

BANKING ON TRANSFORMATION: CHINA DEVELOPMENT BANK'S ROLE IN CHINA'S DEVELOPMENT



China Development Bank (CDB) has been a vital instrument in China's economic transformation, supporting step-changes in infrastructure provision, urban development, energy systems and the green transition. The experience of CDB over the last 30 years has not all been plain sailing. Along the way there have been mistakes, re-calibrations and plenty of useful learning. This case study will offer some observations on what the CDB experience demonstrates about the possible relationship between state and market, the process of 'learning by doing' and the importance of relative size, vision, leadership and expertise in development banking.

China's experience is in line with several other highly successful economies, including Germany, Brazil, Singapore and Korea who have used National Development Banks (NDBs) extremely effectively to support their development.

Today, NDBs are major global financial players. There are about 350 NDBs in more than 150 countries worldwide, accounting for 25 percent of total banking assets around the world.¹ They possess a number of characteristics which make them particularly well-suited to supporting large-scale transformations in low and middle-income countries where private investment bank and venture capital fund sectors are underdeveloped or non-existent: they can provide the patient capital necessary for large-scale, long-maturation projects such as infrastructure, without the demands for short-term returns associated with most forms of private lending; they are well placed to cope with uncertainty as they can pool and spread risk across their portfolios; they can demonstrate the viability of a sector or investment, ultimately leading to the crowding in of private investment and they also have an important role to play in creating bond and venture capital markets which is particularly important for low-and middle-income countries who struggle to raise affordable finance.

FACTS ABOUT CDB



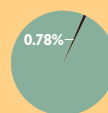
Established in **1994**



12,173 staff, 78% of whom have a master's degree or higher



Total assets of **US\$2.6 trillion** (18% of China's GDP) larger than the World Bank, Germany's KfW, the European Investment Bank, Brazil's BNDES, Asia Development Bank and Korea Development Bank combined



Non-Performing Loan Ratio: **0.78%**²

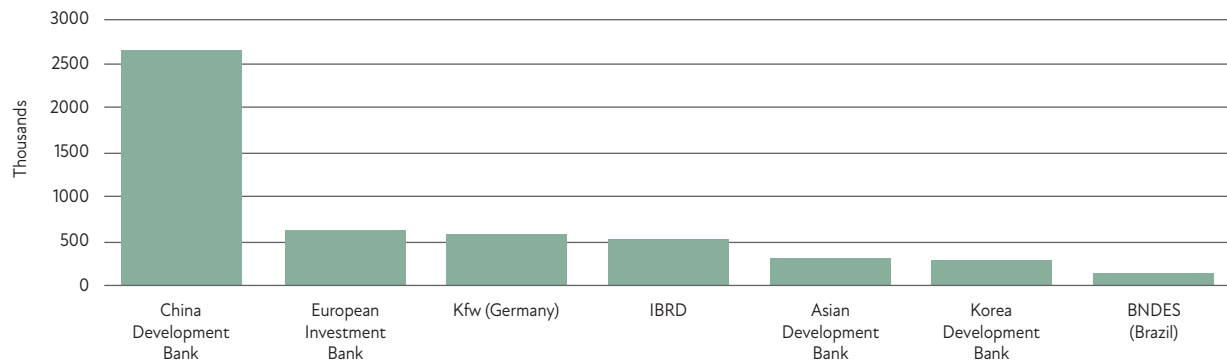
POLICY QUESTIONS FOR CONSIDERATION

- What development priorities would an NDB be best placed to tackle in your country?
- What could be the role of government in shaping the banking sector's activities and developing better-functioning markets in your country?
- How could your NDB be strengthened? Clearer mandate? Improved sectoral expertise? Access to affordable borrowing?
- Is your national development bank able to operate at the scale needed? Would a regional approach or greater collaboration with other institutions help?
- Is there a supportive national policy environment for your NDB?

¹Xu et al. (2021) Peking University of New Structural Economics and AFD, "Public Development Banks and Development Financing Institutions Database"

²Di John, J. (2020) "The Political Economy of Development Banking" The Oxford Handbook of Industrial Policy Oxford University Press

Chart 1: Total Assets of various NDBs 2022 (Million USD)



SOURCE: Xu et al. (2021) Peking University of New Structural Economics and AFD, "Public Development Banks and Development Financing Institutions Database"

THE ROLE OF CDB IN CHINA'S ECONOMIC GROWTH

The Chinese economy has been transformed in the last thirty-five years: extreme poverty has been all but eradicated, annual growth rates have averaged around 10% and per capita income has quadrupled.³ China has leapt ahead in manufacturing, agricultural productivity, infrastructure development and most recently in terms of developing and manufacturing green technology. It now accounts for 80 percent of the world's solar manufacturing capacity, its energy output from wind is more than twice the United States (number 2 in the world) and nine times more than Germany (number 3 in the world).⁴ The extraordinary scale of China's renewables sector output, particularly solar, has driven down prices worldwide.

CDB has been a central – although often overlooked – player in this process of economic transformation. Its priority is to lend to support key strategic sectors including: infrastructure; basic industries and public services; urbanization; the transformation, upgrading, and restructuring of traditional industries; energy conservation; environmental protection; and advanced equipment manufacturing and affordable housing (see Chart 2). In 2023 CDB issued a total of US\$ 433 billion of loans, nearly half of which focused on infrastructure development.⁵

In terms of the green transition, CDB has been a central player in supporting the move towards renewable energy and building China's capacity to process critical minerals and manufacture green technology including solar panels, wind turbines and EVs.



It has provided significant loans to support the roll-out of solar energy including to private company Jinko Solar and to many projects such as US\$31 million to support the forest-solar complementary power project in the city of Jiangshan and US\$433 million in loans to the Longyangxia Solar-Hydro power station, one of the largest photovoltaic power projects in the world.

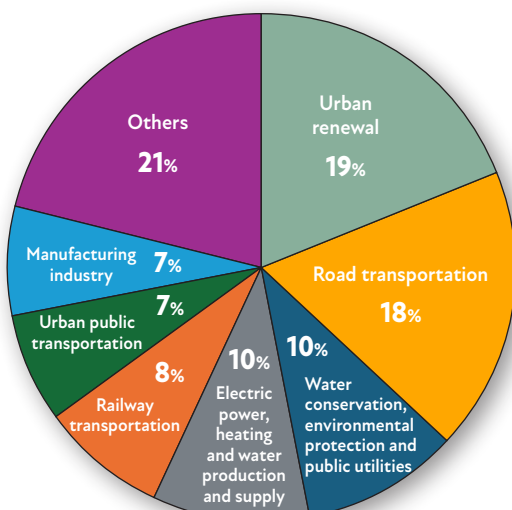


CDB has also been central in BYD's rise to become the largest manufacturer of EVs in the world. It is estimated that the Chinese government has spent \$60 billion in subsidies on electric vehicles between 2009 and 2017.⁶ As of 2024, cumulative credits granted by CDB Shenzhen Branch to BYD exceeded US\$11.2 billion with loans issued worth over US\$7 billion.⁷ In addition in 2016 CBD and BYD signed an US\$8.4 billion strategic cooperation agreement to support rail transit development in Shenzhen.



CDB is also a significant outward lender. From 2010 to 2015 CDB, together with the much-smaller China Export-Import Bank, lent more money annually to developing countries than the World Bank.⁸

Chart 2: CBD loans by sector 2022



SOURCE: CDB Annual Report.

³Various IMF and World Bank statistics

⁴Hilton, I. (March 2024) "How China Became a World Leader on Renewable Energy" Yale Environment 360

⁵China Development Bank Press Release 27/01/2024

⁶Gerbaudo, P. (April 2024) "The Electric Vehicle Developmental State" Phenomenal World

⁷Xu, J. presentation (May 2024) "China Development Bank and Green Industrialisation" given at SOAS DLD Future Leaders Programme

⁸Zhou, L. & Leung, D. (2015) "China's Overseas Investments, Explained in 10 Graphics" World Resources Institute

SUCCESS FACTORS

While all examples of rapid and successful development are unique and context-specific, it is useful to analyse the role of the CDB and make some observations that may have relevance for other countries. It is particularly interesting to note how CDB has created synergies between the state and market by using state levers – sometimes quite proactively and boldly – to incubate frontier markets and also bringing market discipline to facilitate China's transition from a planned economy to a market economy. CDB is also a very good example of organisational 'learning by doing', even of learning by failing, trying different methods and recalibrating as it went along. CDB's experience also demonstrates the importance of *relative* size and of vision, leadership and expertise.

1. Creating synergies between the state and the market in the service of industrialisation

CDB did not just 'fix market failures' – still often seen as the only legitimate role for development banks – but it has also been proactive in incubating and sometimes forcefully creating markets where they did not exist previously and in putting them in the service of the wider development strategy.⁹

In its early days when CDB was struggling to raise finance, government took an active role and the People's Bank of China (PBoC) issued an administrative order which forced financial institutions to buy CDB bonds. This expanded the bond market which then played an important role in promoting industrial policy. Later, CDB was central in further developing China's bond markets, making CDB bonds a mainstay of investors and helping to crowd in private investment, particularly for urban infrastructure. In the famous 'Wuhu model', CDB worked with the Wuhu municipal government to set up a market-based entity (Wuhu Construction Investment Corporation Limited WCIC) to which CDB could lend, using revenue from land sales as collateral, in order to support the development of the infrastructure needed to cope with rapid urbanisation. The WCIC also acted as a central place for coordination and monitoring of costs. Over time the WCIC progressed from a small financing vehicle into a sophisticated modern entity with large lending capacity and high credit worthiness.¹⁰

This example offers a different way of thinking about the relationship between states and markets. The state both created markets and also introduced market disciplines into state-run organisations – both in the service of a coherent industrial policy. In doing so, the state was not merely facilitative, it was directive. The example also demonstrates how NDBs are uniquely well-positioned to bundle projects across energy, infrastructure and industry creating what has been termed 'coordinated credit spaces' which then enable the entry of private finance.¹¹ This experience may be of particular interest to countries with shallow domestic capital markets or unstable or costly access to international financial markets.

“ Our mission is not merely to support social and economic development, but to drive the formation of sound markets and institutions that underpin such development ”

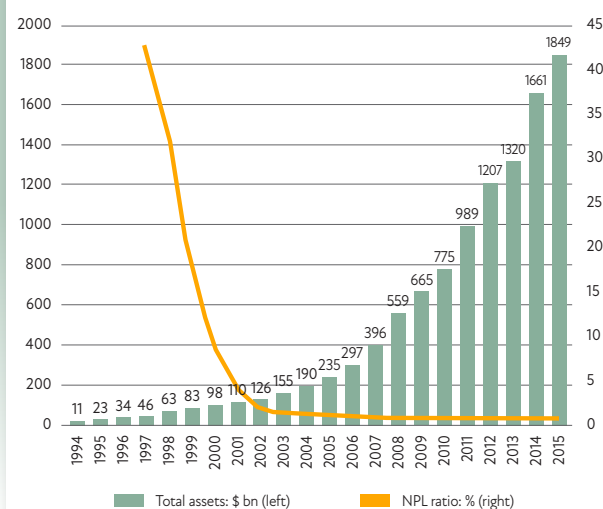
Yuan Chen, former CDB President and Chairman (1998-2013)

2. The process (and the learning along the way) matters

The experience of CDB demonstrates that effective development banks are not born perfectly functioning – there is a process of trial and error to arrive at a mission and structure that works for the given time and context.

Following its establishment in 1994 there was a high degree of government intervention in CDB's operations. It played a vital role in supporting government development priorities, but it was seen as providing 'fiscal handouts – a free lunch with no real obligation to pay'.¹² In its first four years of operation CDB's non-performing loan (NPL) ratio reached an unsustainable 42.7% and it was on the verge of bankruptcy. Under new leadership from 1998, CDB embarked on a series of market-oriented reforms to address the previous shortcomings, including: an internal risk control mechanism for new loans; the resolution of bad debts and measures to bring CDB up to international standards for transparency and reporting. Firewalls were also brought in to guard against undue political influence and make lending decisions more transparent. CDB also took steps to raise funds directly from bond markets instead of relying on the PBOC order. These reforms were very successful in tackling the NPL and growing CDB's assets (see Chart 3).

Chart 3: CDB Total Assets vs NPL Ratio



SOURCE: Xu, J. presentation (May 2024) "China Development Bank and Green Industrialisation" given at SOAS DLD Future Leaders Programme.

⁹Xu, J. (2017) "Market Maker: The Role of China Development Bank in Incubating Markets" *Man and the Economy*

¹⁰Xu, J. (2017) "Market Maker: The Role of China Development Bank in Incubating Markets" *Man and the Economy*

¹¹Chin, G. & Gallagher, K.P. (2019) "Coordinated Credit Spaces: The Globalization of Chinese Development Finance" *Development and Change*

¹²Xu, J. (2017) "Market Maker: The Role of China Development Bank in Incubating Markets" *Man and the Economy*

Nine years later – in part in response to China's WTO accession and in part in response to criticisms from China's commercial banks that CDB was crowding them out – CDB embarked on an ill-advised process of commercialisation which included questioning the sovereign-backing of its loans. The uncertainty this created raised its borrowing costs. There was a seven-year period of confusion where it was unclear if CDB would become a purely commercial entity, losing its developmental mandate. This was finally resolved in 2015 when the State Council designated CDB as a 'Development Financing Institution' that should not aim to maximise profits but should aim to break even.

All NDBs face this challenge of getting the balance right between public policy objectives and market principles and CDB was no exception. It took time, and a process of trial and error, to clarify CDB's purpose and that process of trying new approaches – even if they fail – is important.

3. (Relative) Size matters

The scale of CDB dwarfs its nearest competitors and there is no doubt that this scale has enabled it to achieve significant impact. For example, it would not have been possible for smaller NDBs through their individual interventions to have reduced the global price of renewables. However, as well as absolute size, what matters in terms of the effectiveness of NDBs is their size in proportion to the economy in which they are operating. CDB's assets amount to 18% of China's GDP. Other highly effective NDBs, Germany's KfW and Brazil's BNDES are 17% and 10% of GDP respectively. In contrast DBSA in South Africa and NAFIN in Mexico, which have arguably had less national impact have assets around 2-3% of GDP.¹²

4. Vision, leadership, targets and expertise matter

The experience of CDB demonstrates several well-known lessons regarding effective organisations, which bear repeating. Yuan Chen's exceptional leadership turned a near-bankrupt organisation into the largest and most successful Development Bank in the world. But the astonishing impact of CDB was also made possible by the strategic focus, clear targets and performance criteria set out in successive Chinese government 5-year plans, as well as CDB's position directly under the responsibility of the State Council.

The delivery of this success has also been supported by CDB's expertise. CDB was initially created out of six state-owned investment companies each of which had strong sectoral industrial expertise.¹⁴ This provided a solid foundation for the future as CDB has gone on to develop a staff of over 12,000 highly educated experts.

“ Under the charismatic leadership of Chen Yuan, the CDB's chairman – the “princeling” son of a Communist Party founding father – the bank has morphed from a piggy bank for state construction projects such as the Three Gorges dam into one of the world's most powerful financial institutions¹³ ”

FURTHER READING

Chin, G. & Gallagher, K.P. (2019) **"Coordinated Credit Spaces: The Globalization of Chinese Development Finance"** *Development and Change*

Griffith-Jones, S. (2022) **"The role public national development banks play in the structural transformation of developing countries"** UNCTAD

Xu, J. (2017) **"Market Maker: The Role of China Development Bank in Incubating Markets"** *Man and the Economy*

Xu, J. & Gallagher, K.P. (2022) **"Transformation Towards Renewable Energy Systems: Evaluating the Role of Development Financing Institutions"** *Studies in Comparative International Development*

Xu, Q. (2018) **"China Development Bank: Born Bankrupt, Born Shaper"** in Griffith-Jones (ed) *The Future of National Development Banks*

ABOUT SOAS DEVELOPMENT LEADERSHIP DIALOGUE (DLD)

Economic and social development requires many actors: however, typically these have operated in separate spheres, not understanding each other well and even seeing each other as adversaries. In a world characterised by profound changes and heightened uncertainties, overcoming this 'silo-ization' and the lack of mutual understanding it leads to is ever more important.

DLD brings people and disciplines together to generate more creative and strategic solutions to difficult development challenges.

DLD is generously supported by Hyundai Motor Group UK Ltd. and Kia UK Ltd.

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¹²Stephany Griffith-Jones (2022) **"The role public national development banks play in the structural transformation of developing countries"** UNCTAD

¹³Anderlini, J. (May 2011) **"CDB: Lender with a global reach"** *The Economist*

¹⁴These were the National Energy Investment Company; National Transportation Investment Company; National Raw Materials Investment Company; National Machinery, Textile and Light Manufacturing Investment Company; National Agricultural Investment Company and National Forestry Investment Company.