



# **Understanding the demand for microfinance in Brazil: A qualitative study of two cities**

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## PREFACE

### **About the Institutional Development Program (PDI)**

The Program operates as part of a technical cooperation agreement signed between the National Economic and Social Development Bank of Brazil (BNDES) and the Inter-American Development Bank (IDB), in which BNDES participates as executing agency and beneficiary. Development Alternatives, Inc. (DAI), an American consulting firm with extensive experience in both microfinance and the management of donor resources, was chosen through an international competition to provide technical assistance in the implementation of the program.

The objective of the Institutional Development Program is to strengthen the microfinance industry in Brazil. The vision of the future is one in which the market offers, in a sustainable manner, financial services to microentrepreneurs operating both formal and informal enterprises, and to segments of the population which currently have limited or no access to such services. It is hoped that microfinance institutions will be capable of offering a range of products adapted to the needs of their target clientele, and that these institutions will integrate themselves increasingly into the formal financial system, which represents an essential and permanent source of funds for their operations.

The current stage of operational and organizational development of this industry in Brazil requires an investment in institutional strengthening. For example, access to specific microfinance technologies should lead to improvements in institutional performance. In addition, the program aims to improve the structural conditions for the expansion of the supply of microfinance services in the country.

The Institutional Development Program seeks to implement the following lines of action: first, support institutions whose performance contributes to the industry's development through a demonstration effect, and second, make available new tools in the areas of operation, management and controls, for the consolidation of the industry.



## ACKNOWLEDGEMENTS

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## INTRODUCTION

The microfinance<sup>1</sup> sector in Brazil is defined by seemingly paradoxical characteristics. Despite being the birthplace of Latin America's first microfinance institution (MFI) in 1973<sup>2</sup>, microfinance in Brazil has experienced levels of growth inferior to those of Latin American countries. While the late 1990's have seen an increase in activity<sup>3</sup> as demonstrated by the 220% jump in total portfolio growth of Brazilian MFIs between 1999 and 2001,<sup>4</sup> this indicator must be understood within the larger market context.

An analysis of active client numbers in the seven largest MFIs in Brazil<sup>5</sup> shows that while growth rates reached 40%-60% in 1998, there has been a marked slow-down in this rhythm since 2001.<sup>6</sup> In addition, despite the aforementioned increase in the total portfolio of MFIs between 1999 and 2001, the growth of these institutions is relatively slow compared to other players in the national financial system. Consumer credit lenders, for example, saw their volume of credit increase by 55% in the first six months of 2001.<sup>7</sup>

Overall, the penetration of institutions is weak compared to the size of the potential market. The roughly 100 MFIs in the country account for about 110.000 clients<sup>8</sup>, which represents less than 1% of the potential market of the estimated 15,7 million microentrepreneurs in Brazil.<sup>9</sup> Among the factors that are commonly cited to explain this phenomenon:

- an inadequate regulatory structure, despite recent efforts;
- the availability of substitutes such as consumer credit and;
- lack of a demonstration effect.<sup>10</sup>
- the harsh macroeconomic climate before the stabilization of hyperinflation in 1994;
- a strong tradition of government-subsidized credit programs;

While each of these factors has clearly influenced the development of microfinance, it is equally clear that a lack of understanding of the demand for microfinancial services has been an obstacle to the sector's development.

Providing clients with *what* they want is essential for the growth of any industry. In Brazil, the microfinance sector is dominated by one product: productive credit for microentrepreneurs. This very limited form of microfinance consists of working capital loans of R\$ 500 – R\$ 5000 with eight to twelve month terms. It is important to note, however, that the low-income families who constitute the potential market for microfinance

<sup>1</sup> Microfinance is defined here as small-scale financial services: credit, savings or insurance.

<sup>2</sup> Projeto UNO, the precursor to Centro de Apoio aos Pequenos Empreendimentos – CEAPE, Pernambuco.

<sup>3</sup> The active role of the Brazilian National Development Bank (BNDES) in recent years help explain this growth: in addition to working as a second tier lender, the Bank has helped strengthen and give an impetus to the microfinance sector in Brazil by establishing organizational and management norms for MFIs.

<sup>4</sup> In 1999, 67 institutions were operating with a total portfolio of R\$ 43,4 million (Goldmark, et al, 1999). In 2001, the total portfolio was estimated at R\$ 138.8 million, of which R\$ 49.8 million belong to the portfolio of CrediAmigo, the microcredit program operated by Banco do Nordeste. (Nichter et al, 2002).

<sup>5</sup> Institutions with more than 2000 clients in 1998.

<sup>6</sup> Source: BNDES/PDI.

<sup>7</sup> Study by consulting firm Austin Asis, cited in the Gazeta Mercantil, September 11, 2001.

<sup>8</sup> Of these, 85.000 are clients of the CrediAmigo program of the Banco do Nordeste (Gallagher, et al, 2002).

<sup>9</sup> Source: IBGE, Pesquisa da Economia Informal Urbana (1997).

<sup>10</sup> See Goldmark, et al, (1999) for a more detailed discussion of the Brazilian microfinance sector.



are not *only* microentrepreneurs and have financial necessities that go beyond productive credit. Understanding what these necessities are and how they are currently being satisfied is critical for the development of useful financial services.

Providing a service *how* clients want it is an equally important factor to the development of microfinance. This means designing and adapting products and processes according to what is acceptable in the minds of the clients. To meet these preferences, it is necessary to identify what they are, as well as understand the cultural and social factors that influence them. Perceptions of financial institutions and culturally defined notions of credit strongly influence what clients use and do not use, what they like and do not like. Further, understanding the role social relationships play in how people manage their money can provide important insights into guarantee mechanisms and repayment issues.

The design of this study was based on an overarching question: why are MFIs so little used in Brazil. The research focuses on the problematic of demand in urban zones:<sup>11</sup> the needs, available mechanisms, strategies and motivations that determine how poor people manage their financial resources. Demand has been defined here as *low-income people*, entrepreneurs and non-entrepreneurs alike. It is a broader notion than what is currently used by MFIs in Brazil, and attempts encompass the entire household in which most microenterpreneurial activities are embedded. Microentrepreneurs do not operate in a vacuum that separates their business from their household. Family and business budgets are almost always intertwined and as such, financial pressures that disrupt the income flow or force the reallocation of resources in one setting will have an effect on the other.

The objectives of this research were guided by the following questions:

- ▶ Is the current product offered adapted to the needs of potential clients?
- ▶ How do the cultural factors linked to perceptions of credit and financial institutions influence the use of financial services?

This paper aims to initiate discussion and provide some tentative answers to these questions, based on the results of the qualitative research conducted in the cities of São Paulo and Recife in November 2001.

It should be noted that, on the request of the BNDES, the findings detailed here are being subject to further analysis based on the focus group discussion transcripts. A complementary report of this analysis will be forthcoming.

## **ORGANIZATION OF THE PAPER**

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<sup>11</sup> See Abromovay, R. (2001) for a discussion of demand in rural areas.



Chapter One presents the research objectives and a summarized account of the methodology applied.

Chapter Two will examine the financial services being used by the populations studied and how the institutions that provide them are perceived. The services encountered during the research are presented in matrices, categorized by 1) sector: formal, semi-formal, and informal and 2) types of services defined here as lump-sum credit and installment credit. Savings mechanisms found in formal, semi-formal and informal sectors are also considered. Distinguishing characteristics, perceptions and motivations for using each of the products will be detailed, followed by an analysis of the tendencies identified.

Chapter Three will examine the financial needs of the populations studied and the mechanisms they use to meet them. The framework used for this section is loosely based on recent works<sup>12</sup> that suggest understanding poor people's needs as a result of financial pressures originating in emergencies, opportunities or life-cycle factors. In this paper, needs are presented in a matrix according to these events, in addition to seasonal events. The financial services used to respond to these events are categorized in the matrix by income-levels. An analysis of the necessities identified and the principal strategies used to meet them is followed by a discussion of differences between the different segments of the population studied.

Chapter Four proposes some "answers" to the overarching research question: why the majority of Brazilian MFIs are growing so slowly despite the potential demand. The implications of these findings for the country's microfinance sector are examined, followed by a discussion of product concepts that aim to provide a basis for further research and reflection on the improvement of current products and the design of new ones.

Where appropriate, secondary sources that support conclusions will be footnoted. References are provided in the bibliography.

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<sup>12</sup> Rutherford, S. "The Poor and Their Money", 2000; Wright; Rahman and Hossain.



## CHAPTER I RESEARCH DESIGN

### GENERAL OBJECTIVES

The objective of the study was to test, for the first time in Brazil, a set of market research tools adapted specifically to microfinance and, based on their application in a field study, determine the characteristics of the demand for microfinance.

Based on this general objective, the following specific objectives were defined:

- ▶ Determine how credit and savings are perceived among low-income populations;
- ▶ Examine the behaviors, strategies and mechanisms poor people use to manage their financial resources;
- ▶ Identify the events and circumstances that create the need to borrow money or use savings;
- ▶ Identify the social dynamics behind the relationship between low-income populations and financial service providers;
- ▶ Propose concepts that may be used as a basis for further product development research.

### METHODOLOGY

To better address the research questions, data collection was carried out using a qualitative methodology.

Traditionally used in social sciences, qualitative research aims to investigate and understand human behavior within a given context. It is more descriptive than definitive. Qualitative research does not deal with statistical measurements or proportions, but rather behaviors and attitudes. Data collected in a qualitative study enables the researcher to not only identify tendencies, but more importantly to understand the motivations behind the behaviors, habits or attitudes that create these tendencies.

Data collection was done with a set of tools proposed in the course Market Research for Microfinance Market Research for Microfinance, offered by Micro-Save Africa, an institution which has been working to help MFIs improve their product offerings. Developed with the objective to help MFIs understand and respond to the needs of their existing and potential clients, the course combines the use of Focus Group Discussions (FGD) and Participatory Rapid Appraisal (PRA) techniques (methods commonly used in behavioral sciences and in traditional market research).

Focus Groups are made up of 6-12 participants (depending on the nature of the research) who share a pre-determined set of characteristics, and who are brought together to discuss a given topic under the orientation of a moderator. The objective is to generate conversation about the research questions. The role of the moderator is to bring the group to discuss certain issues, keep the conversation on track, and encourage the participation of everyone in the group. The discussion is directed by a semi-structured discussion guide, designed beforehand according to the research objectives.

In Participatory Rapid Appraisal, participants from the community, with the help of a moderator, collect and auto-analyze information regarding their own experiences and context. The information is gathered and analyzed “by the participants, for the participants” during the group discussion. MicroSave-Africa’s toolkit<sup>13</sup> proposes thirteen different PRA tools. Each one aims to help the researcher to identify specific financial tendencies and behaviors. The tools are applied one at a time in groups of 8-10 people and serve to orient the discussion, as would a discussion guide.

## PRA TOOLS USED

In order to analyze the financial needs of low-income populations (individually and within the household), and discover the ways these populations are currently meeting these needs, the following tools were used:

- ▶ **Life-cycle Profile:** to determine which of the events require lump-sums of cash; to examine the implications of these for household income/expenditure; to establish current coping mechanisms; and to discuss how access to MFI financial services can help the household respond to these.
- ▶ **Seasonality Analysis of household income, expenditure, savings and credit:** to obtain information on seasonal flows of income and expenditure, and the demand for credit and savings services.
- ▶ **Financial Sector Trend Analysis:** to determine which financial services have been used over time and understand why there have been changes in the use/availability of a variety of financial services over time.

For a more detailed examination of the financial necessities of microentrepreneurs, and to identify reasons why MFIs are so little used in Brazil, the following tools were also used:

- ▶ **Financial Services Matrix:** to determine which financial services are used by which socio-economic or socio-cultural strata of society and why;
- ▶ **Relative Preference Ranking:** to see how clients and potential clients perceive financial service providers and characteristics of the financial services they provide.

In addition, the authors conducted a number of FGDs oriented by a discussion-guide in order to complement and complete the information gathered using the PRA tools.

## ORGANIZATION OF FIELD STUDY

The research process began with the training of the research team in PRA and FGD techniques by a certified MicroSave-Africa trainer<sup>14</sup>. Aspects covered included: selection and recruitment of group members, preparation of groups (logistics and design of discussion guide), moderation, use of tools and finally the systematization and interpretation of results and their transformation into product concepts.

<sup>13</sup> Version February 2001.

<sup>14</sup> Henriqueta Hunguana, ICC-Mozambique



The training involved four days of theoretical class work and one day of practical experience that allowed training participants to moderate and/or observe four PRA sessions held with microentrepreneurs from the Municipality of São Gonçalo, Rio de Janeiro.

Following the training, the research coordinator worked with the logistical teams identified in the two cities to be studied, São Paulo and Recife, to define the modalities of data collection (sample size, selection characteristics of FGD participants, time and place of discussions, etc.).

A total of 35 discussion groups (roughly 300 participants), 18 in São Paulo and 17 in Recife, were conducted during the field work.

## POPULATIONS STUDIED

The study examined microentrepreneurs and salaried/unemployed workers from two metropolitan regions, divided into three income levels.

### Regions

In an attempt to account for regional diversity in Brazil, the field research was carried out in two geographically distinct areas.

The choice of São Paulo as the “representative” from the South was based partly on the fact that it represents an enormous potential market for microfinance and partly due to the identification of a local entity that was interested in the research for operational reasons. *São Paulo Confia*, a new microcredit program of the municipal government, had just initiated lending activities and demonstrated a keen interest in taking part in the study in order to gain a better understanding of their clients.

#### A selection of microfinance programs in the state of São Paulo

**Banco do Povo-Santo André:** program of the municipal government. Started operations in 1998. Offers credit to microentrepreneurs who have been exercising their activity for at least six months.

**Banco do Povo do Estado de São Paulo:** Started operations in 1997. Offers credit to microentrepreneurs.

**Centro de Apoio aos Pequenos Empreendimentos-CEAPE - São Paulo**  
Offers credit to microentrepreneurs who have been exercising their activity for at least six months.

**Micro-Cred Ltd.: Sociedade de Crédito ao Microempreendedor**  
Offers credit to microentrepreneurs who have been exercising their activity for at least six months.

Credit lines for microentrepreneurs from the federal program **Programa de Geração de Renda-PROGER**, available in any Banco do Brasil and Caixa Econômica Federal.

**São Paulo Confia:** Began operations in September 2001. Offers credit to microentrepreneurs who have been exercising their activity for at least six months.  
Also offers housing loans, loans for cooperatives and for beneficiaries of select social programs of the municipal government (*Renda Mínima, Bolsa Trabalho* and *Começar de Novo*).



Recife was selected as being representative of the Northern region of Brazil in part because of the availability of a competent local entity that expressed willingness to organize the discussion groups. In addition, it seemed important to examine a Northeastern locale where the *Banco do Nordeste* is implementing the well-known *CrediAmigo* microcredit program. Essentially the only microcredit program in Brazil with a level of outreach that roughly corresponds to what is believed to be the potential demand, *CrediAmigo* further stands out in the sector as the only large-scale microcredit initiative using solidarity group methodology.

#### Microfinance programs in the metropolitan area of Recife:

**Banco do Povo da Agência do Trabalho:** Credit for microentrepreneurs. Administered by *Caixa Econômica Federal* and *Banco do Nordeste*.

**Banco do Povo da Prefeitura:** Credit for microentrepreneurs. Administered by *Banco do Brasil*, *Caixa Econômica Federal* and *Banco do Nordeste*.

**Casa da Mulher do Nordeste-CMN:** Credit for women microentrepreneurs. Also offers training and technical assistance.

**Centro de Apoio aos Microempreendedores-CAM:** Credit for microentrepreneurs, for start-up or expansion of activities. Also offers training and technical assistance.

**Centro de Apoio aos Pequenos Empreendimentos-CEAPE Pernambuco:**  
Offers credit to microentrepreneurs who have been exercising their activity for at least six months.

**Fundo Rotativo da Ação da Cidadania-FRAC:** Offers credit to microentrepreneurs who have been exercising their activity for at least six months. Also offers technical assistance.

**Programa CrediAmigo do Banco do Nordeste**  
Offers credit to microentrepreneurs who have been exercising their activity for at least twelve months. Also offers technical assistance.

Credit lines for microentrepreneurs from the federal program **Programa de Geração de Renda-PROGER**, available in any *Banco do Brasil*, *Banco do Nordeste* and *Caixa Econômica Federal*.

#### Visão Mundial

Credit for microentrepreneurs and cooperatives.

## Income

The income levels were defined based on a classification system used by the São Paulo municipal government to define low-income populations. The economic reality of Recife and the overall lower income levels of its population made it necessary to adjust these ranges. As such, the results of this research are organized according to the following three categories:

	São Paulo	Recife
Very Low		0 - 2 Minimum Salaries (R\$ 90 - R\$ 360)
Low	2 - 3 Minimum Salaries (R\$ 360 - R\$ 720)	2 - 4 Minimum Salaries (R\$ 360 - R\$ 720)
Medium-low	3 - 6 Minimum Salaries (R\$ 540 - R\$ 1080)	3 - 6 Minimum Salaries (R\$ 540 - R\$ 1080)

## Occupation

The studied examined two segments of low-income populations:

- ▶ Microentrepreneurs. This group was further segmented based on branch of activity: commercial/ services and production/industry.
- ▶ Salaried workers and unemployed persons.

This variable was included to compare the needs of these two groups and to determine if non-microentrepreneurs should indeed be considered as potential clients for microfinance services.

## Sex

Only the Life-cycle Profile tool was systematically applied to single-sex groups in order to identify possible differences in perceptions of what events create the most financial pressures.

For more information on the methodology, a detailed description of the tools used and the adaptations made to them during the research, refer to the Annexes.



## CHAPTER II: WHAT IS USED AND WHY

While the majority of low-income populations do not have direct access to the formal banking sector<sup>15</sup>, they are managing to meet their financial needs through a variety of services available to them. This chapter will present these services and their users' perceptions of them.

In the populations studied, resorting to credit in its numerous forms was by far the most common way to satisfy their financial needs. Participants interviewed for this study had no trouble listing the ways that people get by when cash is insufficient—a situation that defines the daily existence of poor families in Brazil. Informal store credit, payment plans, credit cards (bank-issued, consumer lending agencies-issued, department store-issued), post-dated checks, overdraft facilities, family and friends, a salary advance from an employer, rotating savings and credit mechanisms (ROSCAs) known as *sorteios* and *caixinhas*, informal moneylenders (known as *agiotas*), consumer-lending agencies, formal banks...the options appear great. However, a closer look at this list reveals that their apparent variety and accessibility is misleading.

Essentially, the populations studied are using two modalities of credit, defined here as **lump sum** and **installment credit**, being provided by the **formal**, **semi-formal** and **informal** sources. Some savings mechanisms are also used, but in general putting money aside for later usage is infrequent. **Lump-sum credit** refers to credit that is disbursed in the form of cash upfront (loans) while **installment credit** takes the form of the object being purchased. These forms of credit differ in how they are disbursed and not how they are repaid: both forms are repaid over time according to a pre-established repayment calendar.

The financial products and mechanisms<sup>16</sup> encountered in this research are presented here in the form of matrixes using the above-mentioned categories. The definitions of formal, semi-formal and informal used in this paper are based on requirements necessary for accessing the services and not legal definitions. Nonetheless, the majority of the services included in the **formal** category are part of the National Financial System. Very general descriptions of the terms and conditions of the services are provided, although they vary widely from product to product. The characteristics of each service—how it works, application and approval processes<sup>17</sup>—are described followed by a discussion of the populations' perceptions of each one.

The level of usage is roughly evaluated within the matrix framework with asterisks. One asterisk represents very little usage while five asterisks indicate heavy usage. However, because what financial services are used depends on income level and, more importantly, what they are used for, the question of usage will be addressed in more detail in Chapter Three.

This section will conclude with a discussion of the tendencies encountered, including a look at the attributes that appear to be the most and least valued.

<sup>15</sup> Approximately 70% of the Brazilian population does not have any sort of bank account. Gallagher, et al (2002).

<sup>16</sup> The term "product" refers to a good, while mechanism refers to a process or system. Both terms are used in this document. The term "financial services" will be used to refer to both products and mechanisms.

<sup>17</sup> This information is based on the report "O Mercado de Crédito para Pessoas de Baixa Renda no Rio de Janeiro", Gallagher, et al (2002) in which one of the chapters offers a detailed discussion of the formal supply of credit.



**Categorization of the financial services encountered**

	Lump-sum credit	Installment credit
<b>FORMAL SECTOR</b>	bank loan for specific use bank line of credit cash advance from credit cards (bank, department store or consumer credit agency-issued) consumer-lending agencies loan from MFI cashing-in of post-dated checks	credit cards post dated checks overdraft facilities via <i>cheques especial</i> payment plan via retail merchandisers
<b>SEMIFORMAL SECTOR</b>	salary advance from employer loan from <i>agiota</i> cashing-in of post-dated checks with <i>agiota</i> loan from the workplace <i>caixinha</i>	payment plan from small retailer supplier credit
<b>INFORMAL SECTOR</b>	loans from family and friends	informal store credit ( <i>pendura or fiado</i> ) <i>sorteio</i> "borrowed credit"

**FORMAL CREDIT SUPPLY**

Formal sector credit is distinguished by the following:

**1. The requirements:**

- ▶ Cadastro de Pessoa Física (CPF)<sup>18</sup>;
- ▶ Identity Card;
- ▶ Proof of residence;
- ▶ Proof of income or Personal guarantee (individual co-signer or solidarity group);
- ▶ Clean credit record: client's name must not appear on the list of any of the credit protection agencies (*SPC, Usecheque, Telecheque, SERASA, etc.*).

2. The use of a **written contract and receipts** upon disbursement and repayment.

**3. Terms and conditions** may vary greatly:

- ▶ Amounts: R\$ 50—R\$ 5000;
- ▶ Repayment: biweekly or monthly;
- ▶ Terms: 1—36 months;
- ▶ Interest rates (not including fees, late payment penalties): 0—11,5%/month.

<sup>18</sup> Similar to a United States Social Security Number.

Services used in the formal sector

LUMP-SUM CREDIT	USE
bank loan	*
bank line of credit	**
cash advance on credit card	*
loan from consumer lender	**
loan from MFI	*
cashing-in post-dated check	*
INSTALLMENT CREDIT	
credit card	****
post-dated check	***
overdraft facility via <i>cheque especiais</i>	**
payment plans from retail merchandisers	*****

Bank Loans and Lines of Credit

Credit in the form of loans or a line of credit is available from variety of sources. However, the populations studied resort to this kind of lump-sum credit much less than installment credit.

Bank credit comes in a variety of forms: object-specific loans (for the purchase of a car or computer, for example), productive loans for microentrepreneurs via the *Programa de Geração de Emprego e Renda* (PROGER) credit line<sup>19</sup> and fixed limit lines of credit automatically available to account holders with sufficient resources.

<p><b>Conditions</b>  <b>Loan from PROGER line:</b>                  CPF, ID, proof of income (can be substituted by proof of presumed income), collateral (depends on institution: capital asset, personal guarantee, property title, fiduciary alienation, mortgage), a business plan approved by a certified technical assistance entity. An account with the bank giving the loan. Clean credit record.</p> <p><b>Credit Line</b>                  Must have bank account, which requires CPF, ID, proof of residence, minimum income requirement (amount depends on institution), References. Clean credit record. Credit limit depends on account activity and the median balance.</p>
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While bank loans are out of reach for the majority of persons interviewed, those that had taken loans generally complained of lengthy bureaucratic procedures, especially for loans from the PROGER line (too much paperwork, too many requirements, too long a process to receive money).

Credit lines, however, are conceded to anyone with a bank account that maintains a positive balance and are considered very useful and accessible. This service, available from an automatic teller machine, is greatly appreciated, as it requires no paperwork or approval process. Retirees and even very low-income salaried workers can access this service in banks where their payments are deposited.

<sup>19</sup> PROGER is a component of the Program *Brasil Empreendedor*, a program of the federal government aimed at strengthening micro, small and medium enterprises and recently trained entrepreneurs. PROGER is an ensemble of credit lines whose resources come from the Fundo de Amparo ao Trabalhador – FAT. The operators of these credit lines are *Caixa Econômica Federal*, *Banco do Brasil*, *Banco do Nordeste* and *Banco da Amazônia*. For a somewhat partial evaluation of PROGER, see: "Avaliação do PROGER, PROGER Rural e PRONAF do Fundo de Amparo ao Trabalhador-FAT, Instituto Brasileiro de Análises Sociais e Econômicas (IBASE) Ministério do Trabalho, Secretaria de Políticas de Emprego e Salário (1998-99).

## Credit Cards

**Credit cards** issued by banks, retailers or consumer-lending agencies are widely used. Those who do not have their own due to insufficient income or a marred credit record generally have no problem using the card of a friend or relative.

The credit card is mainly used as a form of installment credit, to pay for purchases in up to 30 days without interest. However, it is also a form of lump-sum credit since one can take cash advances from the automatic teller machines. This practice appears infrequent, nonetheless, and is reserved for emergencies. Most people attest to an increase in credit card use over the past three years. It used to be impossible for low-income populations to get a credit card. Nowadays, *“they send it [by mail] without even asking!”*

**Bank-issued credit card**  
Must have bank account. Proof of minimum income of R\$ 400.  
Clean credit record.  
Credit limit depends on card.

According to the populations studied, credit cards are practical, easy to use, and with no bureaucracy once the initial contract is out of the way. Further, credit cards offer automatic renegotiation of debt. The facility of the use of credit cards was nonetheless somewhat polemic in several groups. Those that defend their

*“You think that money is yours, and you spend it. When the time comes to pay, then you really feel it.”*

use underline the convenience credit cards offer and inexistence of interest when the bill is paid on time. Those that are wary of credit cards point out the high interest rates when bills are not paid and the dangers of the losing track of one’s spending and risking debts that are difficult to pay back, which lead to being included on the “black lists” of the credit protection agencies.

**Store-issued credit card**  
CPF, ID, proof of income (depends on the store, generally R\$ 150 - R\$ 300). Clean credit record. Credit limit depends on card.

**Retail store-issued credit cards**<sup>20</sup> (supermarkets, department stores, discount stores) are more common than bank-issued cards among the populations studied. The requirements are apparently easier to satisfy than those of banks, although they usually request proof of income and a clean credit record. In Recife, the large supermarket chains widely distribute credit cards among its clients. These cards are used to pay for purchases made in affiliated stores in up to 30 days, no interest. Some also allow holders to take cash advances from automatic teller machines. Quite popular among the upper level income groups interviewed in this study, store-issued credit cards work like bank-issued credit cards and some have the advantage of not requiring a bank account. As such, even those with negative balances or blocked accounts have access to these kinds of credit cards.

## Consumer-lending agencies

The services offered by **consumer-lending agencies**-credit cards and loans-are used essentially in times of emergency. Credit cards appear to be little used due to the interest rates, considered extremely high when compared to other cards available. Taking loans is slightly more common, but participants expressed great aversion to doing so. The majority of those who had gone to a consumer-lending agency had done so because of lack of options.

**Credit card and loan from consumer-lending agency:**  
CPF, ID, proof of residence, proof of income R\$ 150 – R\$ 270 (depends on agency).  
Clean credit record.

<sup>20</sup> Known as *private label*.



The low income requirements in consumer-lending agencies make them the most accessible formal option for low-income populations. (*Fininvest*, the most commonly cited agency, requires clients to prove a minimum monthly income of only R\$ 150.) Nonetheless, consumer lenders are avoided. They have a very bad reputation, and are considered “legalized *agiotas*” or “the worst of all *agiotas*” because of the high interest rates, the paperwork necessary, the aggressive collection techniques (re-possession of item purchased, insistent phone calls) and the unwillingness to negotiate repayment.

### Loans from MFIs

The use of productive loans of R\$ 300 – R\$ 5000 from specialized **microfinance institutions** aimed at microentrepreneurs is infrequent even in Recife where various microcredit programs work. For the few familiar with these institutions, the amount of paperwork and bureaucracy is highly criticized, as well as the co-signer requirement, considered very hard to satisfy. Many feel that that these institutions engage in misleading propaganda: they are supposed to offer services adapted to the “masses” (*o povo*), but in fact have almost the same requirements as banks or consumer lenders. As such, loans from MFIs are oftentimes out of reach for the low-income microentrepreneurs seeking capital.

**MFI Loans**  
CPF, ID, proof of residence, co-signer or solidarity group or declaration of income tax. Must have exercised activity for at least 6 or 12 months, depending on the institution. Clean credit record.

The *Banco do Nordeste's CrediAmigo* program is an exception. Its solidarity group lending methodology exempts borrowers from the cosigner requirement, which enables even very low-income groups to access loans. However, the solidarity group mechanism is not favored by all; the idea of taking responsibility for the commitments of others is not uniformly accepted by those interviewed.

The reservations expressed vis à vis solidarity group lending may be explained by the uneasiness of having to be responsible for someone else. It is more than a question of trusting one’s fellow group members. The process involves a transfer of responsibility (from the co-signer to the group) that is viewed with discomfort. Further, it is a question that involves money, which contributes to the reservations people express with regard to the idea. While there is a considerable spirit of solidarity in the communities studied and neighbors voluntarily offer help in times of need, money is something very delicate that is difficult to control. An inconclusive business deal, a client who pays late, an accident in the family—such situations can leave even the most honest and well-intentioned person incapable of making a payment. The burden of the unforeseen then falls on the other group members, who are already struggling to pay their own debts. It is one thing to evaluate your friend’s honesty, and quite another to accept the weight of risks that are out of one’s control.

### Cashing in post-dated checks

Little mentioned in this study, cashing in post-dated checks is a service offered by a few banks and *agiotas*, and is well appreciated by those who need to advance payments. The service is used by microentrepreneurs who accept post-dated checks from clients. Banks and *agiotas* will offer cash-advances on these checks, discounting interest that is proportional to the number of days remaining until the check will come due, as well as a transaction fee. If the check is not paid, the microentrepreneur must reimburse the amount received, either up front or in installments, with interest. Check cashing is fast and involves little bureaucracy, but involves relatively high interest rates equivalent to those charged by *agiotas* or bank overdraft facilities.



## Checks

For those who have a bank account, the **post-dated check** is widely used in order to “buy time” to pay off purchases. People who do not have a bank account frequently borrow checks from friends or family. Post-dated checks are considered practical. They offer immediate credit with few requirements. Usually, post-dated checks are used once a certain level of trust has been established between the client (who has previously purchased with cash) and shop owner. Terms are generally very short, between 10 and 20 days. Many people assert that there is no interest on post-dated checks, although it is widely recognized that one can receive a 7% - 10% discount if the purchase is made up-front. Microentrepreneurs of higher income levels tend to negotiate longer terms of 30, 60 and 90 days with their suppliers, and willingly pay clearly expressed interest rates in order to do so.

<p style="text-align: center;"><b>Check</b></p> <p>Must have bank account. Minimum income requirement—of—R\$ 0 – R\$ 1000, depends on institution. Clean credit history. Receiving check book depends on account activity and approval from manager.</p> <p style="text-align: center;"><b>Cheque especial</b></p> <p>Must have bank account. Minimum income requirement—of—R\$ 0 – R\$ 1000, depends on institution. Clean credit history.—Credit limit depends on account activity and median balance.</p>
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Post-dated checks are perceived as a form of payment with a grace period. They are viewed as practical, and entail little bureaucracy, once the account is open. Use is somewhat limited since most sellers will accept this kind of payment only after a relationship of trust has been established.

It is widely believed that that payments with post-dated checks do not incur interest, and, in reality, there are cases where up-front payment is the same as deferred. However, in the majority of cases, the interest rates are calculated and camouflaged in the final price. Even when there is a “discount” for up-front payment, most people continue to assert that there is no interest on checks post-dated 15 or 20 days. For the microentrepreneurs who work with longer terms, the interest rates that accompany the use of post-dated checks are visible and fully accepted, as they are considered to be less than those of other deferred purchase options.

**Cheque especial** is an overdraft facility offered by banks for account holders. The credit line extended to the *cheque especial* user is proportional to the median balance maintained. In practice, *cheque especial* is used much like a credit card, although the term is generally much shorter than available for credit cards. *Cheque especial* can be written for much higher sums than regular post-dated checks, since they are “guaranteed” by the bank. Their use is limited among the populations studied. Among the few people with bank accounts, even fewer have access to *cheque especial*.

Just as with credit cards, a number of those interviewed are very wary of the use of post-dated checks and *cheque especial* out of fear of losing control of spending and not having sufficient resources in the bank account when the payment comes due. The fear is even greater due to the difficulty to negotiate late repayment. When a check bounces, the user not only faces penalty charges, but is discredited vis à vis the person who received the check and may eventually be forced to close his or her bank account. There is also the fear that the check will be deposited before the planned date, which can lead to the same problems.

## Payment plans

Payment plans proposed by large retailers is by far the most commonly used form of credit among the populations studied. Mainly used to purchase furniture, appliances, clothes and shoes, payment plans are nonetheless available for almost anything. User appreciate them mainly because they involve very little bureaucracy (although requirements are not very different from those of other financial services), and they offer the possibility to make payments over a relatively long period which makes for small installments that are within reach of the users. While it is widely recognized that in the end, payment plans bring the final price up significantly compared to buying up-front, the interviewees consider payment plans

"I know that it's going to cost double, but the installments are small and I manage to pay them."

as "the only way of buying what you need." Payment plans

**Payment plans from large merchandisers**  
CPF, ID, proof of residence, proof of income (sometimes may be substituted by proof of payment of previous purchase made with payment plans). Clean credit record.

enable low-income populations to access consumer goods that, otherwise, would be very difficult to acquire. What counts, with this kind of service, is the size of the installment and not the end cost of the good. Payment plans are so favored that those who do not fulfill the requirements necessary to access them end up purchasing goods in the name of their families and friends that do.

## SEMI-FORMAL CREDIT SUPPLY

In this study, semi-formal credit is defined by the following:

### 1. The requirements:

- ▶ Few documents are necessary (CPF, pay stub/proof of reimbursed payment plan, in the case of *agiotas*) to access credit. In some cases, no documentation is necessary at all.
- ▶ A clean credit record is not necessary: there is no name verification with the credit protection agencies.

2. There is a **personal relationship** between the borrower and lender. In general, there is no written contract or receipts that register the operation (except in the case of payment plans made in small stores and certain *agiotas*).

### 3. The terms and conditions vary greatly

- ▶ Amounts: R\$ 10-R\$ 2000;
- ▶ Repayment: biweekly or monthly;
- ▶ Terms: usually 1-4 months;
- ▶ Interest rates (not including fees, late payment penalties): 0-45%/month.

### Services used in the formal sector

LUMP-SUM CREDIT	USE
salary advance from employer	***
loan from <i>agiota</i>	***
cashing-in of post dated checks with <i>agiota</i>	*
loan from the workplace <i>caixinha</i>	**
INSTALLMENT CREDIT	
payment plan from small retailer	*****
supplier credit	*****

### Salary advance from employer

For salaried workers (formal and informal),<sup>21</sup> **salary advances** are common. In some businesses, the concession of advances is very much regulated: they are accorded on specific days and for a limited amount, proportional to the salary.

It is also common (though less so) to take loans for larger amounts, paid over a longer period via monthly deductions to the salary. Usually there is no interest on these kinds of loans, but they are generally conceded only when the need is very specific: times of emergency, to pay off a specific debt, make home improvements or purchase some needed consumer good. A conversation between the borrower and employer or director of the company (in small firms) is necessary to approve the advance. Since repayment is made through salary discounts, there are no requirements or guarantees. What determines the concession of an advance is the personal relationship between the borrower and lender, or, in some larger firms, a specific policy.

### Agiota

Little appreciated but widely used, **agiotas** are present in all the communities studied. The level of formality (i.e. requirements to access loans) of *agiotas* varies, depending on to what extent the *agiota* relies on moneylending activities to support his livelihood, the amount of the loan and how well he knows the borrower. Interest rates of 20% per month are the rule. In São Paulo, it is common for “professional” *agiotas* to demand a pay stub, proof of income, proof of a payment plan that has been reimbursed or some other form of guarantee that the borrower has income. “Amateur” *agiotas* may not require any documentation at all, depending on the social distance between he and the borrower.

In case of non-payment, it is not uncommon for the *agiota* to seize some household good or even take

<p><b>Loans from agiotas.</b> CPF, ID, proof of residence, proof of income (can be substituted by a <i>contracheque</i>, proof of reimbursed payment plan, or other).</p>
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<sup>21</sup> Formal workers have *carteira assinada*, informal workers do not.



control of the borrower's magnetic bank card if s/he has one. While no one could cite a death in which an *agiota* was directly implicated, everyone asserts that violence and threats are common recovery tactics.

*Agiotas* are greatly disliked not only because of the high interest rates but also the high risks (violence, seizure of household goods) involved in case of non-payment, which are considered disproportional to the amount borrowed.

### **Workplace *caixinhas***

Found almost exclusively in formal workplaces, ***caixinhas*** are accumulating savings and credit associations organized by salaried employees. They are relatively common and very much appreciated by their users. This study identified two forms of *caixinhas*.

In the more informal version, a group of employees comes together to create a fund into which they all deposit a pre-determined sum on a monthly basis, usually on payday. Administered by one or several members, the funds are occasionally used to finance parties or gifts for colleagues (upon departure, birth of a baby, etc.). The *caixinha* also works as a revolving loan fund from which members who have contributed can receive loans at very low or no interest. Some *caixinhas* lend to non-members at higher interest rates.

In more formal *caixinhas*, the employer offers employees the option to have a fixed amount of the employees' paycheck deposited into the fund on a monthly basis. Employees are then able to take low-interest loans from the *caixinhas*.

In both cases, the principle and any profits are re-distributed to the participants at the end of the year, in proportion to the monthly contributions of each one.

The *caixinha* is categorized as semi-formal because they take place within the workplace where the guarantee and repayment mechanisms are bound to the receipt of salaries. The deposits and loans from the fund are made on payday, which makes it practically obligatory to follow through on the commitment to repay. As such, as in the informal sector, there is no credit record check.

*Caixinhas* are greatly appreciated by the users, due to the relative ease with which one can take a loan, and also because any interest paid reverts back to the borrowers at the end of the year.





## Payment plans from small retailers

The popularity of **payment plans** is not restricted to large retail merchandisers. Small neighborhood stores also offer a more informal version of this facility, which is widely used among the populations studied. While shopkeepers may request a pay stub or proof of residence, few requirements are necessary to purchase a good on a payment plan in small retailers. Notably, there is no credit record check. The amounts financed are less than with larger merchandising chains, and while many of the small retailers charge interest, the rates are lower and are generally imperceptible to the buyers. Very low-income populations greatly appreciate this service because of its accessibility, facility and rapidity, although the client must be a regular customer before he or she can use it.

Payment plans from small retailers  
Proof of resident, Verbal declaration of income

## Supplier credit

**Supplier credit** is one of the most commonly used forms of financial services among microentrepreneurs. Very few dispose of sufficient capital to purchase stock up-front with cash and for many of the interviewees, supplier credit is considered the only reasonable option for renewing stock without compromising the business' liquidity. Access requirements rarely go beyond a good and relatively long relationship with the supplier. The microentrepreneur's address is usually already known to the supplier, since purchases are delivered directly.

Supplier credit is classified as semiformal despite the informality of many of the microentrepreneurs who use it because it is necessary to have a structured business that the supplier judges sufficient to generate the resources necessary to pay off the debt. In this sense, the business serves as a guarantee for the credit.

According to those interviewed, suppliers generally do not charge interest for purchases of up to 45 days, and do not offer discounts for up-front payments. The use of post-dated checks however usually involves a 6%-7% increase in the price for payments of up to 30 days and 10% per month for longer terms. Terms are short, and rarely surpass three months. Supplier credit is greatly appreciated by the users due to the possibility to renegotiate payment when household emergencies or a lull in activities make it difficult to reimburse on time.

## INFORMAL CREDIT SUPPLY

Informal sector credit is distinguished by the following:

1. The **requirements**:
  - ▶ No documents required;
  - ▶ No credit record check.

2. A **personal relationship** between the borrower and lender. **Absence of written contracts or receipts.**
3. **Terms and conditions:**
  - ▶ Amounts: R\$ 10-R\$ 200;
  - ▶ Repayment: biweekly;
  - ▶ Terms: 1 month;
  - ▶ Interest rates (not including fees, late payment penalties) 0—5%/month.

**Services used in the informal**

LUMP-SUM CREDIT	USE
loans from family and friends	****
INSTALLMENT CREDIT	
informal store credit ( <i>pendura</i> )	*****
“borrowed credit”	*****
<i>sorteio</i>	**

**Loans from family and friends**

**Loans from family members and friends** are extremely widespread and the most commonly used for of lump-sum credit. Loans are characterized by small sums (R\$ 100) and very short terms (rarely more than 30 days). Larger loans, repaid in installments, are not unheard of but rare: relatives and friends usually do not dispose of the resources to lend larger amounts.

“ It is not good to take loans from neighbors. If you delay the payment for five days, the whole neighborhood knows you owe some money.”

“I count more on people that I dont know than on my family. The lady of the house lends to me, but only when I really need it.”

The advantages of rapidity, zero interest and no bureaucracy are counterbalanced by the disadvantages of small loan amounts and terms, and the ill-ease that borrowing from family members can cause. Interviewees often pointed out that a refused loan request or not being able to repay the loan on time can create a very uncomfortable situation. As such, taking sizeable loans from members of one’s social circle is avoided when possible.

**“Borrowed Credit”**

Those who are unable to meet the requirements necessary for accessing payment plan facilities—a clean credit record, for example—almost systematically **borrow credit** from the friends or family members who do have access to credit cards, checks or payment plan facilities.



This practice is relatively common, since purchasing on credit is considered the only possibility for low-income populations to access consumer goods. Those who “lend” their name are fully aware of this reality and rarely refuse to help out a friend or relative who solicits this kind of favor.

“Lending” one’s name, however, only works if there is relationship of trust between the borrower and lender. The non-payment of installments has serious consequences: either the lender must pay the installments, or be registered as a defaulter with one of the credit protection agencies. Stories of non-payment do occur and lenders suffer the consequences, but this does not appear to lessen the practice; people are just more careful.

“A friend took out a payment in my name, but only paid the first 3 installments. I had to pay the rest. Now, I only do this for my children or my brother.”

Moreover, lending one’s name has an up-side. The repayment of payment plans helps build a good credit history, strengthening one’s reputation as a good payer.

### Informal store credit (*fiado or pendura*)

Known as **fiado or pendura**, informal store credit differs from payment plan services in that there are no installments and no documentation required at all. Interest may be charged, but it is not the rule. Purchasing on credit is simply the process by which one can acquire a good with a very small up-front payment, or none at all, paying off the rest 15 or 30 days later. Purchases on credit vary from R\$ 1 e R\$ 50, rarely more. In the low income communities in Recife, the *botijão de gás* is frequently bought on credit. Paid up-front, the price is R\$ 18, purchased on credit, the cost raises to R\$ 20.

Purchasing on credit is very common, especially among the very poor. Among these groups, purchasing *fiado* is the only way they can acquire basic goods like food, gas or medicine during the low period of the month. For these populations, credit signifies more than just a financial transaction; it is the fine line that separates citizenship and marginality.

*Fiado* is the most sacred form of credit for the very poor. Only regular clients that consistently pay off their debts can buy on credit. Losing the right to buy on credit in the neighborhood store is to lose the last recourse that enables one to survive with a minimum of dignity. Not only would it be impossible to purchase the basic necessities, but the news of defaults spreads rapidly, marginalizing the debtor within his or her own community. Consequently, non-payment is rare. It is either calculated (those that plan to move from the neighborhood, for example) or due to a total incapacity to repay. For microentrepreneurs, selling *fiado* is obligatory. Refusing to do so would lead to a significant loss of clients. Only alcoholic beverages are the not sold on credit.

“You have to sell *fiado*. I don’t like it, it creates a lot of problems, but if you don’t sell *fiado*, sales stop.”

“We sell on credit because the person needs to take food home to the kids.”

“If you don’t have money, you don’t drink. A guy wants to drink on credit, but then he gets drunk and forgets how much he drank...it just creates confusion...I never sell drink on credit.”



## Sorteio

Sometimes known as *caixinha*, the **sorteio** is the Brazilian version of rotating savings and credit associations that are found in various forms around the world. Identified among women in Recife in this study, *sorteios* are composed of ten or twelve members, each one contributing a pre-established amount to a “pot” at a fixed frequency during a set period of time. Each meeting, the sum of the pot will go to one member, determined by picking a number at the beginning of the *sorteio*. All the members continue contributing to the *sorteio* until the end of the cycle. Only the organizer does not pick a number, the standard rule being that she will be the first to receive the pot. The organizer is responsible for choosing the members as well as covering any losses incurred in case of default. This form of systematic pooling of money serves both a credit and savings function, depending on one’s placement in the cycle.

*Sorteios* are generally monthly affairs, but occasional weekly or bi-weekly *sorteios* are formed, depending on the organizers needs and capacity. Contributions vary: R\$ 10 seems to be the most popular although R\$ 50 and R\$ 100 levels also exist.

The preference for placement in the rotation cycle is not uniform although more people appear to prefer to receive the pot first rather than last. This is mainly due to the fear that the other members may not fulfill their commitment to contribute each time. However, it appears that such occurrences are rare, and in such worst-case scenarios, the organizer pays the difference.

Completely absent of bureaucracy or specific access requirements, *sorteios*, like all of the other informal financial services described here, are based on personal relationships of trust.

## SAVINGS AND INSURANCE

### Forms of saving

<b>FORMAL</b>	contractual savings	*
	passbook savings	**
<b>SEMIFORMAL</b>	workplace <i>caixinha</i>	**
	funeral insurance	*
<b>INFORMAL</b>	<i>sorteio</i>	**
	in kind	***





Savings behavior is very undeveloped in the populations studied. Despite the availability of passbook savings to most anyone (the *Caixa Econômica Federal* requires CPF, ID, proof of residence and R\$ 10 to open a passbook account), it is used by only a small portion of the population studied: the money that could eventually be put aside is so little that it just isn't worth it to deprive oneself of a bottle of beer or a night of dancing just to save a little bit.

"Savings. Who can manage to save? Nowadays, even little kids can't manage to put a coin in the piggybank..."

Contractual savings (*títulos de capitalização*) are equally rare. Banks encourage such products by "marrying" them with other (usually loan) products as well as proposing monthly or weekly "lotteries" that offer savers the chance to win monetary prizes. Contractual savings products are considered more attractive than savings passbooks due to their obligatory nature (one is forced to build up a reserve, viewed as desirable but very difficult when it must be done spontaneously) and the possibility of winning a prize. Even taking into account the penalties for early withdrawal, contractual savings are considered more advantageous than passbooks. Nonetheless, the fear of not being able to save the necessary amount every month and the extremely low interest rates offered on such products dissuade the majority of the people interviewed from using such products.

**Savings in-kind** is by far the most frequent form of savings. When money is left over, it rarely finds its way to a savings passbook or even under a mattress. The purchase (via payment plans) of stock (for microentrepreneurs), a new television, a freezer, or some other household good is the most common way to invest liquidity.

Attitudes regarding savings involve contradictory aspects. In theory, everyone would like to save (in cash). In practice, however, very few people do and of these few, contractual savings mechanisms such as *títulos de capitalização*, *sorteios*, or *caixinhas* appear to be the most common way to do so. Very small amounts may be kept around the house, but are generally spent as soon as they amount to anything.

The populations studied say they do not save because there is nothing to save at the end of the month. When a little something *is* leftover, it is immediately used to purchase stock (for microentrepreneurs) or spent on a leisure activity. In addition, interest paid on savings passbook account is negligible, especially compared to those of the past when rates of 50%, 60% per month were common (referring to the adjustments made during the inflationary period). "Back then, it was worth it to have a passbook savings account."

"Banks charge interest rates of 7, 8, even 10% per month and pay 0,5% or 0,6% on savings. It's absurd!"

*Caixinhas* and *sorteios* were the most commonly used forms of cash savings identified in this study. The savings aspect of these mechanisms is just as valued by users as the credit aspect, and just as with contractual savings products, their obligatory nature is seen as positive. Without this obligation, the majority declared they would not make the effort to save.





## Insurance

Insurance products are essentially inaccessible for poor families. In the populations studied, only two or three participants had used some kind of insurance, usually “pushed” upon them by banks when taking a loan. Insurance is nonetheless highly desirable. In particular, health insurance, available only for the rich and those who have benefits through work, is a dream for the majority of the people interviewed.

Groups in Recife revealed the existence of a funeral insurance offered by at least one funeral home in the city. Clients pay in R\$ 5 and R\$ 10 per month for a fixed period of time (several years) to cover funeral costs at the time of the beneficiary’s death. This type of service was considered very accessible to low-income populations.

## TENDENCIES IDENTIFIED

There is a clear preference for installment credit, especially payment plans, in the populations studied. Despite the variation between the different types of installment credit (for example, the difference in interest rates using a post-dated check vs. *fiado*), we can identify a number of attributes that are in general shared by the different forms and account for this preference. Conversely, the relatively light use of lump-sum credit can be explained by a number of characteristics that are considered particularly negative by the interviewees. In addition to these observations regarding credit, this study has identified a capacity to save, although not a willingness.

### The preference for installment credit

Installment credit is by far the most frequently used by all low-income populations, since even those who do not have direct access will “borrow” the name of others.

While it is widely recognized and understood that buying on payment plans is in the end more costly than taking a loan, when the choice is available it is rarely made in favor of a loan. Equally curious is that, all the time asserting that they have no money to save, poor families are constantly paying off a debt for a previously purchased item. Were they able to ‘get ahead of the game’ at one point, this debt could eventually transform into savings, i.e. the money that is currently budgeted for debt could go towards savings, which could be used to purchase at a cheaper price what normally would be bought on a payment plan.

The choice to use installment credit rather than take loans can be understood, in part, from a cultural perspective. In the language of the populations studied, *crédito* usually refers only to installment credit while *empréstimos* (loans) refers to lump-sum credit. In the more restricted sense of the term, *crédito* signifies facilitated forms of payment of goods or services that do not involve a physical transfer of cash from the lender to the borrower. In the case of *crédito* what is being bought is the good or service although for a higher cost. In the larger sense of the word, *crédito* is associated with normal behavior, with the habit of meeting obligations. On the other hand, *empréstimos* are perceived strictly as a concession of money from the creditor to the debtor. A loan operation involves the purchase of money for an amount higher than the face value.



In this respect, the conclusions of Gallagher, et. al's qualitative study of demand for microfinance in Rio de Janeiro are similar: to purchase on credit means to acquire the time needed to bring together the right conditions to be able to make the payment. What is being negotiated is *time*, and in the minds of the majority of the microentrepreneurs, there is little correlation between purchasing on credit (a question of time) and loan operations (a financial transaction).

There are also some differences in the process of negotiating. *Crédito* is something "natural," simply a different, more common way to purchase a good. *Crédito* does not need to be "requested" or justified; suffice to satisfy the requirements. Loans involve "abnormal" behavior. The norm would be to have the money, either to purchase something up-front or in installments. With the exception of personal lines of credit offered in banks, loans must be "requested" and justified, involving more complicated negotiations, stricter access requirements and more bureaucracy than *crédito*.

Finally, installment credit enables the immediate acquisition of goods, something that is extremely valued in Brazilian society. On the one hand, it is a question of necessity: if it were not possible to purchase groceries on the store credit card, many houses would go without food. On the other hand, there is a very strong consumer culture in Brazil. The recent increase of the purchasing power of low-income populations has further fueled this culture. With inflation under control, stable prices and relatively low interest rates (thanks to the *Plano Real* of 1994), poor families are able to access consumer goods and services via credit, now that it possible to calculate regular installments. Further, television advertising is widely used to communicate the message that consumption is the sign of success, a means to "happiness."

### Characteristics most appreciated in installment credit

In addition to this cultural explanation, installment credit presents a number of attributes that are highly appreciated by the populations studied, namely accessibility, availability, rapidity, adaptability, service, transparency and the possibility to renegotiate.

- ▶ **Accessibility.** While purchasing on a payment plan almost always requires some sort of formalized procedure involving handing over one's CPF or proof of residence, requirements are considered realistic. Many large merchandisers require nothing more than proof that the client earns the minimum wage and occasionally even this may be substituted by a payment plan that has been reimbursed in full. In addition, once the initial bureaucracy—i.e. the initial presentation of required documents—is out of the way, subsequent purchases are as easy as purchasing up-front with cash.
- ▶ **Availability.** Most everything can be purchased with installment credit, almost any consumer good as well as most services. It is available as long as the store is open and almost all stores offer the option.
- ▶ **Rapidity of transactions.** Purchasing through installment credit is so common that the transaction is no different from up-front payment. Once registered in the store's system, the buyer does not need to wait for approval. The good can be taken home immediately, oftentimes without even paying anything up-front. This rapidity is highly valued by the populations studied.





- ▶ **Adaptability in terms and installment sizes.** Installment credit is adapted to one's financial needs: most stores offer a variety of payment plans (6-12-18-24 months), including what day of the month the client prefers to pay. This adaptability allows clients to choose repayment schedules that suit their capacity and willingness to repay. The size of installments is one of the most valued aspects of store payment plans. While clients may have the income to pay off the item in 12 months, many opt for the 24-month plan. Being in debt is part of life for most low-income families, and they feel more secure paying off very small amounts for a longer time than having to "tighten the belt" during a shorter period.
- ▶ **Service.** The interviewees underlined that that want to be treated with dignity, respect and courtesy, just as the rich are. The feeling that poor people are mistreated by banks and financial institutions in general is very strong. Stores that offer installment credit expect to serve low-income clients and their service reflects this: the relationship is one of equality, the buyer is treated as one of the parties in a business deal, on the same level as the other.
- ▶ **Transparency.** Interviewees appreciate when conditions are clearly presented before the deal is closed: due-dates, installment size, taxes and administration fees, etc. Installment credit by its very nature is usually quite clear in these aspects: stores often have charts hanging up to show the payment plans available and the corresponding installment amounts to chose from. On the contrary, when taking a loan, interviewees felt that information is rarely presented clearly. Clients feel like they have been tricked when told the first installments will be x amount, only to discover that subsequent installments are more due to the inclusion of interest or some other fee that they had not understood would be included.

It appears preferable that financial fees be presented as a fixed amount and not a percentage. This was illustrated by the fact that the majority of the interviewees that had taken loans could easily remember how much the installment was (including which part was principal and which part was interest), but rarely the administrative fees included, unless the latter was expressed as a fixed amount.

- ▶ **Possibility to renegotiate.** For microentrepreneurs, one of the reasons supplier credit is so appreciated is because repayment can generally be renegotiated when necessary. A slow-down in sales, an accumulation of post-dated checks or a household emergency are considered acceptable motives for negotiation, if the relationship between the supplier and buyer is good. Interviewees that had taken bank loans also underlined the importance of "being friends" with the manager, in order to renegotiate loans more easily. That it is nearly impossible to negotiate credit card debt or loans from consumer-lending agencies<sup>22</sup> is seen as one of the main disadvantages of these services, in addition to interest rates and penalty fees.

<sup>22</sup> Consumer-lenders nonetheless occasionally engage in collection campaigns that involve renegotiation of all overdue loans, and one interviewee explained that if one leaves credit card debt long enough, renegotiation becomes possible, albeit after a passage in the courts and a relatively long legal process.





## Characteristics least appreciated in loans

In addition to the cultural perceptions outlined above concerning taking loans, there are several specific characteristics that are highly disliked in the loan process.

- ▶ **High interest rates.** The most typical argument used to justify the disinterest in taking loans is the high rate of interest that comes with borrowing money. Consumer-lending agencies, *agiotas* and credit cards are the financial services most commonly cited as having the highest interest rates. While the majority of those interviewed appear far more concerned with installment size than interest rates, the overall cost of a loan-how much is paid in interest-is examined closely. The majority of those interviewed felt that 3% per month is a reasonable interest rate for loans.

The interest rate question is more complicated than meets the eye, however, since some people are willing to pay 20% per month to access loans from an *agiota*. In addition, while the interest rates charged for purchasing goods on a payment plan can be just as high as those in consumer-lending agencies, the interviewees rarely complain. Another point to consider is that zero interest loans from family members and friends are not the most preferred form of borrowing. Clearly, while interest rates should be as low as possible, it is important to underline that clients accept to pay for a service they consider valuable.

- ▶ **Bureaucracy.** The word bureaucracy is used to describe the entire process that involves the credit operation: filling out the application, providing the documents required, and the time it takes to approve and receive the loan. The initial bureaucracy required to start the operation is considered irritating and is a inhibitive factor for those looking to access financial services. It is nonetheless accepted, since it is understood as a necessary part of the process. However subsequent bureaucratic procedures-having to present a piece of paper in order to make a payment or fill out some document upon receiving a loan-have no justification in the eyes of the interviewees. The operation should be practical, simple and fast, as it is with credit cards, for example.
- ▶ **Misleading propaganda.** The feeling the one is being tricked or misled with false or incomplete information regarding the terms of negotiation (installment size, overall cost of loan, late payment modalities) is greatly disliked. Consumer-lending agencies, banks, credit card issuers and MFIs are pointed to as guilty parties in this area.
- ▶ **Co-signer requirement.** The co-signer requirement is apparently very hard to meet. No one wants to be a co-signer. It is hard enough to be responsible for one's own debt, let alone someone else's. Further, finding someone with sufficient income to be a co-signer is not easy. Agreeing to co-sign a loan is to offer a favor. The borrower is doubly indebted: on the one hand to the lending institution, on the other to the co-signer. Dependence on the co-signer does not end once the loan has been repaid. On the contrary, it continues indefinitely, until the favor has been returned.

Having to seek the guarantee of someone else leads to a sensation that one is incapable, irresponsible or dishonest (Why does someone else have to be responsible for my actions? Don't they trust me? Do they think I won't pay? I always fulfill my obligations!) The interviewees asked why other guarantees, like their personal goods or equipment, are not accepted in the place of the co-signer.



## The capacity and willingness to save

Despite the clear shift taking place in microfinance from credit-based services to savings-based services in light of recent works on what poor people want and need, this study did not observe an overwhelming desire or willingness to save.

While interviewees systematically maintain they cannot save, they nearly all manage to set money aside in order to pay off an ever-present debt, acquired by purchasing goods with installment credit (payment plans, post-dated checks, credit cards, etc.). This behavior could be expressed saving down<sup>23</sup>, and demonstrates the capacity to put money aside when necessary (or desired). In this study, while the capacity to save seems apparent, it is not clear that the populations WANT to save, or perhaps more precisely, the benefits clearly do not outweigh the sacrifices.

Savings takes time, there is no immediate gratification. It is contrary to the consumer culture that is so strong in Brazil. And savings means putting money away, where it cannot be seen, in a place governed by incomprehensible rules and regulations that has a mixed reputation when it comes to dealing with the poor. Based on consumer behaviors and discussions from this study, a physically identifiable and transferable item that can be sold or given as a gift has far more appeal than a deposit slip from a bank that is not entirely trusted.

"We live in a capitalist country.  
You can't just keep your money  
under a mattress"

Nevertheless, the existence of *sorteios*, *caixinhas* and the funeral insurance scheme encountered in Recife is proof that savings behaviors do exist when the conditions are considered favorable and the outcomes beneficial. It appears that obligation is generally viewed as something positive and necessary, at least to initially encourage savings.

<sup>23</sup> As suggested by Rutherford (1998).





## **CHAPTER III FINANCIAL NEEDS AND STRATEGIES**

This chapter will examine the occasions-emergencies, life-cycle events and opportunities-that require low-income populations to pool together relatively large sums of money. These events, identified by the interviewees as illness, death, family celebrations, educational opportunities, house repairs and starting/investing in a business, create more or less acute financial necessities. Commonly experienced by the overwhelming majority of the population studied, they are nonetheless exceptional in nature, as they do not occur on a regular basis.

Populations also identified a number of seasonal events-year-end festivities, Carnival and São João festivals, income taxes and the beginning of the school year-that put financial pressure on households and businesses. Although the sums required for these seasonal events do not necessarily debilitate budgets, understanding their importance provides important insights into the seasonal flux of repayment capacities.

These financial needs and the mechanisms populations use to satisfy them are presented in the form of a matrix, categorized according to 1) types of events: emergency, life-cycle, opportunities and seasonal and 2) income levels: very low, low and medium low. Within each category, the events are listed in descending order of financial pressure: those at the top affect household budgets the most due to their obligatory nature while those at the bottom have a lesser effect on household expenditures. There is no relationship between the categories, i.e. the costs involve in starting a business (classified near the bottom under opportunity) may be greater than the costs related to celebrations (classified above under seasonal events). Mechanisms are listed in descending order of usage.

An analysis of each event follows: its relative importance, the costs it can involve and the main coping strategies to manage it. This section will conclude with a discussion of the principal tendencies identified among the different populations studied.

FINANCIAL NEEDS AND MECHANISMS USED				
EMERGENCIES		Very low-income	Low-income	Medium-low income
		Illness, Health Care Costs	family/friends <i>agiota</i> fiado sale of household good	relative employer sale of household good consumer-lending agency <i>agiota</i>
LIFE-CYCLE EVENTS	Funeral Costs	"collection" from neighbors family/friends financing plan from funeral home	family/friends financing plan from funeral home <i>agiota</i> funeral insurance	family/friends financing plan from funeral home cash advance from credit card bank credit line
	Wedding	savings	savings family/friends	savings family/friends payment plan bank loan
	Other celebrations	savings borrowed credit <i>fiado</i>	savings payment plan	savings payment plan
OPPORTUNITIES	Home improvements	salary advance borrowed credit <i>sorteio</i>	salary advance <i>caixinha</i> bank loan	bank loan <i>caixinha</i>
	Education	use not identified	family/friends	family/friends bank loan
	Start up business	use not identified	indemnities from previous employment	indemnities from previous employment
	Expand business	use not identified	payment plan credit card check <i>agiota</i> MFI loan <i>sorteio</i>	payment plan bank loan credit card check MFI loan <i>sorteio</i>
SEASONAL	End of the year	borrowed credit <i>fiado</i>	payment plan <i>caixinha</i>	payment plan <i>caixinha</i> post-dated check overdraft facility credit card bank credit line
	Carnival & São João	<i>fiado</i> family/friends	payment plan family/friends	credit card post-dated check
	Income taxes	use not identified	use not identified	installments
	School-related costs	family/friends	payment plan post-dated check	payment plan post-dated check credit card



## EMERGENCIES

In this study, illness (including accidents) was identified as the situation that creates the most financial pressure in the household.

### Sickness

The costs incurred during illness are by far the most urgent for the population studied. Sickness is frequently unforeseeable. Any member of the family, of any age, can fall victim during any time of the year, and it is impossible to know how long it will last.

The costs of treatment can rarely be put off. For short-term illnesses, expenses range from R\$ 50—R\$ 300. An appointment with a private doctor is generally between R\$ 80 and R\$ 100. While there have been recent improvements in the public health system and it is easier now than a few years ago to be treated in case of emergency, the public system usually cannot meet the needs for medicine and laboratory tests, leaving poor families responsible for these expenses.

"I fell behind on my tuition payments at college because I used the money to treat an illness. Now I have a huge debt there."

To treat illness, the interviewees use anything they can come up with. Home remedies are commonly used first, and if they fail, family and friends who work in the public health sector are called upon, in an effort to have privileged access to a doctor or access medicine. Even when this tactic has good results, it is inevitable that income in the household budget will have to be reallocated, or a loan sought to cover the costs of medicine or tests.

Low and medium-low income salaried workers use informal store credit (*fiado*) to purchase medicine, or rely on family, friends or employers to take loans. In situations of extreme need, a domestic good like a stereo or television might be sold. Among medium-low income microentrepreneurs, the sale of a car or motorcycle is not uncommon.

Those with bank accounts pay for expenses with post-dated checks or cash-advances. Those without bank accounts frequently borrow credit. Loans from the *agiota* or consumer lenders are used only if all else fails. Interviewees note that despair overcomes reason and the fear of not being able to repay.

"You can't let your child die. You go to the *agiota*, take R\$ 50,00 and pay back 70,00 or 80,00."

Everyone interviewed would like to have health insurance but point out that the high costs of the policies available are prohibitive.

## LIFE-CYCLE EVENTS

This category refers to events that take place during the life cycle and that disrupt the household budget, increasing expenditures and creating the need to "scrape together some cash". The three events that appear to have the most effect on households are funeral costs, weddings and celebrations.





## Funeral Costs

After health care costs, a death in the family is the event that exercises the most pressure on poor families' budgets. There is an attitude of reverence and respect when it comes to the death of a relative that makes people feel obligated to prepare a final homage, a dignified burial. Funeral costs are estimated to be between R\$ 500 and R\$ 2.000, depending on the type of funeral. A death incurs a number of expenses: costs related to the death certificate and other paperwork (registry, attestation), the coffin and flowers, the transport of the coffin to the cemetery, etc.

"You can't have a second grade cardboard coffin. It has to be wooden. It costs more, but that's the way it has to be."

Among the very poor, it is common to go door to door in the neighborhood collecting contributions for the person in need. Community leaders like city council representatives and drug traffickers will commonly appear on the top of these lists. Payment plans offered by funeral homes are also frequently used. Costs are paid in the course of three to five installments, usually via credit card or post-dated checks.

"When my parents die, I will make any sacrifice necessary to give them a decent burial."

A few participants in the low-income groups in Recife mentioned a funeral insurance that is available. Contributions of R\$ 5 and R\$ 10, guarantee a dignified burial for the beneficiary.

When these options are not available or sufficient to cover costs, the interviewees turn to family or friends for small amounts, or consumer lenders and *agiotas* for larger sums. Those with access to banks use credit card purchases and credit lines.

## Wedding

Weddings also incur significant expenses. In addition to the ritualistic nature of this passage from one stage in life to another that is often commemorated with the most pomp possible in all cultures in the world, there is a desire on behalf of the parents to show they are able to honor their children with a celebration.

A wedding, however, is quite different from health care or funeral costs in a number of respects. Firstly, one only spends what one can spend. The range of expenses is huge, varying from R\$ 200 to R\$ 4.000. Large parties and honeymoons are as common as small ceremonies followed by modest or no honeymoons. Secondly, the majority of costs fall on the bride's family. Couples with only male children are generally less preoccupied with wedding costs.

Another phenomenon observed in this study is the decreasing importance of marriage among young people, principally in São Paulo. The instability of marriage and the high costs of a probable divorce lead many people to prefer to simply live together.

"Marriage today lasts very little. Two, three years and the couple already is separated. Divorce costs R\$ 2.000 or even more. Best way to do it is just hook up, no party, nothing."

Planning a wedding appears to be one of the few motives to save. Weddings are generally organized well in advance, which enables the families to prepare the trousseau or make down payments on some of the expenses well before the date. Other costs (presents, remembrances, renting space, food, drinks, clothing) can be paid in installments and shared among the families involved, decreasing the financial burden for the bride's family. Only the church and notary costs must be paid up-front.





Medium-low income microentrepreneurs and salaried workers sometimes take bank loans when wedding costs are elevated. In the lower income groups, however, taking on debt is avoided, except for those purchases made on installment plans. Savings in-kind, i.e. purchasing a good in advance that will be eventually given as a gift to the new couple, is common.

### Other celebrations and birth of the first baby

Other celebrations, such as birthdays, or first communion have less impact on family budgets. Despite the pressure kids put on their parents, it is possible to keep costs low, be it R\$ 100 or R\$ 1000. But no matter what, there must be a party. It is relatively common to throw a joint party, bringing together families to celebrate two birthdays that are relatively close in date, thereby sharing costs.

"The kids put on the pressure, and for us it's a pleasure to have a party for them."  
"You have to have at least a little party. Even if it's just cake, balloons and some drinks."

Gifts are usually purchased with a post-dated check on a payment plan. Costs for the decoration can usually be paid in installments in specialized stores. The food is generally made at home and the drinks can be bought on credit.

The birth of a child has a relatively strong impact on family budgets. On the one hand, a birth clearly incurs expenses. On the other, many of the expenses are foreseen and are prepared for during the pregnancy.

Further, the birth of a child is something shared by other relatives, neighbors and friends. A series of baby showers serve as a pretext to offer gifts (diapers, clothes, etc.) to the expecting family and help diminish the costs during at least the first few months of the baby's life.

Contrary to situations dealing with illness or death, the expenses connected to the birth of a new baby are made with pleasure. Indebting oneself either by taking a loan or purchasing with installment credit is thus less "painful" in this case. Cribs, strollers and clothes are bought with installment credit when not received as "hand-me-downs" from family or friends. Smaller purchases like food or medicine can always be bought on credit or with small loans from a friend or family.

## OPPORTUNITIES

In addition to crises and celebrations, opportunities-to get an education, make home improvements or start/expand a business-can also put pressure on family budgets.

### Education

The possibility to enroll one's children or one's self in a technical training course or secondary/higher education institution is an opportunity that sometimes arises but cannot always be taken advantage of. Inscription fees, materials and transportation coupled with the decrease in income that generally comes with being a student (less time to do paid work) make it difficult or impossible for low-income families to make the sacrifices necessary to pursue studies. Nonetheless, the desire to receive or to see one's child receive professional training was a very common refrain among interviewees.



For the few that make it to this stage of education, the costs are covered by the student's own income or by the parents who sacrifice personal expenditures. Very few interviewees of medium-low income take loans from banks or other entities that offer special education loans.

When it is not possible to cover costs, the solution is usually to suspend studies or quit altogether. The great majority of the participants in the focus groups did not know of or felt excluded from any specific mechanism that could be used to finance educational costs.

### Home improvements

Reforming one's house is an event that can weigh heavily on very low-income families who live in precarious, oftentimes "improvised" housing situations. While reform could be considered a life-cycle event, since at some point almost every family must carry out improvements in some form or another, very few people have the possibility to do reforms unless an opportunity (for example, cheap labor made available with the arrival of a cousin, needed materials available at a discount) presents itself. Costs vary, but are reported to be in the range of R\$ 300 to install a bathroom up to R\$ 2000 for an overall reform (redo the floor, roof, painting, etc.).

The medium-low income interviewees rely on financing to purchase necessary materials, especially from the *Caixa Econômica Federal (CEF)*, which offers a special credit line for home reforms. While installments are considered reasonable, users complain of having to provide three different estimates for the purchase of the desired material. This requirement is time-consuming and demands a lot of work, since rarely can all the needed items be found in the same store. Various stores must be visited for various products three times. Those who have access use bank loans and bank credit lines.

The low-income populations who do not have access to a bank and lack the motivation to work with the CEF manage only very slowly to make improvements. They must rely on the good will of the bricklayer or carpenter who charges less and allows deferred payment or the work themselves. Material is bought in small quantities and accumulated until it is possible to start the work. In cases of extreme necessity, when the living conditions present health or security risks, loans from employers, friends or purchase materials on credit.

While not common, *sorteios* were cited as means of pooling together cash in order to carry out reforms. At least one *sorteio* was organized with the specific objective to finance home improvements of the organizer.

In very low-income populations, the situation is similar to their low-income cohorts, only more dramatic. The need to make reforms is stronger and oftentimes more urgent. However, improvements can only be undertaken once basic necessities are covered, making for a long, drawn out process that depends mainly on opportunities like an unexpected gain or help from family and friends.





## Business start-up or expansion

To start a business, it is common to invest the indemnities received upon leaving a previous job<sup>24</sup>. Generally, this income takes several months to come through due to bureaucracy, thereby allowing the future entrepreneur to plan the business. Faced with a tight job marketplace, starting one's own activities is often viewed as a promising alternative. The study also identified a few cases where start-up capital is borrowed from a relative. In these cases, the activity developed starts small, with the entrepreneur selling some goods out of the home or working as an itinerant vendor.

For business expansion, microentrepreneurs cite the need for working capital, followed by capital for purchasing equipment. Since profits are generally small and end up being used to cover household expenses, microentrepreneurs point out that it is difficult to accumulate sufficient capital to invest in their business.

Traditional microcredit offered by specialized institutions aims to meet this very need, but is rarely used in the population studied. Many do not realize it exists, and those that do find it difficult to meet requirements: finding a co-signer, for example, is reported to be very difficult. Entrepreneurs rely mainly on supplier credit to increase stock, usually turning to loans from banks, *agiotas* or consumer lenders only when the cash upfront is absolutely required. The use of loans appears to be an exception rather than the rule. While most interviewees realize that they pay more for the facility of installment credit, they consider it to be the easier and most convenient option. As discussed in Chapter Two, the ability to negotiate payment with one's supplier is considered highly advantageous.

The feeling is not universal, however. Some participants would prefer to pay up-front and are willing to borrow to do so. However, most of them do not, citing too many requirements, high interest rates and fear of not being able to repay as reasons for not taking loans.

Medium-low income entrepreneurs working in service/commercial sectors use credit cards and *cheque especial* (overdraft facilities) to purchase large amounts of stock and only turn to banks if the occasion is "worth" it. Most lower income entrepreneurs do not meet the minimum income requirement necessary to access formal bank loans), and while consumer-lenders are within reach of most, the interest rates are exorbitant. In certain areas studied, a well-known *agiota* may be a source of financing (valued for rapidity if not for interest rates), but the practice is limited. Finally, while not a common source of capital, *sorteios* are sometimes formed to finance business expansion.

In the end, however, business expansion depends mainly on hard work, investment in stock and installment credit through a supplier, unless the opportunity is too good to refuse, in which case the bank, *agiota* or consumer-lender will be called upon.

## SEASONAL EVENTS

Year-end festivities, Carnival and São João<sup>25</sup>, income taxes and school supplies constitute the main annual events that put pressure on household budgets, forcing low-income families to spend more than usual and go into debt.

<sup>24</sup> Only workers with carteira assinada are eligible for this compensation.

<sup>25</sup> Popular celebrations during the month of June, especially important for people from the Northeast.





### Year-end festivities

Christmas and New Year's are celebrated in some way by nearly all the people interviewed. These two events are very important and immensely popular as they relate to tradition and religiosity of Brazilians. The commemoration of Christmas and New Year's Eve inevitably incurs expenses that push budgets over their limits. The expenditures for presents, Christmas Eve dinner, New Year's Eve parties, New Year's Day lunch may amount to little, but are considered obligatory. In addition, they are augmented by the purchase of new clothes or home improvements, most commonly undertaken at this time of year to prepare the house for the holidays.

Despite the flexibility of these expenses—"if there's not much money, the party is small"—at least some money is inevitably spent. Usually, family members will pool together whatever they can afford to cover costs; there was no mention of saving up for year-end events.

Salaried workers rely heavily on the year-end bonus salary (known as the *décimo terceiro*, or the 13<sup>th</sup> month) to help defer end of the year expenses, and, for those who take part, *caixinhas*. *Caixinhas* generally come to a close at the end of the year for the very reason that the month of December generally comes with an increase in expenditures.

Microentrepreneurs in commerce and service sectors see a pick-up in sales at the end of the year and consequently, an increase in liquidity. This liquidity is rarely taken advantage of, however, since January and February are usually slow months (clients are paying off debt contracted during the holiday season and have less purchasing power), and the profits from December need to be stretched out over the next two months.

The strategies used to realize end of the year festivities were similar among all the groups studied. The very low-income populations rely on installment credit: purchasing goods on informal store credit or payment plans in neighborhood stores. The objective is to keep debt to a minimum and expenses are controlled.

"Everyone has a party. And if we can't throw one ourselves, we go to the neighbors." The medium low and low-income populations are slightly more liberal. Installment credit in the form of payment plans, deferred credit card purchases and post-dated checks is very common, as is lump sum credit in the form of overdraft facilities and personal loans from bank credit lines. Expenses are nonetheless kept in check in order to provision for the months of January and February.

### Carnival and São João

Carnival and São João also mobilize a good portion of the populations studied, especially in Recife, although less than year-end celebrations.

"We try to spend only what we have. If we can't throw a big party, we have a small party, a cake, a few sodas and beer..."

São João appears to be more popular than Carnival, at least in this study. People of all ages and income levels take part in São João festivities, while Carnival is more celebrated among young people and those with higher income levels.





Despite being celebrated collectively, São João involves typical party expenses: food, drinks, games and toys, clothes. Further, it is common for city dwellers in Recife to return to their hometowns in the countryside to celebrate São João, resulting in travel expenses. Carnival-related costs are also minimal. Public festivals, parades and parties are promoted more and more by the state or municipal governments. For the reveling public, the bulk of Carnival expenses comes from alcoholic beverages.

As such, while leisure expenses are generally higher during Carnival (February) and São João (June) than during other months, they are generally not significant enough to provoke indebtedness. At most, one may ask for a loan from family and friends, make a purchase on informal credit or some other deferred purchase modality (post-dated check, credit card). Interviewees made no mention of banks, consumer-lenders or *agiotas*.

### **Income taxes**

For legalized microentrepreneurs, the beginning of the year brings the problem of income taxes.

Microentrepreneurs manifest disgust with regard to income taxes, considered very high and unjust. There is a strong belief that the money earned from taxes is badly administered, rarely reinvested to the benefit of the general population and microentrepreneurs, in particular.

When paying taxes becomes too difficult, the common solution is to put off payment, since the penalties are cheaper than the cost of money and negotiation of overdue sums by the government is a rule. Again, in this case, there was no mention of taking on debt to pay off taxes.

### **School-related costs**

While school-related expenses were commonly cited as a seasonal expenditure that creates pressure on the household budget, in many cases, it appeared that the preoccupation was based more on memories than on the current situation. While in the past the beginning of the school year often incurred relatively high expenses, nowadays the municipal or state government absorbs the majority of costs. Depending on the municipality, books, uniforms and lunch is provided at no cost. Nonetheless, in certain areas, back-to-school expenses can be significant, R\$ 50 – R\$ 100 per child. Given that January is oftentimes a difficult month due to debts accumulated in December, these expenses can create significant pressure on an already tight budget.

## **PRINCIPAL STRATEGIES**

In very general terms, the populations studied are using four principal strategies to manage their financial needs. Taking on debt, increasing income, accumulating physical assets and reliance on social networks appear to be the primary recourses.

The majority of financial needs are being met by **taking on debt**, either through loans or credit. Families reduce consumption to cover unexpected or extraordinary costs (and the debts acquired because of them) by sacrificing leisure activities or purchases considered superfluous like clothes and shoes (generally acquired though installment credit). Usually, one debt (from the clothing store) is replaced with another (at





the pharmacy). Sometimes, paying off an installment is prioritized over paying electricity and gas bills, since the suppliers of these latter services are generally lenient with late repayment. Lastly, food consumption may be reduced.

Working more and harder, taking on odd-jobs or getting involved in some commercial activity (selling cosmetics, sweets or crochet, for example) **to increase income** is also common, although rarely is the additional income enough to avoid taking debts.

Medium-low and sometimes low-income groups **accumulate assets**, such as stock, domestic appliances and vehicles. While not necessarily purchased with the objective to do so, consumer goods such as freezers, radios, television and furniture are necessarily often sold in emergencies such as sickness or death.

**Reliance on social networks**, be it family, friends or neighbors, is a critical management strategy for low-income populations. Oftentimes, social capital is the only capital they have, and the repayment of debt represents not only an obligation but an attempt to maintain, in some respects, their only source of capital: credit.

The reliance on social networks is also manifested in the borrowed credit phenomenon. Lending one's checkbook or credit card to a friend or relative or purchasing a television or refrigerator in the name of someone else who is registered with the retailer is an exceedingly common practice in both cities studied, although not without risk. Equally common are stories of the friend that exceeded the credit limit and could not pay back, leaving the card or account's owner to pay off debts that he or she did not incur. The risk is not a deterrent, however. Many interviewees who had been in such situations reported that they continued to be at the disposal of trustworthy friends and family members when necessary. The obligation to help out and the fear of being considered selfish by community members were the main motives.

## MAIN TENDENCIES AMONG THE POPULATIONS STUDIED

### Regional differences

Few differences were identified between the two regions studied. Overall, behaviors, attitudes, and financial management strategies were very similar, as were perceptions regarding financial institutions and services.

For reasons due to either culture or market landscape, a few products and mechanisms are more common or more frequently used in either one of the cities. *Caixinhas* were frequently cited in São Paulo, but totally absent from discussions in Recife. Conversely, informal *sorteios* were identified exclusively in Recife and not mentioned in São Paulo. The use of department store credit cards were far more common in Recife, due to an aggressive distribution campaign headed up by a large supermarket chain in the city.

Another product identified in Recife but not in São Paulo was funeral insurance. While it is possible that such a product exists in São Paulo, there was no mention of it in the various focus groups, despite the fact that funeral costs were frequently cited as one of the most important events during the life-cycle that created pressure on the family budget.





Financial necessities surrounding illness, funeral costs, end-of -the-year festivities and home improvements registered very similar levels of importance in the Northeast and Southeast. The costs related to the birth of a new child, education, income taxes and celebrations appeared to have a higher degree of importance in São Paulo, while Carnival, São João and wedding festivities appeared to have a greater impact on populations in Recife.

It is noteworthy that groups in the Northeast demonstrate a greater predisposition to the idea of solidarity group lending than groups in the Southeast. This difference may be in part due to the fact that in a number of groups in Recife, participants were involved in community associations and cooperatives. Nonetheless, even in groups where the level of social organization seemed to be weaker, it was not uncommon to hear of ROSCAs, which are based on a form of solidarity not very different from that proposed by MFI group lending.

Some attest that the lifestyle in the Northeast is characterized by a certain level of solidarity that has its roots in the customs of small towns located in the countryside. Since most urban dwellers in Pernambuco continue to keep close ties with their rural roots (the majority of residents in Recife were born in rural areas), these solidarity-based customs are kept alive even in the cities. Among the very poor populations interviewed in Recife, solidarity is very high, personal relationships being the only form of capital available to such groups.

In São Paulo, despite carrying out focus groups in communities where there were a significant number of Northeastern migrants, the level of solidarity among group members appeared weak. Group dynamics were weaker, rather restricted and closed. Even among participants that knew each other, there was not the same level of intimacy perceived in the groups in Recife. The cosmopolitan, individualistic, big-city lifestyle appears to spill out into the peripheries.

## **Occupation**

Microentrepreneurs/self-employed on the one hand and salaried workers/unemployed on the other appear to share certain financial management strategies and diverge with regard to others.

In general, microentrepreneurs express their financial needs in terms of working capital. Maintaining and increasing stock is viewed as critical for good business performance and growth. Those working in commerce, especially, believe that with greater and more diverse stock, sales will increase and as a consequence they will manage to “move up a rung” in the business ladder. In the minds of these microentrepreneurs, there is a direct relationship between the access to working capital to buy stock and the ascension from one level to the next. This notion manifests itself in the demand for working capital among microentrepreneurs of all levels: the itinerants want to move up to a stand, those with stands want to move into a store, and storeowners want bigger and better stores.

For microentrepreneurs working in industry and production, credit needs revolve around the acquisition of equipment, machines, tools, or, to a lesser extent, renovation of workshops. Similar to their service and commercial sector cohorts, these microentrepreneurs believe that there is space in the market to grow and succeed, provided they have a good product and a competitive advantage. All that is lacking, they feel, are the financial resources to help turn plans for growth into a reality. The problem is how to obtain this



financing since the sources accessible to them are limited, charge high interest rates, have too many requirements, or offer terms of payment that are too short and without a grace period-or all of the above.

For the both the unemployed and self-employed, (working informally in odd jobs or as itinerant vendors), credit is often seen as a way to “change one’s life”: start a small business (in the case of the unemployed and semi-employed), or improve working conditions with the better equipment and facilities (in the case of the self-employed).

Contrary to microentrepreneurs, who can count on their own hard-work and investment in stock as a way to grow, albeit slowly, unemployed and self-employed itinerant workers find themselves trapped in a vicious cycle that can only be broken with an injection of resources or external aid. However, they face the same difficulties as microentrepreneurs (high interest rates, difficult requirements), further aggravated by the fact that most financial institutions will only lend to those with a proven track record in a productive activity. In the absence of products and services that are accessible to them, a discussion regarding financial services with the unemployed and self-employed rarely reaches the point of analyzing interest rates or terms of payment.

Financial necessities of salaried workers revolve more specifically around life-cycle and seasonal events. Generally living with unemployed relatives and barely making ends meet, any emergency that arises-illness or death in the family or an urgent home repair-or excess spent-a child’s birthday party or a present for a newborn grandchild-is enough to throw the budget off balance and result in indebtedness. Since these events are frequent, salaried workers are continually relying on some form of credit, be it a personal loan, credit card purchases or payment plans.

Similar behavior can be observed among the microentrepreneurs. Since household and business budgets are rarely separated and mobilizing savings is rare, life-cycle events affect microbusiness owners with the same intensity as the other groups interviewed in the study.

With respect to savings, microentrepreneurs prefer to invest profits in stock or on physical improvements for the business rather than put it aside for eventual needs in the form of formal savings. In Recife, *sorteios* serve as a savings mechanism for a small portion of the population. This informal manner of amassing a lump-sum of cash without bureaucracy and interest is used to invest in some opportunity rather than establish an emergency reserve fund. The habit of saving money for emergencies or to cover projected expenses can only be observed among the salaried workers, mostly women and generally in very small quantities.

## Income

The research revealed a correlation between the income level and the degree of formality of the financial services used. This correlation was in some form expected since those with higher incomes satisfy more easily the demands of formal financial services whereas the majority low-income populations are restricted to informal services or the informal use of formal and semi-formal services.

Of the three income groups studied, interviewees from the medium-low category use bank services most frequently. Those who reported to have a bank account were of this income level, as were the majority of





those reported using pre-dated checks, credit cards and bank loans, especially automatic loans. As a consequence, loans from consumer-lending agencies are infrequently used due to the more reasonably priced bank option. In this income group, moderate use of semi-formal services such as the company *caixinhas* and salary advances was identified among salaried workers. To a much lesser extent, the study identified the participation in *sorteios*, finally and use of *agiotas* to cash post-dated checks in cases of emergency.

In low-income populations, bank services are very little used. With the exception of a few microentrepreneurs and some public sector employees or retirees who receive their pensions through the banking system, people of this income level do not have access to banks. Rather, formal financial services are used in the form of payment plans and store credit cards. Already heavily and widely used, these deferred purchase options offered by stores are being made more and more accessible to this segment of the population, as retailers and their partners seek to penetrate the market. Consumer lenders are only sought in cases of great need although it appears that it is within this population that these institutions find the greatest number of clients. Few admit having gone to *agiotas*, but it is clear from the focus group discussions that these usuries are used from time to time. Those with low income also use informal store credit frequently and take small, short-term loans from relatives and friends relatively often.

The lowest income groups in this study are restricted to informal services especially informal store credit and “borrowed” credit. Users of these services tend to pay their obligations religiously in order to “keep the door open” for future needs that will inevitably arise. Small loans from family and friends are used whenever possible, but cannot be relied upon since family and friends often have similar financial problems and are unable to help out.

## Sex

Generally, women are more conservative, more cautious and more preoccupied with earning or maintaining enough income that enables themselves and their families to live a dignified and relatively comfortable life and ensure a stable future. They are more apt to save, in a passbook or a house coffer (called “*meaeiros*”, in Recife), than men. Likewise, only women mentioned the use of funeral insurance. And while women appear more resistant to the idea of taking money to start or expand a business, they show just as strong a motivation to work hard as men.

Men appear to take more risks and be more ambitious. The majority of the more structured microentrepreneurs were men. Despite changes in relation to the role of women in society and family in the segments of the population studied, the notion that the man has the responsibility for maintaining the home financially remains strong. The men appear more preoccupied with expanding their businesses or consolidating their asset base, with the objective to change their lifestyle and move to a higher socio-economic level. To achieve this objective, they appear more willing to make sacrifices and take risks than the women and are more inclined to the idea of taking loans for business.

## CHAPTER IV IMPLICATIONS AND CONCLUSIONS

The microfinance sector has demonstrated a relatively low level of growth despite a marked increase of new actors in recent years and an apparently large potential market. This study sought to understand the reasons behind the slow development of the sector by examining the needs of a segment of this potential market, as well mechanisms and strategies currently used to satisfy these needs. The results provide useful data to understand the low level of usage of MFIs in Brazil.

The authors were able respond to the initial research questions regarding to what extent products are adapted to the needs of the demand, how cultural perceptions impact the use of financial services and the present level of knowledge of MFIs. The answers to these questions point to some important implications for the microfinance sector as well as several new product concepts.

### LESSONS LEARNED

► **Current products meet only one of the many financial needs of potential clients.**

Microentrepreneurs do express the need for productive credit more or less in the form it is being offered: working capital loans of R\$ 500 – R\$ 3000, interest rates of 3-5%, terms of 8 to 36 months with a grace period. However, this study has demonstrated that the self-employed –just as salaried workers and the unemployed–have financial needs that go beyond productive credit. Poor families are more vulnerable than rich ones when it comes to dealing with unplanned events such as medical emergencies and funerals or taking advantage of educational, business or home-improvement opportunities. The lack of specific financial services to manage these needs leaves families with little choice but to take on debt on terms that are ill-adapted to repayment capacity, thereby weakening further the household (and business) income base. If one considers microfinancial services as offering income security rather than tools of income-generation<sup>26</sup>, then it is critical to address these non-business related needs that heavily impact financial stability.

► **MFIs are targeting too high.**

Most MFIs appear to have terms and conditions that are out of reach of very low and low-income populations. The co-signer requirement, often used as a substitute for proof of income, is very difficult to satisfy and perceived with a certain discomfort. Designed to “simplify” access to credit, the co-signer requirement is, on the contrary, considered one of the principal barriers. Excessive paperwork required throughout the loan process–CPF, ID card, proof of residence (of the client and co-signer), proof of income, trimestral income statement, income tax declarations–also serves as a deterrent to potential clients; gathering the documents is not so much difficult as it is overwhelming. Further, compared to the terms offered with installment credit, terms proposed by most MFIs are too short and payments too big for low-income populations to feel comfortable. There is a common fear of not being able to repay, which probably could be overcome by extending the repayment period and keeping installments very small.

<sup>26</sup> As suggested by Wright (1999).



Clients for whom these conditions do not pose a problem generally have access to other formal credit services such as banks, credit cards and overdraft facilities

▸ **The ambiguities of having a marred credit record (*nome sujo*)**

A credit record check is an integral part of any formal credit process, be it opening of a bank account, purchasing of a good with some form of installment credit or writing a post-dated check. Persons with a marred credit record are therefore unable to carry out any formal credit activity, trapped in a situation of semi-marginality, excluded from a series of financial and economic activities.

The *nome limpo* (clean credit record) requirement is complicated: while interviewees do not contest its relevance, they complain of its arbitrary nature. Many participants underlined that their inclusion on credit protection agencies' blacklists was due to an emergency or an unpaid debt run up by a friend/relative who borrowed the credit card, then disappeared without paying the sum due. Loans from family members, friends, *agiotas*, *fiado* and "borrowed credit" are relied upon to get by until the debt can be paid off, which demonstrates a certain level of creditworthiness, despite having *nome sujo*.

Based on the observations during the field study, it was estimated that between 20% and 30% of interviewees from low and medium-low income groups were on credit protection agencies' blacklists. It was less common to hear of people from very low-income groups with *nome sujo*, since they often do not use financial services that consult SPC, SERASA, etc.

▸ **Cultural perceptions of credit and financial institutions impact the willingness to take loans.**

The colloquial distinction between *crédito* and *empréstimo* (loans) is an important one in the minds of low-income populations. *Crédito* refers almost exclusively to the process of purchasing a good on an installment plan. An *empréstimo* is considered a form of financing that involves the transfer of cash from the lender to the borrower. Most entrepreneurs attest to using credit, i.e. buy in installments, but complain of the lack of availability of financing, i.e. loans.

In general, *empréstimos* are considered solutions to emergencies or problems. To seek a loan is to avow inability to manage the present situation. The use of *crédito* on the other hand carries much less psychological baggage: it is an option that simplifies the acquisition of a good or service. This perception of installment credit as a natural part of the purchasing process helps explain the widespread "lending" of one's name, credit card or checkbook. Purchasing with deferred payment is part of everyday life and the risk that comes with it is nothing out of the ordinary.

While microentrepreneurs tend to perceive taking loans more positively, they feel frustrated by the lack of suitable options. There is a generalized feeling among the low income and very low-income groups that banks discriminate against the poor, although the dislike for these financial institutions accompanies a desire to be a part of them, as banks represent status. Consumer-lending agencies are intensely distrusted because of misleading advertising: they promise low interest but in actuality have extremely high costs, once all the fees are added up. MFIs are frequently so little known and understood that they are not even considered an option or are assumed to be a "relative" of the banks and consumer-lending agencies.



► **MFIs are relatively unknown.**

Microfinance institutions are little known among the populations studied, especially in São Paulo where MFI outreach is yet limited. A handful of participants had heard of the *Banco do Povo* de Santo André; others were aware that the city government had a new program, , although no one knew its exact name. Microentrepreneurs frequently mentioned the PROGER line, referring to it as program offered by SEBRAE<sup>27</sup>. Interestingly, several interviewees in São Paulo had heard of the *Banco do Nordeste's CrediAmigo* program and its use of solidarity lending on television. Populations in Recife were more familiar with microcredit, having heard of *CrediAmigo* and the Municipal government's *Banco do Povo* on the radio, television and via acquaintances who had taken loans.<sup>28</sup>

► **MFIs lack a distinctive competitive position in the market.**

As previously mentioned, MFIs are considered little more than “relatives” of banks and consumer-lending agencies, when considered at all. While MFIs ostensibly target the poor, loan access requirements are similar to those for the middle classes. *Bancos do Povo* clearly enjoy a greater visibility, but appear to raise suspicions among the populations studied that they exist mainly to achieve electoral and political gains and not to offer efficient and inexpensive financial services.

The loan process is frequently not understood. In Recife, there was a widespread belief that the inventory of assets elaborated by the loan officer is used as collateral for the loan, and assets will be expropriated in case of default. The interviewees who had looked into the *CrediAmigo* program, believed the solidarity group guarantee to be a requirement of five co-signers. Further, in São Paulo, a group of microentrepreneurs insisted that the PROGER credit line offer 3 years grace period (in fact loans may be for three years but grace period is never more than 6 months).

## IMPLICATIONS FOR THE MICROFINANCE SECTOR IN BRAZIL

The results of this study suggest a number of operational and institutional changes may be necessary to make the microfinance sector truly relevant and attractive to the populations it is designed to meet.

**Redefinition of the target market and the actual products.** The potential demand for microfinance consists of a broader population than the microentrepreneurs and the self-employed. This study has presented evidence that all low-income populations—salaried, unemployed, students and microentrepreneurs—have financial needs that could potentially be satisfied by the microfinance sector. There appears to be a significant interest for products that reduce vulnerability in times of emergencies such as illness and death, as well as products that help poor people invest in opportunities like education and home-improvement. Meeting these needs will require MFIs to broaden their client base and design new services.

<sup>27</sup> Serviço Brasileiro de Apoio às Micro e Pequena Empresas. In reality, PROGER is a federal program that is part of a larger initiative Brasil Empreendedor. SEBRAE's role is to provide assistance for business planning, which is one of the requirements for accessing credit from the PROGER credit line.

<sup>28</sup> Only three participants made reference to CEAPE-Pernambuco (Centro de Apoio aos Pequenos Empreendimentos), the largest in Brazil; FRAC was mentioned by one person as was the NGO Visão Mundial.





**Revision of requirements and methodology.** Current requirements make access to microcredit difficult for the majority of low-income groups. MFIs are essentially targeting populations—medium-low income entrepreneurs—that have other, more attractive options such as credit cards and credit lines. If the microfinance sector seeks to address clients that are truly excluded from formal banking institutions, then MFIs will need to look for creative options to modify existing requirements.

Solidarity group guarantee is one option, although many potential clients express a strong resistance to this methodology. Nonetheless, experiences in the Northeast, in particular, have demonstrated that solidarity groups can work given the right target population and an effective awareness effort. Further, experience in other countries points to solidarity group loans as an important entry level product, a way of drawing in low-income clients and seasoning them for individual loans.

A stub from a registered payment plan transaction, a new product concept described below, may be another substitute for current guarantee requirements, although further research and refinement is necessary.

The legal seizure of the debtor's goods (*penhora*), or fiduciary alienation, the transfer of property and indirect possession of a good to the creditor, are options that microentrepreneurs themselves cite as viable replacements for co-signers. The legal implications of these alternatives need to be studied further to determine their viability.

**Adaptation of terms of payment.** Installment credit is highly appreciated because installments are within reach of clients' ability and desire to repay. Small payments are reassuring, even among populations that can pay more. They fit more easily into the monthly budget and have less impact on regular expense patterns. Further, the widespread use of deferred payment and installment credit means that paying off small debt is part of life, and most families do not hesitate to make further purchases on credit once one payment plan has been paid off. This willingness to "renew" credit is particularly interesting given the relatively low renewal rates observed among MFI clients.

Grace periods are equally desirable. Microentrepreneurs attest to needing time for a loan to "take effect" in terms of increasing profits. Readjusting expenditures to accommodate a new debt is more easily accomplished when it can be planned for. In order to avoid problems of clients "forgetting" their debt during the grace period and to help MFIs maintain a certain control over the operation, it is recommended that the period be relatively short and the client repay interest starting from the moment the loan is made. Lastly, most households appear to be subject to seasonal fluxes in income and expenses, a factor to be considered when designing appropriate payment plans.

**The use of adapted language.** The language that MFIs use when communicating with clients and potential clients enormously influences client understanding of the credit process. There is a gap in understanding between MFIs and clients due to the language being used, which is further complicated by the little knowledge of microcredit processes in general.



MFIs need to be aware of the connotations of words like *empréstimo*, *crédito*, *financiamento*, *garantia*, and be careful of adopting terms and vocabulary that are clear and familiar to clients. “Formal” terms can scare off potential clients, either because they do not understand them or because the terms are associated with negative images of financial service providers from which they feel excluded or by whom they feel “abused”. Moreover, “formal” terms are often only vaguely understood. This lack of understanding complicates the loan process and leads to feelings of being misled.

**The importance of transparency and clarity.** Interviewees particularly disliked feeling misled. Loan processes and repayment plans should be clear, but not overwhelming in detail. Clients want to know the interest rate and the total interest they will pay, but will generally retain the information in terms of the amount they pay each month and not the rate itself. Regular fixed-sum payments appear to be more easily accepted than payments that change over the period, even if they do diminish. Most people are aware of finance charges, and prefer to know exactly how much they represent.

**The importance of creating a distinctive image.** Overall, MFIs in the regions studied suffer from the lack of a distinctive, positive image. They are little known and are not perceived to be very different from any other financial institution. The exceptions are *Bancos do Povo*, whose political ties can be sources of mistrust. As such, MFIs must invest heavily in customer service, physical presence in the communities they target and building personal relationships with clients in an effort to distinguish themselves from the lot. Regular systematic exchanges (group meetings, individual interviews) with clients should be the keystone to establishing an MFIs image; this not only creates a climate of trust but also helps the MFI respond more rapidly to the needs of its clients.

In creating an image, MFIs should be wary of the consumer-lending agencies marketing techniques, but need not distance themselves altogether from banks. The latter, despite being considered discriminatory, are viewed as “serious” and represent status. In general, the formal sector is something to strive to be a part of. For many microentrepreneurs, microcredit represents the bridge from the informal to the formal. MFIs are in the unique position to reach out to clients and help them cross this bridge.

### The role of savings

For the low-income families, savings can offer an important base of security. For the financial services providers that can accept deposits, it is a source of low-cost resources. Despite these benefits, overcoming the present lack of savings culture observed in the populations studied will require efforts directed at awareness, expansion and adaptation of products, and political will.

The populations studied recognize the benefits of savings, at least in theory, but do not feel capable of saving. The awareness efforts should seek to show that savings is a viable option for the majority by demonstrating that the monthly payments they make for their loans are nothing more a form of saving in reverse.<sup>29</sup>

<sup>29</sup> The notion of saving down is discussed by Rutherford, op.cit.





Savings products should also be expanded and presented in a more accessible format for the low-income populations. The creation of specific products (described below) and services of itinerant community agents should be considered. It is worth pointing out, however, that no matter how great the efforts are, little will be attained unless the present interest rates paid on savings passbooks—considered a major disincentive to saving by the populations studied—are reviewed and modified.

## **NEW PRODUCT CONCEPTS**

The authors propose the following unrefined concepts for new products based on the findings of this study. All low-income individuals, microentrepreneurs, salaried/unemployed, would be eligible for these products, although access requirements would need to be established by MFIs according to risks involved. All of these concepts raise issues of viability. Further research is necessary to study their operational and legal feasibility.

### **► Insurance for prescribed medicine and laboratory tests**

Public health services do not cover the costs of prescribed medicine and laboratory tests, creating a serious financial burden for low-income populations. An insurance product to cover these costs would help decrease considerably the impact an illness can have on household budgets. The costs of such a product could be kept to the minimum by not including office visits or hospitalization, currently covered by the public system.

Like other health insurance plans in Brazil, clients could make very small bimonthly or monthly payments to have access to a credit card with a pre-established limit that could be used to pay for prescribed medicines and tests in certain pharmacies or laboratories. The card would be non-transferable, but could be used to cover the tests and medicines of self-defined family members.

### **► Funeral Insurance**

There is a recognized and partially met demand for funeral insurance among low and medium-low income groups, but the demand still appears great. The product would involve the payment of very small monthly installments for a few years, making the client eligible for a pre-determined sum to be spent on funeral costs. The benefits would be transferable to self-defined family members, named in the initial contract.

### **► Professional Training Loan**

There appears to be demand for a loan available to salaried workers, the unemployed or microentrepreneurs to pursue secondary, university or professional training. To help clients gain confidence in their ability to repay, the loan could initially be offered with a grace period and involve repayment in very small installments. The use of vouchers that cover part of the training cost distributed to the consumer may also be an option to meeting this need.<sup>30</sup>

<sup>30</sup> See Goldmark and Schor (December 1999) for a detailed discussion of vouchers.





#### ▶ A loan to rehabilitate one's credit record

A considerable number of people in the medium and low-income segments are excluded from the financial market due to being on the blacklists of the credit protection agencies. Many end up on these lists as a result of adverse circumstances and not deliberate negligence of their obligations. These people are often eager to rehabilitate their names and fulfill their obligations but cannot do so because they do not have sufficient resources to pay the debt that has invariably increased due to interests, fines and fees.

Likewise, the financial credit institutions are also anxious to have these liabilities covered. They are open to agreements that will facilitate the payment on the part of the debtors and pay high commissions to collection agencies for each payment received.

This kind of loan product, to be offered by an MFI, could consist of a package that includes direct negotiation with the creditors to decrease the amount due by promising a single up-front payment and a custom-designed payment plan between the MFI and borrower with elastic terms and reasonable interest rates.

The product would also contribute to broadening the MFI's client base for other microfinance products.

#### ▶ Home improvement loan

Demand for home improvement loans among the low-income population is strong, and although the *Caixa Econômica Federal* offers products to meet this demand, the truly low-income segments do not appear to use them.

The great number of governmental or non-governmental organizations that support the financing of the housing programs in Brazil and the rest of the world point to the existence of a variety of innovative methodologies in this area that could be taken into consideration.<sup>31</sup> The program *Casa Melhor* in Fortaleza is an example of how it is possible to stimulate savings as well as provide direct support to the investments channeled into the housing sector. This project, implemented in partnership with various entities,<sup>32</sup> offers financing for home improvements that involves a combination of client savings, low interest loans and government subsidies.

#### ▶ Community credit card

Credit cards that allow payment in up to 30-40 days without interest are greatly appreciated due to the convenience by the and security they offer. The high acceptance of credit cards in low-income populations could be exploited MFIs to not only increase their client base but to contribute to growth in local economies: the small-scale experience of Banco Palmas, in Fortaleza, shows that a community credit card—i.e., one that can only be used in stores within the community—can play an important role in spurring local economic growth.<sup>33</sup>

<sup>31</sup> Mitlin (1997); Cabannes, Y. (1996); Mitlin and Satterthwaite (1996). Ceará Periferia e IIED (2000).

<sup>32</sup> Projeto do Centro de Estudos, Articulação e Referência sobre Assentamentos Humanos - Cearah Periferia; entidades comunitárias; Groupe de Recherche et d'Echanges Technologiques - GRET; Prefeitura Municipal de Fortaleza (Secretaria do Trabalho e da Ação Social).

<sup>33</sup> Banco Palmas, Relatório II (2000).



▶ **Registration of third-person payment plans**<sup>34</sup>

Using “borrowed” checks and credit cards and the common practice of purchasing items in the name of someone else point to a largely hidden potential market for MFIs. Institutions working in the microfinance sector could harness this potential through an optional registration process that would formalize the informal. In a situation where the “lender” allows the “borrower” to purchase, for example, a refrigerator in his name, both parties would “register” the transaction for a small fee. The registration could be done with the MFI or in partnership with banks or stores. Once the “borrower” has completed repayment, a register would be made in her client file. Upon completion of three “registered” transactions between the borrower and any three lenders, the borrower would have a document declaring creditworthiness. The document could be used to strengthen a client’s future application for various sources of credit and perhaps take the place of a co-signer.

Many issues need to be addressed to determine the viability of this concept, among them: what would be the bottom-end limit for the amount of the transaction to be registered? Who would administer and account for the “register”? Only further research could provide answers to these questions.

▶ **Micro-leasing**<sup>35</sup>

As a way to avoid the use of a co-signer, MFIs could introduce micro-leasing, aimed at microentrepreneurs wishing to purchase equipment, in which the good acquired would serve as a guarantee. Similar to a traditional leasing plan, the microentrepreneur would pay a monthly installment. The maximum payment would be equivalent to the maximum amount of credit.

▶ **Contractual savings for education**

A product of contractual savings for education can be extremely useful for the medium-low income groups of the populations studied.

This product could consist of the payment of fixed installments for a period of time (5, 10 or 15 years), to be determined by the client according to his capacity. At the end of the term, the accumulated amount would be used for payment of educational expenses or professional training.

A variation of this product could involve one deposit that earns interest over a pre-determined period.

▶ **“Incentivized” savings**<sup>36</sup>

Populations studied almost universally recognize the usefulness of saving but find current incentives unattractive. The low interest rates and vague chances to win the monthly drawing that many banks propose do not appear to motivate clients to place the little money that is left over in a savings account: purchasing a good is perceived as more satisfying.

<sup>34</sup> The authors thank Lara Goldmark for this suggestion.

<sup>35</sup> The authors thank Henriqueta Hunguana for this suggestion.

<sup>36</sup> The authors thank Lara Goldmark for this suggestion.





This product concept proposes banks to partner with stores to establish an incentive plan that corresponds to the apparent cultural preference to spend. Savers who maintain a certain amount in their account would be offered a discount at participating partner stores or be exempt from the last installment of a payment plan in a partner store. A higher savings balance would correspond to larger discounts.

There would need to be a ceiling on the discounts offered as well as a selection process to avoid abuse: not all savers could take advantage of the incentive packages. Moreover, further research would be necessary to determine the level of willingness on the part of stores to take part in such a program.

## **CONCLUSION**

Microfinance in Brazil is essentially driven by the belief that small-scale credit is a tool of income-generation. Consequently, small and microbusiness owners are the targets of microcredit and the main product offered is credit for working capital. This type of credit serves the unique purpose of increasing income of the business, which it is hoped will impact the standard of living of the household. It is indeed likely that investment in well-managed microbusinesses contributes to an overall increase in profits, barring any unforeseen issues.

However, faced with an external shock, business or non-business related, gains that have been made are oftentimes lost or at the very least put at risk. Capital that may normally be reinvested in the business must be reallocated to manage the situation at hand. A decrease in investment leads to a decrease in profits, which in turn increases the vulnerability of both the household and the business. In the end, the productive loan ends up doing little more than filling holes.

It has been suggested that microfinancial services be viewed as offering income security rather than contributing directly to income-generation. This implies considering the diverse needs of the domestic unit as much as those of the business. The financial health of one depends largely on the other and the needs of both must be considered to create a more solid financial "platform" from which to manage opportunities and risks. In practical terms, this involves enlarging the current target population by offering greater diversity products and services.





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**Additional resources provided upon inscription in the Microsave-Africa course:**

Manual for Day 1 of Market Research for Microfinance, *Overview of Product Development and Market Research*, MicroSave-Africa, Nairobi, Kenya, February 2001.

Manual for Day 2 of Market Research for Microfinance, *Understanding Customer Needs and Opportunities Using Focus Group Discussions*, MicroSave-Africa, Nairobi, Kenya, February 2001.

Manual for Day 3 of Market Research for Microfinance, *Understanding Consumer Needs and Opportunities Using Participatory Rapid Appraisal*, MicroSave-Africa, Nairobi, Kenya, February 2001.

Manual for of Market Research for Microfinance, *PRA Toolkit*, MicroSave-Africa, Nairobi, Kenya, February 2001.

Manual for Day 5 of Market Research for Microfinance, *Concept Ddevelopment and Introduction to Concept Testing*, MicroSave-Africa, Nairobi, Kenya, February 2001.

Manual for Day 6 of Market Research for Microfinance, *Concept Testing, Pilot Testing and Planning*, MicroSave-Africa, Nairobi, Kenya, February 2001.



## **ANNEXES**

### **COMMENTS ON THE METHODOLOGY**

The Microsave-Africa Market Research methodology is interesting and worthwhile. There is no doubt that focus group discussions (FGDs), when moderated well, are sources of a great deal of rich information that is otherwise difficult to gather, outside of individual interviews. Yet the value-added of the MSA methodology is not in the use of FGDs, but the use of FGDs guided by PRA tools.

#### **The main advantages**

This study applied 5 of the 13 tools, and overall the researchers were pleased with the results. The tools are particularly helpful in 'directing' discussions. While FGDs oriented by a discussion guide require the moderator to be highly adept at subtly steering conversations towards the study's objectives, the PRA tools mobilize the group around an activity that is clearly defined and structured. The moderator remains a key figure, probing and provoking the participants on certain points, but overall the participants "run" the activity. Having a chart to build or table to fill in is very helpful for organizing the session and keeping the conversation on the desired topic.

A second advantage to the PRA tools is that they lead the researchers to examine the research question from various angles. Depending on the tool, the cultural, historic, social and even geographical influences on certain behaviors are highlighted, permitting researchers to understand the participants' opinions from a very broad perspective.

Further, unlike most quantitative methodologies, FGDs can have a positive impact on the participants. In well-moderated FGDs, participants become aware of the importance of their opinions, and share them more freely. It can be truly empowering, especially for very marginalized populations that are rarely consulted on anything.

#### **A question of objectives**

Commissioned by the BNDES' Institutional Development Program, a major funder of a select number of microfinance institutions, our research was guided by a "big" question, "why are MFIs in Brazil so little used?" The tools proved very useful in revealing a variety of "answers" to our question—indeed, we had so many answers that it was difficult to explore each one in-depth to determine their relative importance.

This difficulty was likely due to our lack of an operational "goal", i.e. the study aimed to identify and explain certain tendencies, but the results are not destined to inform any specific operational changes, at least in the short term. Rather, the conclusions will contribute to orienting further research by individual MFIs. As such, during the fieldwork, it was difficult to decide what points needed to be probed the most, what details needed to be drawn out, in what direction to steer the research.

While the objectives of this study were satisfactorily met using the MSA tools, our impression was that the tools are better suited to answering precise "operational" questions rather than more general, overarching ones. This should not come as any surprise, given the methodology was designed specifically for MFIs wanting to carry out their own market research.





The kinds of specific market-research questions that the MSA tools would be very effective in answering include assessing an MFIs image, examining reasons for high drop-out rates, assessing clients' perceptions on products/services offered, identifying the need for refinement of products' attributes, determining the saturation level of certain activities in a particular area, examining seasonality trends and their implications on client' needs and repayment capacity, evaluating clients' opinions of loan policies and assessing the effect of the slogan or logo of an institution.

With respect to this specific study, the tools would be useful in researching further a number of issues such as:

- ▶ Obligatory savings mechanisms: when do the benefits outweigh the sacrifices?
- ▶ Mistrust in financial institutions: what makes a certain institution or service trustworthy? What do institutions have to do to win over the client's trust?
- ▶ "Drop-outs": what are the reasons behind clients not renewing loans? What aspects of the service leave clients unsatisfied?
- ▶ "Refusals": why are loan applications rejected? Which requirements are the hardest for clients to meet and lead to refused applications?
- ▶ Refining the product concepts laid out in Chapter 4 and determining marketing strategies to introduce new products.

### **The importance of training**

The Market Research tools could initially be downloaded for free from the MicroSave-Africa website. MSA took them off the site when they realized that many people were using the tools without proper training, oftentimes leading to disastrous results that were blamed on the methodology. While simple in appearance, the use of the tools requires a highly skilled moderator and a great deal of preparation and organization on the part of the coordinating institution.

The moderator must be familiar with the financial sector and the microfinancial sector in particular. In-depth knowledge of the research objectives is also critical. A good discussion guide will help the novice, but it is not enough. The moderator must know the subject to be studied. If not, it is likely that important aspects that come out in the discussions will not be probed sufficiently.

Not all of the qualities of a good moderator can be taught. The ability to create a certain harmony early on in the discussion, to show genuine interest in the participants' point of view, to use language that is adapted to the group, and to be able to introduce new topics with fluidity and without disrupting the logic of the discussion—these are qualities that come with practice, but are natural for those who have the vocation. The selection process for a moderator must take these qualities into account.

It is also important that the coordinating institution understands the care that must be taken when organizing and setting up discussions. The quality of the results depends a great deal on the logistics (ex.: identifying participants with the proper profile, scheduling the meetings at appropriate times, ensuring transport for participants, etc.), and preparation should not be underestimated.

In short, training in the methodology—including a period of training in the field—is highly recommended for anyone wishing to use these tools.



## DESCRIPTION OF TOOLS <sup>38</sup>

Tool	Objective	Justification
Life-Cycle Profile	The Life-Cycle Profile seeks to identify the phases of a typical individual's life-cycle and the key milestones in it; to determine which of the events require lump-sums of cash; to examine the implications of these for household income/expenditure; to establish current coping mechanisms; and finally to discuss how access to MFI financial services can help the household respond to these. The information gathered can be useful in terms of designing financial product that match the various needs expressed at different milestones during a person's life-cycle.	This tool was used to help determine whether current microfinance products satisfy the various necessities expressed at different points of reference during the life cycle of a person.
Analysis of Seasonality	This tool is useful For obtaining information on seasonal flows of income and expenditure, the demand for credit and savings services and the key issues relating to these four factors. This exercise also provides important insights into some of the risks and pressures faced by clients and how they use MFIs' financial services to respond to these.	This exercise was chosen to give an idea of the ability to pay and when credit and savings are more needed during the year, with the objective of obtaining useful information to come up with products adapted to these necessities.
Analysis of Financial Sector Tendencies	This tool is useful in determining which financial services have been used over time and thus understanding the changes in the use/availability of a variety of financial services over time, and why participants used them. The listing of financial services here is only tentative and will require modification based on the participants' knowledge and awareness of the various products.	Chosen to understand the changes in the use of the availability of financial services, in the long run, and why the participants use them.
Financial Services Matrix	This tool is useful in determining which financial services are used by which socio-economic or socio-cultural strata of society, and why, and thus the potential for designing or refining appropriate financial products. The listing of financial services here is only tentative and will require modification based on the participants' knowledge and awareness of the various products.	Used to provide information about the obstacles faced in using certain services, with the objective of helping to determine the terms and conditions best adapted to microfinance clients.
Classification of Relative Preference	Relative Preference Ranking can help identify how clients and potential clients perceive the financial service providers and components of the financial services they provide.	Used to determine what are the desired and most valued characteristics of financial services currently available, with the objective of providing information for the creation and refinement of financial products.

<sup>38</sup> Taken from the Market Research for Microfinance PRA Toolkit, MicroSave-Africa, Nairobi, Kenya, 2001.

## DIFFICULTIES ENCOUNTERED WITH THE TOOLS AND SUGGESTIONS

The research team ran into a few difficulties with the tools and made the following adaptations to better meet our research objectives.

Tool	Difficulties/Notes	Suggestions
Life-cycle profile	It is very difficult to stimulate discussion with young people who are still living with their parents or very old people. It is difficult to get detailed information regarding the quantity of money the different events require. Depending on the group, it is possible to use another tool after this one.	Ideal population: homogeneous group (in terms of revenue and age) between 25 and 55 years of age, excluding young people still living with their parents. Any revenue level. Probe the populations to compare the pressure that each event creates and not just the quantities of money involved. We must remember that while a funeral may cost less than a wedding, it may create more pressure due to the obligation involved.
Seasonality analysis of household income, expenditure, savings and credit	It is very difficult to apply this tool with very heterogeneous groups (involved in different activities). The variety in income and expense flows makes it very hard to come to a consensus. This tool is good with groups who have little experience with financial services (unemployed, salaried workers). Depending on the group, it is possible to use another tool after this one.	<b>Ideal population: homogeneous group (in terms of revenue and, especially, activity), between 25 and 55 years of age. Any revenue level.</b> We substituted the more popular terms <b>Ganhos, Gasta, Sobra, Pega</b> for those suggested in the Manual ( <b>Redimento, Despesas, Poupanças, Crédito</b> ).
Financial Services Matrix	Salaried workers and the unemployed do generally do not talk spontaneously about financial services. They do not appear to know the different services very well. It is very hard to stimulate conversation with very low-income microentrepreneurs (Minimum Salaries). This group generally has little experience and knowledge of financial services. Informal mechanisms like ROSCAs, raffles, and <i>caixinha</i> are not mentioned spontaneously. The heterogeneity of financial products in Brazil makes it difficult to establish a list. Frequently, participants mix products with institutions. Generally, this exercise takes time. However, if the group is accustomed to using financial services and the list is established quickly, another tool may be used after Matrix. We liked to apply the Trend Analysis too after the Matrix when possible.	Ideal population: homogeneous group of microentrepreneurs, preferably with a medium (and not very low) income level. The moderator may need to ask about informal mechanisms, offering examples. The moderator must know the products and institutions that exist in the area being studied in order to be able to categorize the participants' response properly. Depending on the objectives of the research and the type of MFI, the moderator could suggest the type of products the institution wants to investigate. The list could be developed beforehand if the institution doing the research wants to compare their products/services with those of another specific category. We did not use the categories "rico", "nãotão-rico", "pobre", "muito pobre" which did not seem to make much sense in the populations studied. We preferred to ask participants to categorize the services according to ☺ and ☹, i.e. if they overall liked the service or didn't like it.
Relative Preference Ranking	The heterogeneity of the sources of financial services in Brazil makes it difficult to apply this tool. We would have to list a motley group composed of large department store chains, small neighborhood stores, informal merchandisers, banks, consumer credit companies, government programs, etc. Not impossible but difficult. The list of the institutions does not come spontaneously, and there is a strong tendency to mix products and institutions (ex.: post-dated checks, store credit at department store X, moneylenders, credit cards) This tool would probably provide more interesting results in an area where competition among similar kinds of institutions is very strong. Generally, this exercise takes time.	Ideal population: homogeneous groups of microentrepreneurs with experience and knowledge of financial services. Again, depending on the type of MFI, the moderator could suggest the type of products the institution wants to investigate or prepare the list in advance.
Financial Sector Trend Analysis	The exercise is generally completed quickly and can be done with another tool.	Ideal population: any group.