage lending market, and to implement products and services to stimulate supply and demand for housing; etc.
FondoMiVivienda (FMV):

(+) sources of financing, from 2012 the FMV's funding has changed drastically, increasing its share of bonds and notes issued abroad. Previously, its funding was equity-based.

(+) resource usage, credit picked back up after the 2008-09 recession; in the 2014-15 slowdown of the economy, credit increased less than external funding raising liquidity.

(+) since 2013, FMV has faced an unfavorable differential of -376 basis points between the aggregate return on its interest-bearing assets and the aggregate cost of its interest-bearing liabilities.
FondoMiVivienda: differential between return and costs (2006-2015)
Conclusions:

(+) since the 1990s, the four state-owned financial entities have not had much significance as instruments of public policy used to mitigate the market failures of the Peruvian financial system.

(+) these financial companies are subject to discriminatory legal regulation and do not coordinate with each other. Objectives overlap and synergies go unutilized. Some of these companies promoted greater financial dollarization. None of these institutions constitutes an effective state development bank such as exists in other countries.
Conclusions:

(+) for example, the BN could help to make the concentrated Peruvian banking system more competitive in the loan and deposit markets, but it is not allowed to operate in places covered by commercial banks. The CFD and the BN are required to meet the financing needs of small enterprises, but they are not authorized to carry out the direct intermediation of such credit.

(+) for example, the high costs of external liabilities and derivatives of CFD in 2013-15 could have been reduced if the BN had lent CFD some of its liquid resources in local currency deposited in the central bank at very low interest rates.
Conclusions:

(+) the external funding of these state financial institutions arises because they are not allowed to compete in the deposit market with private banks or participate on an equal footing with commercial banks in the money market governed by the central bank.

(+) with the exception of the BN, these institutions have ended up as followers of international investment banks through the local intermediation of the greater external debt that these entities offered them.
Thanks