

## **Brazil's Banks Adjust View of Their Market**

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Brazil has never been considered a leader in microfinance, even though it has a huge poor population. There has been speculation that big countries like Brazil that are making large investments in IT may quickly expand commercial microfinance through commercial banks and eventually outpace other countries that have invested in NGOs and other specialized microfinance institutions. Only time will tell if that view holds up. The article below from the New York Times is of interest in this regard.

**SÃO PAULO, Brazil, April 8** - Banco Popular do Brasil was looking for customers like Lauziete de Sousa Gouvêa when it opened a branch in the shantytown where she lives on the western outskirts of São Paulo.

Ms. Gouvêa, who supplements her husband's modest salary as a security guard by selling lunches on the street from a food cart, had never had a bank account. But she had no trouble opening one at Banco Popular, a bare-bones operation of the government-owned Banco do Brasil. With just an identity card and her social security number, she opened a basic checking account, with no monthly fee and no minimum balance requirement.

The bank is one of several that have recently started or expanded operations to reach out to the 40 million poor Brazilians who had previously been shut out of the banking system.

For decades, banks here almost exclusively catered to the middle and upper classes, aiming at a small but wealthy minority in a country with one of the world's most skewed income gaps. But that is now starting to change, in part because Brazil's moneyed classes are already over-served by banks. That, analysts say, means the growth potential for financial institutions at the high end of the market is diminishing.

Banks are also shifting their attention to the poor because interest rates in Brazil are expected to drop in the coming years as inflation declines and the economy grows robustly. And as interest rates fall, banks will lose one of their biggest sources of revenue - trading government bonds indexed to the central bank's overnight lending rate.

"Banks have to look for alternatives to their classic investments in government bonds," said Rodolfo Spielmann, a partner at Bain & Company in São Paulo. "And they are waking up to the fact that the low-income classes are going to be the biggest source of growth for the future."

The government, too, is doing its part to bring the poor into the banking system. Two years ago, shortly after Luiz Inácio Lula da Silva became Brazil's first working-class president, the central bank loosened banking regulations after verifying that 1,750 of the country's 5,500 municipalities offered no financial services.

Under the new rules, banks can set up kiosks and banking terminals in supermarkets and drugstores instead of opening and running new branches. Because Brazil's banks are highly automated, these terminals tend to be inexpensive to operate, making it easier for banks to get a return on their investment.

To encourage lending to the poor, the government also allowed banks to use up to 2 percent of reserve requirements - money that would otherwise be parked at the central bank - to offer low-interest loans to low-income customers. By law, the interest charged on these loans cannot exceed 2 percent a month, a far cry from the 10 to 12 percent that most Brazilians pay for a consumer loan.

The new regulations set the stage for initiatives like Banco Popular, which was created in February 2004 and already has more than 1.3 million accounts and 6,000 branches. Caixa Aqui, a similar operation run by the government-controlled Caixa Econômica Federal, has 2.8 million accounts and has lent some 2.5 billion reais (\$916 million) in less than two years of existence, all to customers who earn no more than 1,000 reais (\$366) a month.

Government banks are not the only ones reaching out to the poor. Banco Bradesco, Brazil's largest private-sector bank, has its own version of these so-called people's banks, named Banco Postal, which provides banking services at post offices. Banco Postal has more than three million account holders, and a third of them have taken out loans.

Though most of the clients of these banks are unskilled workers with little job stability, their default rate - 9 percent at Banco Postal, for example - is not much higher than the market average. "In our experience, the first chance the customer gets he pays," said Odair Rebelato, an executive director at Banco Postal.

Other banks, like the privately owned Lemon Bank, a small bank based in São Paulo that operates exclusively through automated teller machines in outlets like bakeries and corner stores, are more interested in providing basic financial services than in offering credit. The bank, which was created by two Argentine investors in mid-2002 and broke even in the last quarter of 2004, handled 72 million transactions last year, mostly bill payments by nonaccount holders in poor urban neighborhoods. (In Brazil, bills can be only paid through a bank.)

"There's a lot of romanticizing about credit," said Michael Esrubilsky, Lemon Bank's general manager. "But what our client really needs is convenience to pay bills, to not have to spend an hour to get to the nearest bank and to not have to spend 10 reais on transportation to get back and forth."

Another way banks are reaching out to the poor is through partnerships with retail chains, which have been offering their own credit to low-income consumers for decades. Bradesco, for instance, signed a deal in November with Casas Bahia, the country's largest retailer of furniture and household appliances, to manage its credit portfolio. And Banco Itaú Holding Financeira, Brazil's No. 2 private-sector bank, recently agreed to provide consumer financing for a handful of retailers, including Companhia Brasileira de Distribuição, the leading supermarket chain.

For banks, joining forces with retailers is an easy way to "expand their operations to a broader client base without having to invest in organic growth or in acquisitions," said José Francisco Canepa, the executive director of Itaú's consumer finance unit.

Foreign banks are also joining in. Citigroup, which has long been considered a bank for the elite in Brazil, is now increasing its lending to the lower middle class through its consumer finance unit, CitiFinancial. HSBC Holdings, the British banking giant, has been even more aggressive in its quest to win over low-income consumers.

In late 2003, HSBC paid \$815 million to buy Lloyds TSB's assets in Brazil, which included a leading consumer finance company called Losango. With the acquisition, HSBC added seven million customers and immediately became a major player in the low-end consumer finance market. By the end of this year, HSBC expects Losango's credit portfolio to have more than doubled, to \$1.7 billion.

Ms. Gouvêa is pleased with her new bank account. She can accept payment in checks without the humiliation of asking friends to cash them. She can pay her bills every month at the Banco Popular kiosk in her neighborhood, instead of paying for bus fare to get to the nearest bank in the city. And in February, Ms. Gouvêa, who is 34, got her first bank loan - a low-interest advance of 300 reais (\$110) to pay some debt and have a bit more money available.

"I had always avoided banks because of all the bureaucracy," she said. "Now, all of a sudden, I even qualify for a loan. It's hard to believe."

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