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BANKS IN BRAZIL: CHALLENGES AFTER THE GLOBAL CRISIS

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ABSTRACT

Since the 1980s, the expansion of the private banking system in Brazil has favoured financial holding companies with diversified management of centralized assets which strategies are based on organizational changes, technological innovations, new labour relations, outsourcing, besides networks of retail outlets that offer financial services. This paper states that in spite of this expansion, the role of public banks has been outstanding in order to support the consumer credit cycle after the global crisis.

KEYWORDS

banking, Brazil, global crisis.

INTRODUCTION

 Since the 1980s, the expansion of the private banking system in Brazil has favored financial holding companies with diversified management of centralized assets which strategies based on organizational changes, technological innovations, new labor relations, outsourcing, besides the networks of retail outlets offering banking services (correspondents).¹

As of 2003, the Brazilian government was the prime mover of consumer lending as public banks turned out to expanding consigned loans to workers of the public sector and pensioners. However, after the global crisis, the role of public banks has been outstanding in order to support the consumer credit cycle. Since then, public banks Caixa Econômica Federal and Banco do Brasil have already stimulated, through competition, the sustainability of financial access.

This article aims to present an overview of the recent changes in the Brazilian banking sector in order to highlight the main role of public banks after the global crisis. Section one presents the banking dynamics before the global crisis. Section two examines the aftermath of the global crisis and the government policies oriented to liquidity and consumer credit growth. Finally, the conclusions identify challenges after the global crisis.

1. BANKING DYNAMICS BEFORE THE GLOBAL CRISIS

Changes in organization and dynamics of the Brazilian banking sector have been driven by political and institutional guidelines in a context of changing competitive strategies. In 1988, new financial regulations² officially sanctioned multi-function banks, which can be characterized by flexibility in the management of assets and liabilities integrating several financial portfolio -such as the commercial, investment, consumer finance, real estate, leasing and development. In the period between November 1989 and July 1990 the growth of the number of multi-function banks was 73.86% (from 88 to 153). However, it should be noted that this result was due mainly to the migration of specialized financial institutions towards multi-function banks.

In the first half of the 1990s, the banking expansion strategies were subjected to the parameters set by the stabilization plans. After the 1994 economic stabilization plan (*Real Plan*), price stability and financial integration were pillars of the expansion of financial activities in Brazil. The changes in the regulatory framework encouraged capitalization and the increase of the scope and scale of the banking institutions.³ Additionally, the Basel Agreement was adopted as a prudent guide. The key idea was that banking capital should be adjusted to risk assumed by financial institutions in the context of self-regulation and transparency of the markets. At this very juncture, the privatization of public institutions and the entrance of international retail banks contributed to accentuate the transformations already underway. In the late 1990's, the banking sector in Brazil became even more concentrated, privatized and internationalized. However, this trend caused the large private banks to adopt national strategies for consolidation and expansion in the domestic market based on the acquisition of control of small and medium institutions. Thus, mergers and acquisitions in the banking sector began to dominate the scenario of consolidation towards new structures further concentrated. During the layoffs of 1995 and 1996, on average, 174 workers were dismissed per day. In the first eight months of 1997, some 28,000 jobs were cut. This trend was exacerbated through a process of privatization, mergers, acquisitions and liquidations that reduced the total number of banks by 12% between 1999 and 2002. Reducing the number of employees was also associated with the intense process of outsourcing, especially from the 1990s onward.

In truth, a main feature of this adjustment was to reduce the total number of banks and increase the participation of foreign capital in the assets of the system by 2002. In 1994, there were 243 banks: the ten largest banks held 60.2% of total assets and 66.1% of total deposits. In 2002, there were 180 banks. The top ten had total assets of 68.3% and 75.7% of deposits. The new configuration of the banking sector in Brazil in terms of shares of domestic and foreign banks in total assets can be seen in Table 1.

TABLE 1: BANKING SECTOR IN BRAZIL: TOTAL ASSETS (in %, 1993-2003)

Banks	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Foreign Control	8.35	7.16	8.39	9.79	12.82	18.38	23.19	27.41	29.86	27.38	20.73
Domestic Control	40.67	41.21	39.16	39	36.76	35.29	33.11	35.23	37.21	36.93	40.76
Public Control	13.41	18.17	21.9	21.92	19.06	11.37	10.23	5.62	4.3	5.87	5.79
Credit Cooperatives	0.13	0.2	0.24	0.3	0.37	0.5	0.66	0.76	0.9	1.04	1.28
Total	100	100	100	100	100	100	100	100	100	100	100

Source: Banco Central do Brasil

¹ In Brazil, there are various retail outlets where bank services are offered. They can be post office agencies, lottery offices, supermarkets, etc.

² With regards to the regulatory framework and the evolution of the Brazilian financial system, it is important to emphasize the creation of the multi-function bank officially in 1988 by means of the Resolution No. 1524 - National Monetary Council.

³ With regards to the regulatory framework and the evolution of the Brazilian financial system, in 1994 the Resolution No. 2099 - National Monetary Council - decided on the adoption of new requirements for corporate and prudential regulation. It also recalled that in the absence of regulation of Article 192 of the Federal Constitution, the Ministry of Finance through the Explanatory Memorandum No. 311, 24/08/1995, proposed the release of the entry of foreign capital in the institutions of the national financial system, which could be authorized by the President, when approved by the National Monetary Council.

In the second half of 1990, the demand for new sources of revenue, in addition to the traditional activities of financial intermediation, stimulated new movements to diversification. The search and consolidation of new opportunities for expansion strengthened and increased the performance of existing financial conglomerates, enhancing activities related to asset management (mutual and pension funds), insurance, credit cards, consumer credit, consortiums, and brokerage (Table 2).

TABLE 2: BRAZIL: NUMBER OF FINANCIAL INSTITUTIONS PER TYPE, 2001-2007

Type of financial institutions	2001 Dec.	2002 Dec.	2003 Dec.	2004 Dec.	2005 Dec.	2006 Dec.	2007 Aug.
Multi-Function Bank	153	143	141	139	138	137	134
Commercial Bank	28	23	23	24	22	21	20
Development Bank	4	4	4	4	4	4	4
Caixa Econômica (Commercial and Saving Bank)	1	1	1	1	1	1	1
Investment Bank	20	23	21	21	20	18	17
Credit and Finance Institutions	42	46	47	49	50	51	52
Brokers (securities)	177	161	147	139	133	116	109
Brokers (exchange)	43	42	43	47	45	48	48
Dealers (securities)	159	151	146	138	134	133	132
Leasing	72	65	58	51	45	41	40
Real State credit institutions and Savings and Loans	18	18	18	18	18	18	18
Mortgage Companies	7	6	6	6	6	6	6
Development Agencies	9	10	11	12	12	12	12
Subtotal	733	693	666	646	606	606	693
Credit Cooperatives	1379	1430	1454	1436	1452	1452	1466
Micro-credit Lenders	23	37	49	51	56	56	55
Subtotal	2135	2135	2169	2133	2114	2114	2114
others	399	399	365	364	333	333	330
Total	2534	2536	2534	2497	2464	2447	2444

Source: Banco Central do Brasil

Multi-function banks are still the largest deposit-takers and financial service providers, although their number in Brazil has declined since 2001 (see Table 2). The contraction of the number of institutions can also be observed in commercial and investment banking besides leasing and brokerage (securities) activities. In addition, the expansion of financial access has enabled cooperatives to increase their activities in number, although their participation remains low in terms of the total assets –1.28% as of 2003.

As a matter of fact, the advances in the flexibility of the banking strategies were made possible by encouraging the creation of financial holding companies.⁴ In 2002, changes in the financial regulation sanctioned a new dynamic that favored the expansion of activities beyond the multi-function bank and involved the consolidation of new forms of concentration, diversification and management of capital in the banking sector. The main purpose of this corporate structure is to control diversified financial activities with a reduction of the opportunity cost of capital. Computer based investments, the diversification of delivery channels⁵ and the flexibilization in working conditions turned out to be part of an accumulation strategy supported by transparent corporate governance standards. In this sense, the financial regulation has reinforced an internationalized competitive business environment that justified new labor practices with relevant impacts on the future of bank workers and their forms of organization in the financial branch.

Considering the strategy centered on operational efficiency with diversification of the delivery channels (Table 3), the emphasis felt on the self-service network. In the investment diversification process, the operational expansion of credit, and finance institutions, insurance and supplementary pension funds fostered the employment beyond the multi-function banks. Besides, the strengthening of the computer technological controls also enhanced the delivery channels diversification process. In the period between 2004 and 2007, the weight of the self-service banking transactions in addition to the growth of the internet banking⁶, points of sale in the retail networks and correspondents are expressions of the recent transformations in the working conditions (Table 3).

TABLE 3: BANKING TRANSACTIONS BY TYPE, RELATIVE PARTICIPATION (2004-2007, in %)

	2004	2005	2006	2007
Self-service	32.9	30.7	32.4	33.5
Internet banking (corporations)	6.2	7.6	7.9	8.5
Internet banking (households)	6.8	9.0	8.9	8.4
Points of sale in retail networks(1)	3.3	3.2	4.1	4.1
Branches	12.0	10.6	10.4	10.4
Correspondents (2)	0.6	0.8	3.9	4.5

(1) such as shops, supermarkets, oil stations

(2) such as shops, lottery offices and post-mail offices.

Source: Febraban (2008)

The recent rise of transactions made through correspondents was supported by the expansion of physical units (Table 4). In this settlement, part of the financial transactions of the biggest retail banks has been transferred to the correspondents. Small banks like Lemon Triangulo have no bank workers related to traditional branches.

TABLE 4: CORRESPONDENTS RELATED TO SELECTED BANKS, 2009

Bank	Quantity of physical points/correspondents
BRABESCO	22,184
CAIXA ECONOMICA FEDERAL	13,773
BANCO DO BRASIL	13,645
HSBC BRAZL	7,198
LEMON	5,860
TRIANGULO	4,541
UNIBANCO	3,173
REAL	2,453
CITIBANK	2,113

Source: Banco Central do Brasil

⁴ In 2002, the Resolution 3040 -National Monetary Council - was published in order to give guidelines to the new conditions of access to the financial system.

⁵ In 2003, the Resolution No. 3110 - National Monetary Council- was published in order to define the possibilities of expansion of the correspondents.

⁶ As for the Internet banking transactions, the users totalled 25 million individual clients, after a growth of 12.6 million between 2006 and 2007.

The biggest retail banks have also stimulated the correspondents' expansion in order to enhance further mass credit services (Table 5). The workers that belong to these physical points are not considered bank workers, although they could develop similar tasks.

TABLE 5: CORRESPONDENTS RELATED TO MASS CREDIT SERVICES IN SELECTED FINANCIAL INSTITUTIONS, 2009

Institution	Conglomerate/holding	Quantity of physical points/correspondents
AYMORE	Real	31,847
BANCO POPULAR	Banco do Brasil	7,414
BANCO FININVEST	Unibanco	4,239
UNICARD	Unibanco	1,633
FINASA	Bradesco	1,293
HIPERCARD	Unibanco	1,028

Source: Banco Central do Brasil

In the context of technological changes, the ATM (Automatic Teller Machine) network was expanded from 14,453 units in 2000 to 34,790 in 2007. In the meantime, the number of bank branches and traditional points of attendance has had little significant increase, rising respectively from 16,396 to 18,308 and 9,495 to 10,427 in the same period. In the context of diversification of the delivery channels, the number of correspondents has grown, from 13,731 in 2000 to 84,332 in 2007 (Table 6). Thus, the channel represented by the correspondents in 2007 showed a growth of 15.5% and currently represents over 80% of all physical facilities provided by banks. As of 2007, correspondents opened 10.4 million new current accounts and 5.7 million savings accounts. In fact, correspondents initially offered financial services, such as opening current and saving accounts, withdrawals and deposits, loans, payments and tax collection, among others. In other words, without abandoning transaction activities (means of payment), the Brazilian correspondents turned out to foster credit operations (sale of personal loans and credit cards) (Gonçalves et al. 2009)

TABLE 6: BANKING SECTOR IN BRAZIL: DELIVERY CHANNELS (2000-2007)

	2000	2001	2002	2003	2004	2005	2006	2007	Variation 2007/2006	Variation 2007/2000
									%	%
Bank Branches	16,396	16,841	17,049	16,829	17,260	17,515	18,067	18,308	1.3	11.7
Traditional Points (1)	9,495	10,241	10,140	10,045	9,837	9,527	10,220	10,427	2.0	9.8
ATM network (2)	14,453	16,748	22,428	24,367	25,595	27,405	32,776	34,790	6.1	140.7
Correspondents (3)	13,731	18,653	32,511	36,474	46,035	69,546	73,031	84,332 (3)	15.5	514.2
Total	54,075	62,483	82,128	87,715	98,727	123,993	134,114	147,857	10.3	173.4

1. Include advanced points of attendance (PAA), points of banking attendance (PAB), points of cooperative attendance (PAC), points of micro-credit attendance (PAM), advanced points of rural credit (Pacrc), points for collection and payment (PAP), points to buy gold (PCO) and administrative units.
2. Automatic Teller Machines
3. Information from Febraban

Source: Banco Central do Brasil

Indeed, due to the overall transformations and the intensification of the technological resources, the trends in the banking computer technology investments turned to favor the expansion of the financial services in the context of a model of flexible production. The accumulation pattern enhanced not only the productivity growth, but also the increase in the work intensity. The search of productivity growth fostered the adoption of outsourcing (Sanches, 2006). In the last decade, there has been an increase in outsourcing of services related to telecommunications, help desk, projects and maintenance of systems, in addition to the processing of cards. In 2007, the banks outsourced a higher volume of services related to the maintenance of systems. The outsourcing of the back-office activities are beginning to be increased (Table 7).

TABLE 7: OUTSOURCING OF ACTIVITIES: DEGREE OF UTILIZATION, IN %, 2005-2007

Year/Activities	2003	2005	2006	2007
Telecommunication	47	68	68	74
Print Services	21	62	76	73
Help desk	32	48	63	67
Project and development of applicatives	-	52	62	64
System maintenance	32	43	43	55
Card Processing	21	52	58	54
Software House	nd	43	52	46
Back up site	11	38	49	44
Body shop	nd	20	37	37
Back office	-	-	-	7
Infrastructure de Central Processing Data	11	29	29	33

Source: Febraban (2008)

As a result of the new trends, management strategies centered on the shareholders have been the focus of the banking sector while productivity strategies put pressure on the reduction of the workforce (Table 8). The participation of human resources in the financial results of the banking sector has been strongly reduced in the period between 2000 and 2007.

TABLE 8: BRAZILIAN BANKING SYSTEM*: DISTRIBUTION OF THE FINANCIAL RESULTS, 2000 -2007, IN %

Year/December	2000	2002	2004	2005	2006	2007
Human Resources	60.6	42.3	43.5	37.98	39.6	33.2
Governement	22.2	23.1	26.2	25.1	25.9	24.3
Profit/ shareholders	17.3	34.7	30.4	37.0	34.4	42.5

* information from 150 banks

Source: FEBRABAN (2007)

2. THE AFTERMATH OF THE GLOBAL CRISIS: GOVERNMENT POLICIES ORIENTED TO LIQUIDITY AND CONSUMER CREDIT GROWTH

In the period between 2005 and 2007, the annual rate of growth of credit to households was 30%. As a matter of fact, banks modified consumer credit risk management practices by adopting new rules and standards in terms of types of contracts, credit –risk management, transaction costs and delivery channels. Consumer lending was stimulated by less-strict requirements in terms of income certification, payroll loans (consigned loans), loans against cars, besides the issuance of credit cards (Table 9). Banks turned out to focus on credit segments that would preserve liquidity targets and yield higher returns (Table 10).

TABLE 9: BRAZIL: CREDIT INDICATORS, 2005- 2010

Year/December	Total credit as a percentage of GDP (households plus corporations) In %	Consumer credit loans Average rate of growth (December/January) In %	Number of borrowers- individuals registered at the Central Bank of Brazil (In millions)
2005	28.3	21.46	10,580
2006	30.9	21.08	12,509
2007	35.2	24.71	15,146

Source: Bacen. Banco Central do Brasil. Sistema Gerenciador de Séries Temporais (SGS) www.bcb.gov.br/?seriestemp; Bacen (2011)

TABLE 10: SPREAD IN CREDIT OPERATIONS, FREE RESOURCES, IN %, 2000- 2010, DECEMBER

Year	Corporations *	Personal loans*	Tota consolidado	Meta Selic	CDI
2000	12.3	49.7	26,0	15,75	16,13
2001	13.3	51.0	28,7	19,00	19,05
2002	16.3	54.5	31,1	25,00	22,91
2003	14.4	50.9	30,0	16,50	16,81
2004	13.0	43.9	27,2	17,75	17,46
2005	13.8	42.7	28,8	18,00	18,15
2006	13.5	39.6	27,2	13,25	13,14
2007	11.9	31.9	22,3	11,25	11,11

Note: * The gross spread is obtained from the difference between the rates of funding and credit operations. Fixed rate operations are considered.

Source: FEBRABAN (2005)

Considering this background, the immediate responses of the government to the 2008 global crisis included measures aimed to increase liquidity and support fundraising in the domestic financial system to maintain and/or increase the supply of credit. Under the impact of the 2008 global crisis, credit policies supported the recovery of aggregate demand and the maintenance of high employment levels while monetary and financial stability was preserved.

Table 11 summarizes the set of measures taken by the Brazilian government between October and December 2008. In this scenario, the government decided to stimulate the levels of domestic consumption in order to preserve economic growth. The redefinition of credit policies- oriented to households was centered on the expansion of domestic credit flows by public banks (Banco do Brasil, Caixa Econômica Federal).

TABLE 11: RESPONSES TO THE FINANCIAL CRISIS: LIQUIDITY AND CREDIT MEASURES, 2008

Measures	Objectives
Reduction of the rate of compulsory deposits (at time deposits) from 45% to 42%.	Increase liquidity in the domestic financial system and enhance interbank flows and domestic credit operations
Definition of new requirements and conditions in compulsory fundraising/ allocation of bank resources.	Support credit flows to agriculture.
Redefinition of the compulsory allocation of bank resources.	Support credit flows to civil construction (housing).
Introduction of financial changes (assets, risk diversification) in the management of the deposit insurance system.	Increase liquidity and support fundraising in the domestic financial system.
Definition of new financial strategies (assets, spreads, risks, capitalization) in the management of public banks, mainly Banco do Brasil, Caixa Econômica Federal and BNDES.	Support credit flows to households, civil construction and private companies.

Source: Banco Central do Brasil

The reduction of 0.8% of the GDP (Gross Domestic Product) in the first quarter of 2009, in relation to the last quarter of 2008, revealed a soft landing of the Brazilian economy. To achieve this result, the credit expansion of the public banks was decisive (Table 12). As a matter of fact, the relative participation of public banks in the total amount of credit of the domestic financial system grew from 37.15% on February 2009 to 37.6% in March 2009, while this participation was only 34.2% in March 2008.

TABLE 12: CREDIT OPERATIONS IN THE BRAZILIAN FINANCIAL SYSTEM, TOTAL AMOUNT BY ECONOMIC ACTIVITY. FIRST QUARTER 2009, RATE OF CHANGE, IN %

	Public banks 1/	Domestic private banks	Foreign Private Banks
Public Sector	4.2	-0.4	-7.1
Private Sector			
Industry	2.8	1.2	-2.6
Housing	8.0	3.7	7.1
Agriculture	2.0	-3.5	2.3
Trade	3.5	-7.2	-6.1
Households	9.3	3.5	0.1
Total private sector	4.8	-0.9	-0.4
Total (Public and private sectors)	4.8	-0.9	-1.0

1/ Institutions where the government has participation superior to 50% in capital with right to vote.

Source: Banco Central do Brasil.

Table 12 reveals the role played by public banks in order to support the credit flows to the public and private sectors in a conjuncture where there was a reduction of the total amount of credit operations supplied by domestic and foreign private institutions. Indeed, in the first quarter 2009 the actions of the public banks have been outstanding in their attempt to preserve households' level of spending. Up to 2010 consumer loans increased sharply in all the regions of the country. The number of borrowers reveals the recent fast growth of consumer loans, increasing from 17,927 million people, as of December 2008, to 30,159 million in December 2010 (Table 13). The highest rates have been related to personal loans, credit cards and loans against cars.⁷

TABLE 13: BRAZIL: CREDIT INDICATORS, 2005- 2010

Year/December	Total credit as a percentage of GDP (households plus corporations) In %	Consumer credit loans Average rate of growth (December/January) In %	Number of borrowers- individuals registered at the Central Bank of Brazil (In millions)
2008	40.5	19.91	17,927
2009	44.4	15.16	22,233
2010	46.4	16.95	30,159

Source: Bacen. Banco Central do Brasil. Sistema Gerenciador de Séries Temporais (SGS) www.bcb.gov.br/?seriestemp; Bacen (2011)

⁷ Almost 60% of the total consumer credit refers to loans against property or cars and consigned loans (Financial Times, 2011).

With the advancement of public banks, their participation in the credit consumer market increased 10 % from 2008 to 2011. As of 2011, this participation amounted more than 45 % as of 2011. During this period, the rate of asset growth in the three largest private banks amounted 12.9%. However, the public bank Banco do Brazil achieved an increase of 20.8% in total assets in that period.

4. FINAL CONSIDERATIONS

After the global crisis, private banks have been increasingly selective in consumer lending (Abbc, 2012). In a conjuncture of crisis, as Minsky (1986) warned, financial fragility tends to grow due to increased indebtedness. Considering the Brazilian evidence, the delays in payroll of personal loans grew from which 5.7 % of total loans in December 2010 to 7.8% in November 2012, mainly in credit cards and overdrafts.

In addition, competitive pressures have increased in the banking sector, since retail private banks have been trying to regain or even maintained the market share that they lost to public banks in the aftermath of the global crisis. The comprehension of this Brazilian business reality is decisive to any transformation in institutions and policy making to promote sustainable economic growth and financial inclusion in the context of economic global integration.

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