

**SYNERGY BETWEEN MICROINSURANCE
AND MICROCREDIT
AND THE DEVELOPMENT OF THE MARKETS IN BRAZIL**

Lauro Gonzalez (Coord.)

Caio Toledo Piza

Daniel Bruno Garcia

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Executive Summary

The aim of this work is to discuss the probable synergy between microcredit and microinsurance. The analysis started from the present definition of microcredit and the characteristics of its offer in the Brazilian market, chiefly by describing the main players and the business models in use. The main database about the informal economy was explored in order to analyze the main characteristics of the potential market of microcredit and microinsurance. The innovations of the microfinances in Brazil, considering the offer of microcredit as well as other financial services, can be useful to the synergy between microcredit and microinsurance.

The idea that there is no microcredit in Brazil is false. Though there are few banks operating in the productive microcredit, and the unexplored potential market is large, the rates of growth, not only in volume but also in active clients, are quite high in comparison with other credit segments, even in the pre-crisis period when most traditional credit segments were growing at high rates.

Microcredit in Brazil and around the world is characterized by the creation of innovative ways of conceding credit. Among these innovations, one should detach the mechanism of group loans and the role of the credit agent. The first diminishes the risk represented by the lack of guarantee because the poor have nothing to offer for this purpose, as real estate to guarantee for the loans. The group represents a kind of “joint guarantee” based on the several forms of link (social capital) between the borrowers. The credit agent is responsible for the relationship between the institution and the borrowers, with whom there is constant contact and monitoring.

The credit agent has the potential to act in the distribution of other financial products. The existence of the credit agent has a great potential for distributing other services and financial products that affect the well being of the poorer. In the microcredit, the credit agent goes to the client and not the other way round. There is evidence that the poor will not seek microinsurance. Lack of information, mistrust and unfamiliarity with the product are the main obstacles. The credit agent has an enormous potential to overcome such obstacles. To take the most from this potential is a question of developing adequate business models.

Innovations like flexibility of payment produce synergy between microcredit and micro-insurance. One of the great innovations of microcredit is to develop a model of business in which the conditions of payment are adequate to the clients’ cash flow, be it daily, weekly or fortnightly. Concerning the microinsurance as well, market research indicates the preference for flexible payments adjusted to income. Consequently, the distribution of microinsurance together with microcredit would permit the creation of important synergies as to the cash flow.

Innovations focused on women promote synergy between microcredit and micro-insurance. Experiences with microcredit in Brazil and around the world testify the importance of focusing on women. Such strategy tends to augment the benefits for the family. Market research indicates that women understand better than men the benefits of microinsurance, opening space for models of business in microinsurance focusing on women that use microcredit.

Bank correspondents are channels of potential distribution for microinsurance and microcredit. About 90% of all existing bank correspondents around the world are in Brazil. Their distribution net is much larger than the number of bank branches. Market surveys about microinsurance strongly stress the role of correspondents in the life of the poorer, though pres-

ently the main objective of correspondents is payment services. There are microfinance institutions (MFIs) that use the correspondents' model. The channels of distribution and the technology are already available. Their use to bring out the joint offer of microcredit and microinsurance is chiefly a question of developing adequate business models.

For the MFIs, microinsurance adds value. In the first place, because insurance linked to credit can contribute to a lower risk of default and an effective loss for the MFI. Furthermore, the MFIs should try to offer services that cover the whole of their clients' needs. As they are generally excluded from the traditional financial system, the clients are severely affected by unexpected events. Thus, microinsurance contributes to increase the well-being of the clients by complementing the credit.

A correct mapping of microcredit should include the various segments concerning the offer of credit to low-income people. The productive microcredit for financing micro enterprises is the core of the microcredit activity. Nevertheless, one must consider that a credit to fight poverty should consider the whole need of the poor such as consumption and housing. In Brazil, the government has indirect action through legislation that demands banks to direct resources to microcredit (mandatory). Concerning direct action, the most noteworthy program is the CrediAmigo of productive microcredit, run by the Bank of Northeast (Banco do Nordeste). Among the traditional commercial banks, the only one that has a program of productive microcredit in a larger scale is Real Santander Bank. Cooperatives of producers are important vehicles for micro finances, but their action in microcredit is still not well mapped out.

INTRODUCTION

Sustainability is very commented nowadays. Basically the term sustainability concerns the involvement of a firm in acting in a viable economic way while trying, at the same time, to generate social benefits also keeping the environmental resources. Microfinances fit exactly in such context, i.e., the search for inclusive business in the offer of services and financial products, thus contributing to combat poverty through market solutions.

Microcredit represents the best known face of microfinances and its development is linked, above all, to the use of innovative mechanisms which put out a great number of flaws that have kept the poor away from the market. Microinsurance has a high potential impact on the well-being of the poor and, as such, must be included in the traditional lines of business. Above all, there are important synergies with microcredit that need to be made profitable, encouraged and operational.

In order to give basis and discuss such potential synergies in the specific case of the Brazilian market, this document is divided into three parts. The first presents the offer of microcredit in Brazil, giving special attention to the question of how term microcredit is conceived, as well as to the existing segments and their respective players.

The second part presents an exploratory analysis of the so-called Urban Informal Economy (ECINF), a public database under the responsibility of the Brazilian Institute of Geography and Statistics (IBGE). The clients of microfinance institutions (MFIs) are generally informal and it is indispensable that their characteristics be studied in order to carry out any concrete intention of business in microfinances.

The third part deals directly with the synergy between microcredit and microfinances, taking into consideration not only the existing business models, but also the potential of changes through the introduction of new technologies and kinds of institutions.

PART 1 – THE OFFER OF MICROCREDIT IN BRAZIL

1. Microcredit: How to define it?

1.1 The innovations

The term microcredit, as popularly used, appeared in the '70's starting with the adoption of an important set of innovations that aimed at making possible the offer of credit for the poor. Its appearance is not linked to any theoretical or academic concept but rather to a "concrete revolution" in the way to offer small-amount credit to poor people who generally live outside the formal economy. The traditional business models excluded the needy because they didn't present new solutions to overcome three great obstacles: 1) high risk; 2) high transaction costs; 3) absence of guarantees.

So the lines along which microcredit is presently defined are given exactly by the innovation which aims at overcoming the obstacles mentioned above. Such innovations are:

a) Group loans

Group loans can be defined as arrangements made by individuals who do not dispose of the guarantees normally required by the bank system. These people spontaneously form a group with the object of obtaining loans. Each member of the group receives a certain amount and simultaneously guarantees the loans of the others. In case of default from one of the members, the others have to pay the correspondent installment, under penalty of having their credit cut off.

There are many models of group loans. For example, in the Grameen Bank model, the groups have about five members and the funds are initially released to two members. When some part of the loan has already been paid back, four to six weeks after the first release, two other members get their part. The process goes on until the last member gets his loan. The variations of the group loan model depend on the size of the group, the moment when amounts are released and the frequency of payments.

The great advantage of group loans is to deal with the problems of asymmetry of information and the high costs of business. In a market where there are good and bad payers, the latter tend to benefit whenever the bank cannot tell who is who. In economic terms, high-risk borrowers (bad payers) end by getting a subsidy from the low-risk ones. Inefficiency emerges when such subsidy is so high that reliable payers leave the market. Group loans may reduce the interest rates and keep these payers in the market.

To understand such behavior it is necessary to keep in mind that the formation of groups is spontaneous, and if the credit contract establishes the so-called joint responsibility, i. e., everybody is responsible for everybody else's default, potential debtors are encouraged to use all information available in order to form a group with the best possible peers. Assuming that the borrowers have better information about each other than the bank has, the effect on the expected default will be beneficial. Furthermore, it should be noted that the bank keeps on ignoring the credit reliability of the borrowers. The borrowers themselves are better informed and will take care of the screening and subsequent monitoring of the group. It is important to remind that, as the groups are formed spontaneously, a certain level of relationship amongst the borrowers is expected. Consequently, the above mentioned (social) costs associated with the selection and monitoring become cheaper, for it will be less costly for a borrower to monitor his peers than it would be for the bank to do it.

b) The credit agent

Another crucial innovation is the credit agent. This official is responsible for gathering data about the borrowers (chiefly new entrepreneurs or groups), for accompanying and helping clients, for preparing and analyzing technical reports and for recovering credits from borrowers

in default. The credit agent has the prime responsibility for introducing microcredit in a community. No wonder many institutions consider the agent as the key to all small-loan activity.

Looking at the traditional banking market, one can see that it is usual for the banks to have employees to attend a specific group of clients. The greater the economic importance of the client, the greater degree of exclusiveness in attendance. In the world of micro-entrepreneurs, this market logic would not make sense, as it would just represent automatic models of decision and transaction. The credit agent breaks this paradigm and leads to an activity that constitutes an “upside down private banking”. Even dealing with small sums, the borrower enjoys a near and special relationship, similar to that of the high income clients.

A highly productive credit agent may handle, in the average, 300 clients, something that allows the credit institution to get a certain economy of scale. Furthermore, with the greater proximity between the agent and his clients, one of the essences of the traditional credit operations is recovered: the structuring of a long-term relationship between creditor and debtor, with a potential impact over the levels of default.

Besides, the credit agent tends to spend a lot of his time close to the borrowers. The agent often lives near the neighborhood of his clientele, or even in their community, reinforcing the link between them and allowing a better accompaniment of their portfolio. This way, it becomes possible, for example, to handle problematic credits with specificity, investigating why a certain payment was not accomplished. A case of illness in the family, of theft or delay in delivering products to be sold may afford a negotiation that simultaneously attend the debtor, giving him a chance to redress his cash flow, and reduce the effective loss on the loan.

It should be added that, despite the economy of scale obtained by the credit agent through growing productivity, the operational costs tend to be high. That is why, taking into consideration usual market rules, the interest rates charged would hardly ever be similar to those applied to great organizations, though for this analysis it is fundamental to consider not only the costs but also the risks involved.

c) Progressive loans

The concession of progress in granted loans represents a fundamental dynamic incentive for the administration of risk in microcredit operations. Typically the loans start with small values and, if repayments flow regularly, the ceiling on the value borrowed is increased. The repetition of the operations permits the accumulation of information about the client. In the model of progressive loans, the menace of cutting down future loans has more weight, because the entrepreneurs may understand that if they fail to fulfill their obligations, they won't get the higher amounts that would follow those granted at the beginning.

Considering this flow of thought, it is understandable why microcredit, despite high operational costs, should keep interest rates lower than those traditionally applied to micro-entrepreneurs, as those offered by usurers. The smaller the interest rate, the bigger the present value of the benefit the entrepreneur loses if he fails to pay. To summarize, the rates must be sufficient to cover the capital cost of all investors, but they become counterproductive if they are too high. Another important factor is the mobility of the borrowers. The more an entrepreneur changes from one place to another, from one city to another, the less will be the efficacy of these dynamic incentives.

d) Frequency of payments

The design of an adequate frequency of payments was another innovation among the practices of microcredit. From the point of view of the borrowers, it is important that the payment of the loans be synchronized with the cash flow of the financed enterprises, according to the famous “golden rule” of matching installments proposed by the financial administration. Payments are collected weekly by most of microcredit institutions, which seems logical due to the cash cycle typical of the attended entrepreneurs.

For the creditor, regular weekly payments allow bad payers to be quickly detected, so that action may be taken by the agent, and, in the case of group loans, by the partners. Another advantage is having at hand a cash flow that may be used for different objectives, not only for monitoring the payments. Many institutions demand that all members of a group be present at the moment of payment, or else, that one member (leader) be responsible for the whole payment, i. e., in one and only booklet. This way, the leader will, in due time, collect the money from the other participants, creating an immediate pressure on potential delays.

Though weekly (or fortnightly) payments preserve for the borrowers the system of matching installments, cultural factors tend to weigh heavily against such practice. To educate the market seems to be a constant defiance for the creditors. Many entrepreneurs end by being charged with much higher interest rates for having chosen to pay monthly.

e) Focusing on women

Another important innovation of microcredit is the focus on women. It is better to offer microcredit to women than to men. The main reasons that support this assertive are to oppose the frequent sex bias shown at the financial market and to acknowledge the role played by women in the family and the society, which contributes a lot to the reduction of poverty.

The difficulty for women in obtaining material and financial resources is obvious, although less now than decades ago. This fact is due to different cultural aspects and to the way social relationships are constructed. The main inequality comes from the condition of access to the labor market, but the gender difference in the access to financial services is also important. In the 70's, women represented less than 1% of all loans in Bangladesh. In Brazil, IBGE estimated in 33% the number of informal urban businesses led by women. Out of 10 million concerns in this segment, only 5% had obtained access to credit. It is important to have in mind that, in 2007, 19% of the families were led by women without spouse. Such percentage goes up to 33% if one includes families in which the woman is the reference, according to a survey also done by IBGE.

The second argument refers to the concept of women empowerment, which is the increase on autonomy, authority and legitimacy of women in the face of family and society. It is believed that women are more cautious than men in the administration of resources. Consequently, higher income resulting from the efforts of women lead to higher welfare benefits like better nourishment, health and education for children, as well as renovation and enlargement of homes. So credit granted to women tends to bring greater benefits to members of the household. There are researches that demonstrate statistically significant differences of these effects among men and women.

If we consider a chain of impact, women empowerment brings up broader social changes. This may be related to the greater use of contraceptive methods that can cause variations in the rate of fertility. There is concrete evidence of the broader participation of women in community associations and in political activities in general. Thus the focus on women represents a redefinition of their social role. According to Amartya Sen, Nobel Prize of Economy, women are now seen as endowed with a condition of free agent, with capacity to act on their own and promote dynamic social transformations.

1.2 Microcredit in practice

To sum it up, microfinance is related to the offer of financial services to low-income population, generally excluded from the traditional finance system, in different ways. Amongst such services, the most outstanding (not necessarily the most important) is microcredit. Other services are microinsurance, savings accounts, means of payment etc. Therefore, microcredit is nothing more than credit within the definition of microfinance.

Though there is a relative agreement about such definition, in a practical viewpoint there is no manual of classification, as microcredit or not, for the financial products, either formal or not. A certain kind of loan may be classified as microcredit or not by two different institutions.

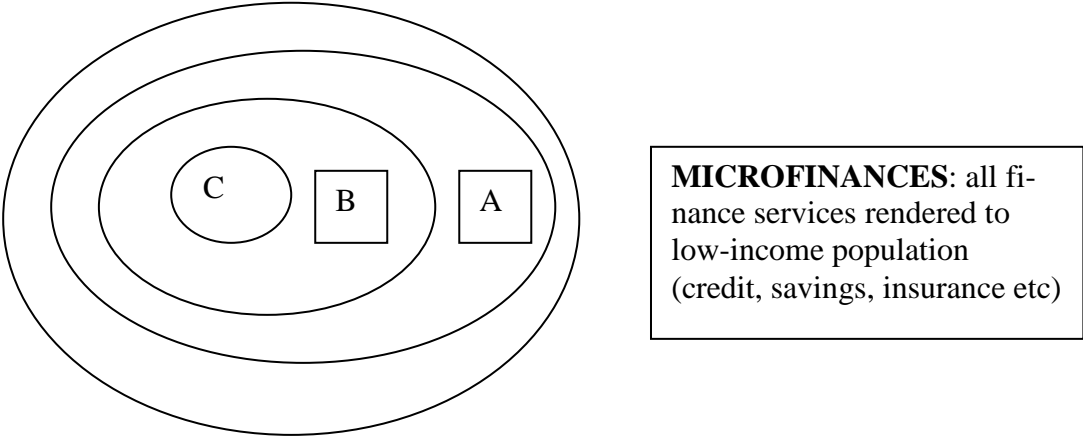
The question above makes it difficult to systematize information on the subject and evaluate the size of the market. Even institutions specialized on benchmarking in this field recognize the existence of different definitions and also the implications of such great diversity, as is the case of Microfinance Information Exchange (the MIX)¹ who defines microcredit as any credit inferior to 250% of the per capita GDP adjusted by the parity of the purchase power (PPP). From a practical viewpoint, this definition classifies as microcredit all loans inferior to R\$ 10,000, approximately.

For others, microcredit may have the following definitions:

- (A) Microcredit as **popular credit**: refers to the loan of small amounts to the low-income population. The object for which the loan is granted (consumer items, payment of debts, productive investment) has no importance in this definition. The methodology of concession is not different from the one used by the traditional financing system. The main providers of this product are the public banks (Caixa Econômica Federal – CEF, Banco Popular, Banco do Brasil) and the finance companies;
- (B) Microcredit as **productive microcredit**: it refers to credit services chiefly to finance assets (fixed investment or working capital) for activities of self-employment, formal or informal;
- (C) Microcredit as **oriented productive microcredit**: it refers to the concept of productive microcredit, aiming at the low-income population. The methodology for granting the credit depends on the action of credit agents².

Figure 1, below, helps to understand this:

Figure 1: Financial services oriented to the low-income population



Discussing which of these definitions is the most adequate is not the purpose of this document, mainly because there are clearly political and ideological positions involved. More than deciding which definition is the best, what really matters is the design of differentiated credit products fit

¹ MIX is the most important supplier of business information dedicated to strengthen the microfinance activity. The main focus of the organization is to provide objective data and analyses on the microfinance providers. Through this, MIX promotes financial transparency in this industry and helps to build an information infrastructure in the developing countries (www.themix.org).

² Officials trained to prepare socioeconomic reports on self-employment activities, give educational orientation on business planning, identify the need for credit and management, and keep a close relationship with the clients.

for the integration of the poor to the market. The focus of this report shall be the mapping of institutions that **offer services of productive microcredit to activities of self-employment, formal or informal, for the low-income public.**

1.3 Governmental initiatives and types of institutions linked to microcredit

1.3.1 National Program for Oriented Productive Microcredit (PNMPO)

Due to the potential importance of microcredit as a tool to combat poverty, several areas of the government have been strongly active on the subject (for good and for bad), directly and indirectly. In order to characterize the offer of microcredit, Federal Law 10,735, of September 11, 2003, is worth mentioning. According to this law, 2% of cash deposits in commercial banks, multiple banks with a commercial portfolio and the Federal Savings Bank (CEF – Caixa Econômica Federal) must be destined to microcredit. To identify institutions authorized to operate with microcredit, it is indispensable to examine the National Program for Oriented Productive Microcredit (PNMPO), set up by Federal Law 11,110, of April 25, 2005 under the Ministry of Labor and Employment (MTE) to direct funds to the microcredit sector. The main characteristics of the PNMPO are:

- **Objects:** (a) promote the generation of jobs and income amongst popular micro entrepreneurs; (b) offer resources for the oriented productive microcredit; and (c) offer technical support to the institutions operating with Oriented Productive Microcredit.
- **Source of funds:** (a) Workers' Support Fund (FAT); (b) pegged down resources: part of the cash deposits of commercial banks, multiple banks with a commercial portfolio and the CEF, according to Law 10,735;
- **Definition of popular micro entrepreneur:** a natural or legal person engaged in productive activities with an annual gross income up to R\$ 120,000.00;
- **Qualification of oriented productive microcredit institutions:** (a) independent credit cooperatives; (b) fomentation agencies (Provisory Measure 2,192-70, of August 24, 2001); (c) micro entrepreneurs' credit societies – SMCs (Federal Law 10,194, of February 14, 2001); (d) Civil Society Organizations of Public Interest – OSCIPs (Federal Law 9,790, of March 23, 1999). To be able to operate with PNMPO resources, such institutions must register with the MTE;
- **Qualification of organizations that forward funds to the oriented productive microcredit institutions:** development banks, fomentation agencies, cooperative banks, credit cooperative federations.

1.3.2 Summary of operating institutions

Starting from the characterization of the program PMNPO, it is possible to classify the operating institutions as follows:

Banks: initiatives promoted by public and private banks. In relation to public banks, the CrediAmigo initiative of BNB deserves special mention. It is the most important microcredit initiative in the country. As for the private banks, the arrival of the big banks in the activity is to be noticed, with emphasis in the Real Microcrédito, an initiative of Real Santander Bank. It is worth noting that CrediAmigo is operated in partnership with an OSCIP.

NGOs and OSCIPs: In 1999, Federal Law 9,790/99 (called the Law of the Third Sector, i. e., neither public nor profit-oriented) improved the regulatory structure of the relationship between NGOs and the government. From then on, in order to obtain public funds, NGOs must qualify as OSCIPs before the Ministry of Justice and execute a Term of Partnership. In the same year of 1999, a Provisory Measure (MP 1,914, of July 28, 1999) excluded OSCIPs and SCMs from the Usury Law, allowing them to operate credits with an interest rate above 12% per year. This measure opened the possibility for OSCIPs to have some income (and for SCMs to obtain prof-

its). In this category, among other entities, it is worth citing the network of Centros de Apoio a Pequenos Empreendimentos – CEAPE (Centers for Backing Small Businesses), the Women’s Bank, the VivaCred Program, the Community Credit Institutions, the São Paulo Confia program, and the Popular Bank of Santo André.

SCM: the Micro-entrepreneur Credit Society (SCM) is a special kind of entity under the control of the Central Bank of Brazil (BACEN). It was created as a profit-making institution, with the exclusive purpose of operating in microcredit.

Public Funds: these are microcredit initiatives from states and municipalities. At the sites of the 27 federated units, 14 indicated the existence of a microcredit program. In this category, the program Banco do Povo Paulista (São Paulo State Bank for the People) stands out, with 10 years of operation in 2008.

Independent Credit Cooperatives: Soares and Melo Sobrinho (2008), while mapping the evolution of credit cooperative regulations issued by the Central Bank, selected two moments that were milestones in the effective engagement of these organizations into the productive microcredit activity. The first moment was marked by the issuing of Resolution 3,058, of December 10, 2002. This document allowed the creation of cooperatives of small entrepreneurs and micro-businesses. Formerly this type of organization was only authorized for rural activities. Besides, the focus on micro and small entrepreneurs became a priority.

The second moment resulted from Resolution 3,106, of June 25, 2003, which introduced the possibility of creating free-admission cooperatives. The authors say that the approval of this document became a great benefit for the cooperative and financial sectors, for it enlarged the scale of the service and, consequently, brought about smaller spreads and fees.

In practical terms, free admission brought microcredit services nearer the potential demand. To give an example, a self-employed merchant, like a pop-corn seller, does not need to find another 19 people in the same trade to form a credit cooperative. Joining a free-admission cooperative he may get individually the credit he may need.

1.4 Assessment of microcredit supply in Brazil

1.4.1 Previous studies

The last published survey of microcredit supply in Brazil is reported by Soares and Melo Sobrinho (2008), and contains information additional to the reports on the activities of the PMNPO. Its numbers are shown in Table 1.

Table 1 – Microcredit offer, December 2006 and December 2007 (average loan value in R\$)

Type	Dec/2006		Dec/2007			
	Entities	Clients	Entities	Clients	Average Loan value	Total loans (R\$ x 10 ⁶)
SCMs	56	21,286	53	20,145	2,531.92	51.01
NGOs, OSCIPs and Public Funds	136	89,997	143	94,856	724.47	68.72
CrediAmigo	1	235,729	1	299,975	782.07	234.60
Micro-entrepreneurs’ cooperatives	23	33,672	27	64,637	3,921.06	253.45
Private banks	4	42,083	4	65,587	1,680.00	78.80
Foreordained funds	--	267,512	--	518,182	970.74	503.02
Total	220	690,278	228	1,063,383	1,768.38	1,189.49

Source: Soares e Melo Sobrinho 2008

Foreordained funds come from the “2% of call deposits received by various financial entities, except credit cooperatives, under Law 10,735/2003 (...)” (Soares; Melo Sobrinho, 2008: 30). In order to estimate the supply of oriented productive microcredit, this value should not be considered (it either represents the microcredit supply or the productive microcredit supply).

Comparing data of 2007 with those for 2005, as presented by Monzoni Neto (2006), one may see a remarkable growth in oriented productive microcredit. Data for 2005 are shown in Table 2.

Table 2: Microcredit supply in 2005 (value of active portfolio in R\$)

MFI name	MFI type	N ^o active clients	Value active portfolio
Banco do Nordeste	Public bank	195,378	136,200,000.00
CEAPE – MA	OSCIP	14,018	7,600,000.00
CEAPE – PE	OSCIP	4,610	5,400,000.00
CEAPE – RN	OSCIP	3,265	2,200,000.00
CEAPE – SE	OSCIP	2,679	2,000,000.00
S. PAULO CONFIA	OSCIP	3,458	2,630,000.00
CEAPE – RS	NGO	2,111	2,300,000.00
BANCO DA MULHER	OSCIP	1,400	1,800,000.00
VIVACRED	NGO	4,800	4,700,000.00
Others	NGOs & OSCIPs	50,107	32,570,000.00
MICROINVEST– UNIBANCO	SCM	5,100	12,000,000.00
Others	SCM	29,052	72,340,000.00
REAL MICROCREDITO	Private bank	8,236	11,190,000.00
TOTAL		324,214	292,930,000.00

Source: Monzoni Neto (2006)

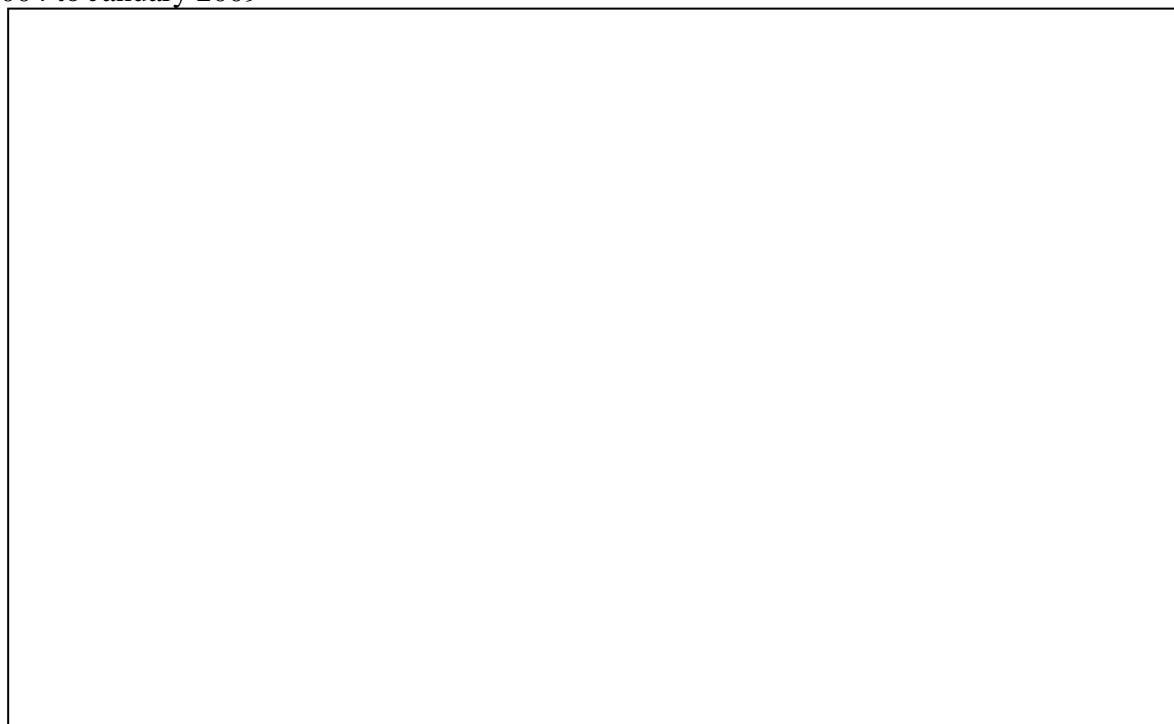
Looking at the number of active clients in Table 2, it can be seen that it almost trebled between 2005 and 2007. This growth is even more robust if 2007 is compared with 2001. Nichter *et al.* (2002) estimated the number of active clients in 2001 at 159 thousand. Comparing this number with the one obtained by Soares and Melo Sobrinho (2008), in Table 1, one can see that the number of active clients has grown almost sevenfold between 2001 and 2007.

1.4.2 Central Bank Statistics

Since January 2004, the Central Bank (BACEN) supplies information about resources directed to microcredit (consumption and productivity). This section will show the evolution of the numbers in productive microcredit.

According to BACEN, the balance of funds directed to productive microcredit has been growing remarkably, as shown in Figure 1.

Figure 1: Evolution of the balance of funds directed to productive microcredit, from January 2004 to January 2009



Source: Central Bank of Brazil (BACEN)

If a comparison is made between productive microcredit and total credit operations, and also between the former and the total loans made to natural persons, one can see that in several moments productive microcredit has grown at a higher rate than other forms of credit offered in the market, as shown in Table 3.

Table 3: Comparison between productive microcredit, loans to natural persons and total loans, from 2004 to 2009

Period	Productive microcredit R\$ x 1,000	% ⁽¹⁾	Credit to nat. persons R\$ x 10 ⁶	% ⁽¹⁾	Total credit R\$ x 10 ⁶	% ⁽¹⁾
Dec 2004	197,383.60	-	136,455.81	37.84	498,721.51	19.24
Dec 2005	197,383.60	47.59	188,783.82	38.35	607,023.30	21.72
Dec 2006	301,050.13	52.52	235,815.59	24.91	735,589.65	20.69
Dec 2007	355,043.39	17.94	314,352.79	33.31	935,972.83	27.76
Dec 2008	509,529.31	43.51	389,540.87	23.92	1,227,294.10	31.13
Feb 2009	512,729.77	0.63 ⁽²⁾	399,092.06	2.45 ⁽²⁾	1,229,016.00	0.14 ⁽²⁾

Source: Central Bank of Brazil (BACEN)

(1) growth rate in relation to the same period, previous year

(2) growth rate in relation to December 2008

1.4.3 Considerations about the Evolution of Productive Microcredit in Brazil

Once the amounts and the growth speed of productive microcredit are known, it is important to name some players that perform an important role in the market. Their names are in the papers of Soares and Melo Sobrinho (2008) and Monzoni Neto (2006).

According to the numbers shown, one can see that CrediAmigo (Banco do Nordeste/ Instituto Nordeste e Cidadania) and Real Microcredito (ABN Amro) together have more than 50% of

the market. Adding their active portfolios³ and comparing the total with the active portfolio of PNMPO⁴, one can see that, in 2008, they made 63.7% of the market.

The extensive participation of those two institutions in the sector also shows that the activities of productive microcredit take place predominantly in the northeastern region, where both of them predominantly operate.

Although some conclusions may be taken from the data presented, it is not possible to reach a firm assessment of the sector. There is no updated information on the SCMs and few systematized and consolidated data about the cooperatives concerning productive microcredit. It is worth considering that only the ANCOSOL system, which, by its nature (familial agriculture), fits the concept of productive microcredit, has accumulated from June 2007 to June 2008 a total of R\$ 261,207,000.00 in microcredit operations, comprising 198 independent credit cooperatives.

Summarizing, the productive microcredit (and the conditioned productive microcredit) has a large potential market and is already expanding at a considerable speed. Should it keep the present speed for some 10-15 years, the market will be totally served.

³ CrediAmigo, December/2008 = R\$ 362,200,000.00 (Source: www.bnb.gov.br) ; Real Microcrédito, December/2008 = R\$ 88,811,000.00 (Source: contact with the Program operators). Sum: R\$ 451,011,000.00.

⁴ Total active portfolio PNMPO, December/2008 = R\$ 708,162,212.65 (Source: PNMPO, 2008)

PART 2 – INFORMAL ECONOMY AND MICROFINANCES: EVIDENCES FROM THE DATABASE OF ECINF

2.1 Definition of the potential market

The object of this part of the paper is to explore the social-economic characteristics of informal workers who constitute the main target public of microfinances in Brazil. We shall use information from the Informal Urban Economy (ECINF), a public database under the responsibility of IBGE (Brazilian Institute of Geography and Statistics). The option for ECINF is due to the fact that it gives socioeconomic information on autonomous workers and employers with up to five employees who operate informally at the economy. ECINF is a rich source of data on a relevant part of the target public of the MFIs as one can see in the table below. Paradoxically this database is not very explored in studies related to the several themes of microfinance, above all microcredit and microinsurance.

Table 4: Percentage of informal clients per region where MFIs operate

Region	Total
North	99%
Northeast	84%
Southeast	90%
South	74%
Central-West	76%
Total	83%

Source: Prêmio Itaú Apoio ao Empreendedor (Itaú Bank Award to Stimulate Entrepreneurs)

As a starting point for this analysis, the amount of R\$ 1,000 was defined as the ceiling income of the autonomous workers to be investigated in this section. The choice of this amount was based on three reasons. The first is that this number is very near the median of the 39 institutions analyzed by Banco Itaú in its study (2005) titled “Diagnóstico das Instituições de Microcrédito no Brasil” (A Diagnosis of the Microcredit Institutions in Brazil). The second is that this parameter corresponds to the methodology adopted by the *Microbanking Bulletin*. Finally, the third reason is that this procedure follows the one adopted by SUSEP in its Partial Report for 2008 (GT Microseguros), though in this report it is recognized that other variables – like education (years of schooling) – should be considered in the identification of groups eligible to use Microinsurance, beside the fact that, in the report, the income cutting limit was clearly higher than the one adopted here.

Table 5: Proxy of relative poverty (average loan value/GDP per capita)

Region	GDP per capita*	1,000/GDP per capita
Central-West	9,823	10%
North	4,642	22%
Northeast	3,498	29%
South	9,185	11%
Southeast	9,977	10%

* values referred to 2003

Source: Ipeadata

Table 5 contains two fundamental indications. The first relates to the differences between the regional per capita GDPs. It is easy to see that, if the definition of poverty is based exclusively in income, the north and northeast are much poorer than the other regions. This comparison must be taken cautiously, since although the incomes are expressed in real terms, no allowance was made for the difference in cost of living in each region.

To avoid this problem, *Microbanking Bulletin* defends that the comparison between loan values granted by MFIs that operate in different regions should be made using the per capita GDP as a reference, that is to say, the value of the loans should be expressed in terms of the correspondent regional per capita GDP. That is exactly what is shown in the last column of Table 5. The amount of R\$ 1,000 is very near the average value of loans granted by CrediAmigo and the median of the 39 institutions analyzed by Banco Itaú in its study (2005) titled “Diagnóstico das Instituições de Microcrédito no Brasil” (A Diagnosis of the Microcredit Institutions in Brazil).

Dividing the values by the regional per capita GDP, we come to a number which is commonly used as a proxy to evaluate the focus of the MFIs. According to the *Microbanking Bulletin*, this number should not be higher than 25% of the per capita GDP. Looking at the table, one can see that only in the northeast this ratio is more than 25%. Nevertheless, if the per capita GDP is duly adjusted to the regional cost of living, the ratio would come nearer to 25%.

Table 6 shows the number of informal workers divided into two groups, the autonomous and the employers with up to five employees. It is noticeable that the number of autonomous workers corresponds to almost six times the number of employers.

Table 6: Composition of workers in the informal economy

Region	Autonomous	Employers
North	87%	13%
Northeast	87%	13%
Southeast	84%	16%
South	80%	20%
Central-West	81%	19%

Source: ECINF, 2003

Due to the high proportion of autonomous workers, this report will focus only the sample that represents this category. Furthermore, a limit of R\$ 1,000 will be adopted for the familial earnings. Thus, the potential market here defined is composed of informal autonomous workers with a familial monthly income of less than R\$ 1,000.

2.2: Socio-economic characteristics of the potential market

It is vastly known the preference of some institutions for female clients, as shown in the literature about microfinance. The reasons for this predilection have been previously analyzed. Basically, empirical studies and the experience of credit agents have come to the conclusion that women are wiser in allocating resources amongst the members of the family and less prone to fall behind in paying the installments on loans. Table 7 shows informal autonomous workers with incomes up to R\$ 1,000 (October 2003) classified by gender.

Table 7: Composition by gender of autonomous workers with monthly income up to R\$ 1,000

Region	Men	Women
North	50%	50%
Northeast	55%	45%
Southeast	39%	61%
South	48%	52%
Central-West	48%	52%

Source: ECINF, 2003

Except in the southeast region, the proportion between men and women among the self-employed is well balanced. In the southeast the proportion of women is much higher than men.

This datum may be useful for the MFIs that give priority to women in the formation of solidarity groups or loans to groups (PIZA, 2005). The next table presents the level of instruction, by region, for the autonomous workers with incomes up to R\$ 1,000.

Table 8: Schooling status of autonomous workers with monthly income up to R\$ 1,000, per region

	North	Northeast	Southeast	South	Central-West
No schooling	156 (4%)	563 (7%)	204 (6%)	54 (3%)	29 (3%)
Read & write	131 (4%)	371 (5%)	149 (4%)	45 (2%)	34 (3%)
Incomplete grammar school	1288 (36%)	2588 (34%)	1157 (34%)	613 (29%)	280 (28%)
Complete grammar school	438 (12%)	871 (11%)	365 (11%)	332 (16%)	162 (16%)
Incomplete High school	433 (12%)	781 (10%)	309 (9%)	190 (9%)	101 (10%)
Complete High School	846 (24%)	1786 (23%)	796 (23%)	572 (27%)	236 (23%)
Incomplete College	107 (3%)	270 (4%)	114 (3%)	81 (4%)	52 (5%)
Complete College	166 (5%)	453 (6%)	314 (9%)	235 (11%)	124 (12%)
Total	3,565 (100%)	7,683 (100%)	3,408 (100%)	2,122 (100%)	1,018 (100%)

Source: ECINF, 2003.

The data show that more than 50% of the autonomous workers do not have high school education, with the highest percentages in the north (68%) and northeast (67%). This seems to show a negative (positive) correlation between the per capita GDP (poverty) and level of instruction in each region.

One of the most important discussions in the world of microcredit deals with the depth of outreach, i. e., to what point those institutions are actually assisting the poorest of the poor. The database of ECINF may be used to explore preliminary this topic of interest. The table below illustrates this discussion and shows the proportion, by gender, of autonomous workers with an income up to the minimum wage.

Table 9: Proportion of autonomous with an income of up to the minimum wage in 2003

Group	Estimate	Poverty line
Men	2.98%	240.00
Women	2.97%	240.00
Sample	2.98%	240.00

Note: minimum wage in 2003 was at R\$ 240.00

Source: ECINF, 2003.

Estimates for men and women are extremely similar to each other and, consequently, to the result of the sample. For both sub-samples, about 3% of autonomous men and women had an income of R\$ 240.00 or less in October, 2003. Therefore, if we adopt this value as the limit for

the line of poverty, we would have about 3% of men and women below this line. For this public (the poorest of the poor), the microfinance studies indicate a low possibility of inclusion through usual business models, showing the need of a public policy sponsored by the State. Anyway, there is evidence that a substantial part of the poor can be attended by inclusive business models.

2.3 The use of insurance

This section tries to explore the database in search of information about the use of insurance by informal workers, already considering the previous criteria of income (R\$ 1,000) and autonomy. The data will be used for a preliminary analysis of the potential synergy between microcredit and microinsurance. The argument is based on the economies of scale that can be explored by the microfinance institutions considering that the characteristics of those that seek microinsurance are very similar to those of microcredit clients.

Although the financial needs of informal, low-income workers are relatively modest, the risks involved in their activities may be considered relatively high. With a precarious production technology and low specialization, the payoff of the investments tend to be low, since there is no investment diversification, the production scale is very limited and available market savings and insurance to soften adverse shocks are limited (Piza, 2005). Considering these facts, families that depend on subsistence activities become vulnerable to adverse exogenous shocks that impair their cash flow and their consumer habits (Zeller, 1999).

The first step in this analysis consists in checking whether the persons that used credit, loans or other type of financing in 2003 had access to some type of insurance. Though ECINF does not contain information whether the person had resorted specifically to an MFI, on limiting the income level of informal workers to R\$ 1,000, it is believed that the sub-sample thus obtained corresponds to people that are apt to try the services offered by the MFIs. The main conclusion is that greater use of credit does not keep a relationship with greater use of insurance.

Table 10: Usage of credit and insurance by autonomous workers with monthly income up to R\$ 1,000 in 2003.

Credit user?	Insured?	
	No	Yes
No	(80.6%)	(19.4%)
Yes	(79.5%)	(20.5%)

Source: ECINF, 2003

The following tables show information about the type of insurance most sought for by low-income workers.

Table 11: Demand for life insurance among autonomous workers with monthly income up to R\$ 1,000 in 2003.

Region	No life insurance	With life insurance
North	61%	39%
Northeast	65%	25%
Southeast	53%	47%
South	55%	45%
Central-West	60%	40%

Source: ECINF, 2003

There is a potential demand for life insurance for the poor. Besides, the different researches already carried out reinforce the arguments of Morduch (2006) about the importance of such type of insurance for poor families. In the event of death of the family head, the insurance can be of extreme usefulness for (i) avoiding an abrupt reduction of consumption and (ii) helping to face funeral expenses. Besides, it is known that, contrary to other types of insurance, life insurance is less prone to have problems of asymmetric information – moral hazard and adverse selection – thus becoming the preferable candidate of many institutions when they extend their products to the poor.

Examining the operations of MFIs, life insurance shows at the top of the list of the products offered, due to its lesser degree of complexity for the MFI. For example, FINCA, in Uganda, offers life insurance to its clients of credit, charging an additional 0.5% to the interest for the loan operation (Morduch, 2006). This strategy shows the scale gains to be explored by the MFIs and the insurance companies, with evident benefits for the clients.

In general, the second type of insurance most mentioned in microfinance is health insurance. There are innumerable reports about poor people who could escape the condition of extreme or chronic poverty simply by ingesting vermifuge. A great number of people die of dehydration, diarrhea and other diseases associated with worms (Ray, 1998). This way, health insurance and life insurance would walk side by side. This is the reason why Morduch (2006:348) concluded that life and health insurance are complementary in reducing the vulnerability of poor people.

Nevertheless, it is known that this type of insurance demands coping with the problem of agency, which may raise the cost of the product and, at the same time, demand a certain degree of administrative sophistication. This brings up, once again, the potential synergy between microcredit and microinsurance. The agency problems observed in the microinsurance are exactly the same that inhibited for a long time sustainable microcredit operations. However, the innumerable successful cases of MFIs, also in Brazil, show that microcredit players have developed innovative mechanisms to mitigate risks associated with information asymmetry.

The following table pictures the demand for residential insurance for the potential market here defined. This is another product of potential relevance (but with low penetration among the poor), since a large part of the micro-endeavors takes place in the residence of the entrepreneur.

Table 12: Demand for residential insurance from autonomous workers with monthly income up to R\$ 1,000

Region	No insurance	With insurance
North	96%	4%
Northeast	95%	5%
Southeast	80%	20%
South	82%	18%
Central-West	94%	6%

Source: ECINF, 2003

The database from ECINF brings interesting information about private social security, which is but a form of savings. The demand for this kind of insurance from the poorest informal workers, as shown by the table below, reinforces the need to demolish the myth that “poor people do not save”. Studies in several countries have demonstrated the existence of various informal savings (and insurance) mechanisms among people that do not have access to the conventional banking system. The most common of such mechanisms is the acquisition of physical assets, basically animals (Ray, 1998). The table below reveals simultaneously the existence of this market and its unexplored potential.

Table 13: Demand for private social security from autonomous workers with monthly income up to R\$ 1,000

Region	No private social security	With private social security
North	76%	24%
Northeast	77%	23%
Southeast	78%	22%
South	82%	18%
Central-West	87%	13%

Source: ECINF, 2003

2.4 Potential market and access to financial products

This section deals with the access to an assemblage here defined as the potential market for microinsurance and some financial services. From the viewpoint of microfinance, this discussion has to do with the role of the financial system in contributing to economic development and, more specifically, in the item of fighting poverty. In Brazil this discussion is incipient, for there is no consensus about the concept of bank access. Obviously, such discussion transcends the scope adopted here and, from a practical point of view, an exploratory analysis of the potential market of microinsurance in relation to access to financial services is important.

Starting by the access to check accounts, table 14 shows that, in spite of the governmental program of creating simplified accounts, a major part of the population, especially in the north and northeast regions, still does not have access to this product. Table 15 has special interest for microfinance studies because savings accounts are one of the basic mechanisms through which the poor deal with adverse events. As a whole, the analysis is similar to that of the preceding table, showing low penetration of savings, chiefly in the north and northeast. Thus, a product which is potentially a replacement for microinsurance is not used for that purpose.

Table 14: Number of workers with income up to R\$ 1,000 that had checking accounts in 2003

Region	Yes	No
North	29%	71%
Northeast	32%	68%
Southeast	53%	47%
South	50%	50%
Central-West	49%	51%
Total	38%	62%

Source: ECINF, 2003

Table 15: Number of workers with income up to R\$ 1,000 that had savings accounts in 2003

Region	Yes	No
North	21%	79%
Northeast	24%	76%
Southeast	27%	73%
South	27%	73%
Central-West	32%	68%
Total	25%	75%

Source: ECINF, 2003

Table 16: Number of workers with income up to R\$ 1,000 that had credit cards in 2003

Region	Yes	No
North	23%	77%
Northeast	27%	73%
Southeast	34%	66%
South	32%	68%
Central-West	36%	64%
Total	29%	71%

Source: ECINF, 2003

The penetration rate of credit cards shown above reveals some paradoxes. Firstly, as confirmed by various studies, credit cards have quite a presence in Brazil, even among the poor. Nevertheless, especially when directed to the low-income public, the potential market is still large. Studies on microfinance involving credit cards are still scarce in Brazil, but they are another potential channel for inclusive businesses.

The table below shows one of the most interesting aspects of the access to financial services in the informal economy. It shows clearly that banking correspondents are part of the day-by-day life of the public and constitute the main channel for paying bills in the poorer regions, the north and the northeast. It should be noted that the postal bank (at the Post Offices), which appears in the table, is also a correspondent of sorts. The potential of these correspondents to offer products and financial services is very high, as will be seen afterwards.

Table 17: Main locales for paying bills used by autonomous workers with monthly income up to R\$ 1,000

Region	Bank branch	Postal bank	ATM	Banking Correspondents	Debit in account	Telephone	Internet	No fin. transactions
North	28%	11%	2%	47%	1%	0%	1%	12%
N.East	26%	6%	2%	49%	1%	0%	1%	16%
S. East	45%	4%	3%	29%	3%	0%	3%	12%
South	40%	6%	2%	40%	2%	0%	2%	7%
Center-W	40%	1%	3%	43%	3%	0%	3%	7%
Total	32%	6%	2%	43%	1%	0%	1%	13%

Source: ECINF, 2003

PART 3 – MICROCREDIT AND MICROINSURANCE: ANALYSIS OF SYNERGY

3. Innovations about microcredit and microinsurance

Innovations introduced from the 1970's, notably with the creation of the Grameen Bank in Bangladesh, represented a great rupture with the traditional mindset of the financial community. Lending low amount resources without guarantees for a generally informal public seems quite contrary to what is prescribed by the credit risk management manuals. However, the success of uncountable microcredit institutions the world over, mostly due to low rates of default and effective losses, shows that there is room for inclusive business models, capable of integrating the poor into the market in a sustainable way.

This set of microcredit innovations must be somehow used to bring to the poor other financial products, mainly those related to microinsurance. Due to the methodology of the MFIs and to the characteristics of the enormous market of low-income people, there is a relevant potential of synergy between microinsurance and microcredit that should be explored. It is worth reminding that such synergy is not only related to the possibility of obtaining better economic results (though this is essential to promote new business models), but also to offer products of greater impact on the well-being of the poor, who need credit as well as insurance.

3.1 Synergy through the credit agent

Credit is a financial service typically based on relationship. The so-called microcredit has been innovative by creating a new form of relationship through the credit agent, as described at the beginning of this paper. The diverse market researches⁵ on microcredit invariably point to mistrust and scant knowledge about insurance. This is aggravated by the low schooling level of the public. The fact is that potential clients find it difficult to obtain information about the real benefits brought out by insurance. The general perception is that insurance is an expensive product and the public fear about to whom they should claim in case of necessity.

So, for the commercialization of microinsurance it is essential to create proximity and interaction along time so as to build a relationship based on trust. At the post-sale phase, researches indicate that keeping a periodical contact with the client makes him feel protected and safe to keep the payments going. Microcredit, as well as microinsurance, may be inserted in the concept of "Proximity Finances", understood as those originating from *direct and permanent* contacts with the productive agents. Abramovay (2004) points out that organizations operating under the concept of proximity finances are able to convert social relations between individuals, enterprises and institutions into transactional cost reductions.

In practical terms, the great innovation capable of turning feasible a permanent contact with the poorer is the credit agent, described above as one of the innovations of microcredit. This is where a fundamental element of the synergy between credit and insurance lies. Insurance is still viewed with mistrust, originating many doubts in the potential client, caused by lack of information and also lack of schooling. All this is relieved by the presence of the credit agent, who looks for the client, speaks his language and gives orientation about his deals.

A research by the Boston Consulting Group revealed that a significant part of the poor has interest in the product insurance, but at the same time believes they cannot afford it. However, looking at some types of insurance already operative, with a cost of R\$ 10/month, a paradox appears, because at this price accessibility exists (although limited to the offer of few players). Once more there is a problem of information because people do not realize that insurance is compatible with their financial resources and, at the same time, feel doubtful about prices that seem too low.

⁵ The several researches here mentioned are: Novos Produtos e Canais de Venda em Microseguros (New Products and Selling Channels in Microinsurance, Data Popular), Next Billion Customers (Boston Consulting Group) and Microseguro: Negócio ou Inserção Social (Microinsurance: Business or Social Insertion – Fenaprevi).

The same research has shown that, among the poor, individual incomes are generally considered as a package within the family and, consequently, decisions are taken jointly, so it is necessary to know and/or influence the members thereof. In other words, the profile of the family is as important as that of the individual for certain decisions. For sure, buying insurance is among those decisions.

In all the above cases, the credit agent may have a vital role as a reliable source of information to the client, having a better chance to influence and know specifics about the domicile and not only about the individual. Therefore, if the potential clients of microinsurance look for assurance along all the acquisition procedures: good counseling, clarity of the product, channel, means of payment and relationship, the presence of the credit agent stands a good chance to cover all these requirements.

Furthermore, researches indicate that there is no specific quest for insurance among the poor. In general, the access to insurance occurs through other services. The credit agent could become the promoter and the connecting link between microcredit and microinsurance.

3.2 Synergy through frequency of payments

One of the important innovations in microcredit comes from the frequency of payments. No matter what product is offered – credit or insurance – it is important that the rhythm of payments matches the cash flow of the clients. Surveys indicate that around 50% of the poor are paid fortnightly, weekly or daily. Besides, they show that a crucial element for the acquisition of insurance is flexibility of payments, since income flow of the poor is irregular.

Several MFIs in Brazil already adopt flexible payment systems, as is the case of community banks in the CrediAmigo program (Banco do Nordeste), the São Paulo Confia and the CEAPE-MA. Thus, concerning preferences of the demand as well as existing business models (in microcredit), the frequency of payments indicates potential synergy between microcredit and microinsurance.

3.3 Synergy through focus on women

A research made by Data Popular showed that women have a better understanding about the benefits of insurance, manifesting greater interest in this type of product. In fact, as described in the first section, women are more concerned about keeping the family well-being, above all their children's. Women perceive, for instance, that in case of death of the family head, insurance can be extremely useful for (i) avoiding an abrupt reduction in consumption and (ii) paying the funeral expenses.

It is known that a considerable part of microcredit operations are directed to women. In the case of Grameen, around 95% of their clientele are women. In the model of the FINCA community banks the percentage of women is similar. An ample research⁶ about MFIs in Brazil revealed that about 55% of microcredit clients are women. The predominance is observed in 25 of the 37 institutions that answered the query. In April 2009, the CrediAmigo program (reminding, the amplest productive microcredit player in Brazil, run by the Northeastern Bank – Banco do Nordeste Brasileiro) reported that 65% of its operations were directed to women.

Although in Brazil there are no major microcredit institutions clearly focusing especially on women, there is evidence that, in practice, operations have privileged women. Focus on women means, therefore, an evident potential synergy between the offer of microcredit and the offer of microinsurance.

⁶ Diagnosis on Microcredit Institutions in Brazil, Itaú Award 2005.

3.4 Potential interest of MFIs in microinsurance in Brazil

The basic activity of MFIs all over the world is the offer of loans to the low-income population. MFIs are subjected to the same risks as their clients. When an adverse occurrence hits upon a debtor or his family, the effect on the capacity for microcredit repayment is immediate. Consequently, the incorporation of insurance to the business model of MFIs can aggregate value and serve as an important tool for credit risk management.

Taking as an example the simplest case, i. e., the life risk of the clients, the main options for the MFI would be:

- (i) Ask for cooperation from the other member of the group, if the loan was made in this modality. Market experience signalizes that, in these cases, the group tends to resist, with negative effect on the default rate. The MFI still runs the life risk on other member of the group;
- (ii) Write off the loan, an obviously costly option that affects financial sustainability. In this case, it is necessary to keep track of losses associated with the event (death) in order to segregate them from other losses, to check which costs are specific for that event;
- (iii) Charge an additional rate (self-insure) on the loan. At granting the microcredit, MFIs could transfer to the borrower the costs associated with life risk, raising the interest rate. The proceeds of this supplementary charge could be posted as a reserve fund to be used in case an adverse event occurs. This procedure could be extended to other types of risk. However, the great problem here would be, on the one hand, the greater complexity of needed controls, which can deviate the MFI from its core business, and on the other hand, the price may become excessively high for the takers.
- (iv) Partnership with an insurance company. One of the possible solutions would be the MFI offering microinsurance as an agent for an insurance company. From the standpoint of the MFI, the advantage would be to obviate the risk (life) from the portfolio. Besides, aspects related to the administration of the processes may be facilitated by the presence of an insurance institution, familiar with the procedures related to this type of service. The disadvantage would be the difficulty in finding an adequate partnership, capable of generating mutual benefits.

The advantages and disadvantages mentioned above and the current degree of sophistication of the MFIs, beside their degree of capitalization and access to financial sources indicate that the best option should be a partnership with an insurance company. Resorting to other members of the group or absorbing the loss are not First Best strategies in Brazil. In the former case, not all the products of the institutions are group credit, some are individual insurance. In the latter case, a simple writing-off of the loss does not seem justifiable since there is the possibility of sharing the risk with an insurance company. Although helpful, the creation of a reserve fund has the disadvantage of not eliminating the risks of covariance.

An actual event, symbolic of the importance of microinsurance for the MFIs is what happened with CEAPE-MA. The institution is known as one of the best OSCIPs of microcredit in Brazil. It has about 25,000 clients and is now going through a transitional phase from a non-profit OSCIP to another model in which profits are admitted. The months of April and May were especially hard for CEAPE-MA in view of the floods that occurred in the Northeast, especially in the state of Maranhão.

In a concrete example of covariance risk, as there is little geographic diversification in the portfolio, all concentrated in Maranhão, the effects of the flood were in great extension passed over to the MFI. As this is a recent event, numbers for an in-depth analysis are not yet available. However, an interview with the executive director of CEAPE-MA revealed that there was a

surge in the rate of default. A partnership with some insurance company could have mitigated the risk to the portfolio.

3.5 Potential distribution channels: the case of correspondents

Market surveys on microinsurance strongly stress the role of non-banking correspondents in the life of the poor. The research made by Data Popular found out that correspondents are the choice place of people interviewed for making their payments. The two main reasons for that are easy access and reliable, though informal, atmosphere.

For those who study the question of microfinance, Brazil has promoted a real revolution in giving the poor access to financial services with the model of correspondents. Nowadays, around 90% of all correspondents in the world are in Brazil. In 2000, a third of Brazilian municipalities did not have a single point of access to banks. Their population had to travel long distances just to pay a bill or to receive a retirement benefit. Adaptations in the rules of the financial market, chiefly aiming at the expansion of the (then called) Bolsa-Escola program allowed the Federal Savings Bank (Caixa Econômica Federal) to use its network of lottery-betting shops to pay this benefit to the poor population in a much large number of localities.

In parallel, taking advantage of the new regulations, many Northeastern networks of shops integrated their services electronically with the banks, transforming pharmacies, small markets and other retail shops into banking service points. In the Northeast this was especially important, since banking services in that region was scarce. This is how the model of correspondents created, leveraging the expansion of financial services in Brazil to less developed regions and low-income populations.

In 2003 there were no localities in Brazil without access to financial services. In 2009, with around 127 thousand points, correspondents outnumbered bank branches more than six to one. Thanks to the sophisticated network technology that supports its infrastructure, correspondents are already the main low-income banking channel in Brazil. It is through them that the population pays the majority of their bills, receive governmental benefits etc. It is also remarkable the significant number of simplified banking accounts opened at the correspondents, without the account holder having to go to a bank.

Table 18: Banking correspondents. Evolution of points of attendance per region

Region	2000	2003	2006	2007
Central-West	3,482	4,334	7,766	7,884
Northeast	7,450	10,276	18,092	18,149
North	2,837	3,399	3,134	3,332
Southeast	42,116	50,852	49,084	47,500
South	7,624	9,678	17,158	18,984
Brazil	63,509	78,539	95,234	95,849

Source: Central Bank of Brazil

Up to now, researches indicate that there is a large space to amplify the offer of financial services to the poor through the correspondents. Various studies show that the use of correspondents as a technological infrastructure to support the activities of MFIs – credit selection, distribution and monitoring – appears to be promising. *To include microinsurance* in this roll of services would be quite natural. It should be also said that although MFIs and Credit Cooperatives are allowed to become correspondents, few of them have adopted this role.

Correspondents are still much concentrated in the southeast region and focus chiefly in paying and collecting. However, the evolution of this channel in the country shows a gradual but

consistent regional deconcentration and an increase in the diversity of offered services, something that may attract other financial institutions beside a more effective exploration of all its potentiality by traditional banks.

Thus, the potential synergy between microinsurance and microcredit can be fostered through the development of business models which, starting from the existing channel of the correspondents, go beyond the present focus centered on typically transactional products like payments. Furthermore, the use of correspondents amplifies the potential synergy with microcredit because it includes the possibility of partnerships with credit cooperatives, whose volume of credit and clients is many times larger than that of the traditional MFIs.

3.6 Important points in the interaction microcredit-microfinance

Four interviews⁷ were carried out with four institutions, operational and potential, concerning microcredit and/or microinsurance. The main objective was to hear the participants' comments on the main points related to the development of business models for joint microcredit/microinsurance operations. Their principal observations are listed below. It should be noted that they represent the opinions of the interviewed, not of the authors of this paper. Furthermore, the items listed contain only the passages duly authorized by the interviewed.

- i) The MFIs perceive the added value of microinsurance chiefly for the potential reduction of losses by default. The potential for generating revenue is perceived as relatively low;
- ii) Among the MFIs there is a clear understanding that the credit agent may be used for the distribution of several services, financial or not. Microinsurance is one of such services;
- iii) MFIs stress that the productive microcredit needs a proactive publicity. People do not look for it, it is up to the credit agent to go after potential clients. It is the same with microinsurance. MFIs already have a relationship and a methodology to take the product to the client, chiefly by using the credit agent;
- iv) MFIs single out life insurance and accident insurance as the two products with more potential demand among microcredit borrowers;
- v) MFIs say that insurance companies offer a choice of products which are, almost always, incompatible with what is needed by the poor;
- vi) Mainly among the smaller MFIs, there is a suspicion that a partnership with an insurance company would be only an "excuse" to get in touch with the clients of the MFI. Once the access is established, principally if the insurer is connected with a bank, the next step would be to offer other products, especially credit, creating a competition with the MFI itself;
- vii) For the larger MFIs, mainly those linked to banks, the greatest problem is to offer a product fit to the reality of the clients and adjusted to the set of procedures of any other product offered by the bank. For example, to issue a payment voucher with non-monthly payments, how to make the controlling system of the insurance company compatible with those of the MFI?
- viii) If the MFIs use their credit agents to distribute insurance, when the time for collecting arrives, there would be difficulty in sending the agents only to "collect insurance premiums". This would occur with clients that would choose to keep the insurance while not asking for new credits or renewing existing ones;
- ix) MFIs emphasize that, in the use of correspondents, it is necessary to develop more adequate models. São Paulo Confia said that it received a proposal for its credit agents commercialize also insurance. However, the credit agent should also be re-

⁷ The institutions were: São Paulo Confia (microcredit OSCIP), American Life (insurer that started a microinsurance program in 2009), Real Microcrédito (a microcredit initiative of Banco Real) and Bradesco bank.

- sponsible for filling the insurance form for the client and taking it, with the client, to the nearest correspondent. In the opinion of the institution, this procedure is not efficient and is time-consuming.
- x) The coupling of microcredit and microinsurance may be an important niche for the small and medium-sized insurance companies. High fixed costs of larger insurers may end by invalidating the development of partnerships with institutions whose client portfolio is small. The small and medium-sized insurance companies would have more flexibility to offer products adequate to the reality of the MFIs.
 - xi) Insurance companies know very little about the world of the MFIs. The main reason for this lack of knowledge may be the absence of a microcredit model consensually accepted in the Brazilian market. There is no demonstration effect in the exclusive case of the MFIs. The lack of knowledge has prevented the formation of partnerships, especially between the small and medium-sized insurance companies and the MFIs.
 - xii) Projects about microinsurance should carefully avoid forcible sales (by hook or by crook). Many traditional insurance products are so commercialized.
 - xiii) For insurance companies, partnerships with MFIs should reduce the costs of project implementation, because it would be cheaper to train the credit agent, who has the main asset necessary for the success of microinsurance: access to the clients and their trust.

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