

## PROMOTION PRACTICES REVIEW – BRAZIL – ACCESS TO FINANCE

### I. Main institutions involved in agricultural and rural finance in Brazil

This briefing focuses on government, private sector and third sector interventions to promote equitable access to responsible finance for small farmers – commonly referred to in the Brazilian context as ‘family farmers’.

What follows is an overview of the main actors involved in rural finance in Brazil which are most pertinent to BCI’s interest in access to finance for smallholder cotton farmers. For this reason, large-scale commercial agricultural banking is not included, but where large private banks operate or support rural micro-lending schemes, these are covered.

#### Government

Preferential access to credit for agricultural producers is a key element of the Brazilian government’s agricultural policy, summarised in the table below.

Policy Objective	Programme / Policy instrument
I. Working Capital & Investment Credit Subsidies (for commercial farmers)	<ul style="list-style-type: none"><li>• Production &amp; Marketing Credit (product specific)</li><li>• Production &amp; Marketing Credit (non-product specific)</li><li>• Investment credit</li></ul>
II. Income support programmes	<ul style="list-style-type: none"><li>• Contract option acquisition &amp; Government Acquisition</li><li>• Minimum support programme</li><li>• Equalization Premium Programmes (PEP / PEPRO / PROP)</li></ul>
III. Rural Development & Family Farming Support	<ul style="list-style-type: none"><li>• Production &amp; Investment Credit for Family Farmers (PRONAF)</li><li>• Debt Rescheduling Programmes (Family Farmers)</li><li>• Agrarian Reform Programmes</li></ul>
IV. Debt rescheduling & management	<ul style="list-style-type: none"><li>• Debt rescheduling programmes (commercial farmers)</li></ul>
V. Rural Insurance	<ul style="list-style-type: none"><li>• New rural insurance programme (since 2005)</li></ul>

Source: ICONE, 2008

Whichever course BCI chooses to pursue with regard to improving access to financial services for smallholder cotton farmers will involve close coordination with state actors. It should also be noted that the government’s Agriculture and Livestock Plan 2008 highlights the following areas for agricultural policy development which are entirely focused on improving access to finance: higher supply of resources for the official rural credit system; lower interest rates; higher rural credit limits by borrower; intensification of the use of private credit instruments; increased support to medium-scale agriculture; ensure resources for Rural Insurance Premium equalization; and pursue Rural Insurance consolidation efforts.

The Ministry of Agriculture and Food (MAPA) is responsible for formulation of general agricultural sector development strategies and policies and their implementation. Affiliated to MAPA is the Brazilian Corporation for Agricultural Research (Embrapa –

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*Empresa Brasileira de Pesquisa Agropecuária*), the national agricultural research and extension centre.

The Ministry of Agrarian Development (MDA) was created in 2000 and in 2001 assumed responsibilities from MAPA related to support and promotion of family agriculture. An affiliate of MDA is the National Institute of Colonisation and Agrarian Reform (INCRA – *Instituto Nacional de Colonização e Reforma Agrária*). INCRA's mandate includes the implementation of agrarian reform, maintenance of rural real estate cadastre and administration of federal public lands. INCRA has 29 regional administrations across Brazil. The Centre for Agrarian and Rural Development Studies (NEAD – *Núcleo de Estudos Agrários e Desenvolvimento Rural*) is another MDA affiliate responsible for policy research and analysis, and involvement of civil society in the implementation of rural development policies.

The Ministry of Social Development and Combating Hunger (MDS) was formed in January 2004. MDS is one of the principal bodies responsible for implementation of the Zero Hunger Programme.

The National System of Rural Credit (SNCR – *Sistema Nacional de Crédito Rural*) incorporates 298 federal, state and co-operative banks providing government-supported credit to agriculture. The system is controlled, co-ordinated and supervised by the Central Bank of Brazil. The leading banks are the Banco do Brasil, Banco do Nordeste, Banco da Amazônia, all three of which are mixed public-private banks.

Of these public-private banks, Banco do Brasil is the largest provider of agricultural finance, particularly to large-scale commercial farming. Banco do Nordeste<sup>1</sup> (BNB), operating in the poorest region of Brazil, has a solid track record in the micro-credit market. It has been operating in this field since 1997, but has only recently begun to focus on rural microfinance (see AgroAmigo below).

Affiliated to the SNCR, is the Brazilian National Bank for Economic and Social Development (BNDES), which is under the authority of the Ministry of Development, Industry and Trade. BNDES administers the family farming support programme PRONAF.

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<sup>1</sup> BCI may also wish to note that BNB operates a Programme for Financing Environmental Conservation and Control (FNE VERDE), which seeks to finance environmental protection activities which permit conservation of the environment, including: organic farming projects, including conversion of conventional systems; productive enterprises based on sustainable use of local biodiversity; control, reduction and prevention of soil, water and air pollution; undertaking of environmental studies; environmental certification (ISO 14000 series and green stamps) including consulting and technical support services necessary for implementation of project, as well as hiring of certification institutes; environmental auditing and environmental management systems; projects on efficient use of water and power; and acquisition and implantation of protection equipment for worker health and safety.

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It should be noted that in August 2008, BNDES signed a Socio-Environmental Protocol with the other state banks: Caixa Econômica Federal, Banco do Brasil, Banco da Amazônia And Banco do Nordeste do Brasil. In the ‘Green Protocol’ (*Protocolo de Intenções pela Responsabilidade Socioambiental*), the institutions agree to abide by five general principles, including:

- To finance, by means of credit facilities, the sustainable use of natural resources: this entails continuous improvement of loan portfolio sustainability profiles, proactively financing activities and projects with ‘socio-environmental additionalities’, and guide clients to adopt sustainable production and consumption practices
- To consider the socio-environmental impacts and costs in the management of assets and in risk-screening customers and projects of investment. This entails inter alia, incorporating socio-environmental criteria within the process of project assessment and developing and applying socio-environmental ‘performance standards’

Moreover, public financial institutions such as Banco do Brasil, Banco da Amazonia, Banco do Nordeste and BNDES and also private banks, such as Banco Real ABN Amro, Santander and Bradesco, will not grant loans to any farm named on the forced labour ‘blacklist’ (see Decent Work Practices Review).

Another example of using access credit to promote sustainable change is the federal programme on production and use of biodiesel (*Programa Nacional de Produção e Uso de Biodiesel*) launched in 2004, and which has a strong social component (*Selo Combustível Social*). Producers of agro-fuels enjoy tax relief when sourcing from categories of family farmers, who themselves benefit from access to PRONAF credits provided they produce according to the conditions established by the ‘Social Seal’ (see Decent Work Practices Review).

Production and marketing credit in Brazil are possible since the federal government requires that banks keep a total of 25% bank deposits available for farming credit. (Banks are obliged to hold a certain share of their sight deposits as an obligatory reserve (*exigibilidades*) at the Central Bank, and are given the option of lending 25% of this obligatory reserve to agricultural borrowers at controlled interest rates, instead of transferring it to the Central Bank at zero-interest.) Moreover, rural savings, the BNDES and the Workers Support Fund (FAT) complement the remaining source of funding for agricultural credit. In addition, these funding channels provide preferential loan rates to commercial and family farming which in turn receive the support of the federal government.

### Commercial banks

Under the National Financial System, Financial Institutions (FIs) are identified as either ‘Banking’ or ‘Non-Banking’ FIs:

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- Banking: multiple banks; commercial banks; savings and loan banks; cooperative banks and credit cooperatives
- Non-Banking: investment banks; development banks; finance companies, saving & loan companies and mortgage companies.

This section looks at the main commercial banking institutions in Brazil, in their potential relation to BCI work on access to finance.

The major private lending banks in Brazil are: Bradesco, Banco do Brasil, Banco Itau S.A., Banco Real, Banco Santander S.A., Unibanco, Citibank, Caixa Economica Federal and HSBC. Only a few of these institutions have any real presence in micro-lending, and where commercial banks have developed micro-lending schemes, these have been largely urban-focused.

Micro-lending development is still largely restricted to state-owned banks and state-administered credit lines. The largest rural microcredit scheme in Brazil is the lending facility offered under the PRONAF family farming support programme (to lenders categorised as ‘Group B’ – see below). Within this initiative, Banco do Nordeste has recently expanded its urban microcredit CrediAmigo programme to the agricultural sector under the AgroAmigo banner (see below).

Banco Bradesco is the most important private lender to the agricultural sector in Brazil. However, the vast majority of this portfolio resides in lending to large-scale commercial agribusiness. Bradesco has also purchased the rights to use the national post office network as a banking agent network. By May 2007, “Banco Postal” had an agent network of about 5,600 agents, two-thirds of which were post offices. Out of 18 million Brazilians having access to bank services through Banco Postal, 88% of them have monthly income lower than three times the minimum wage.

Unibanco has offered micro-credit since 1998 through its affiliate Fininvest, focusing on Rio de Janeiro and the consumer segment. It has also inaugurated a São Paulo service through a joint venture with the IFC, called Micro-Invest. While Unibanco’s micro-lending activity has developed significantly in mainly urban low-income areas, there is no focus on lending to agricultural smallholders / family farmers.

ABN-AMRO launched its micro-credit business in 2002 in with Acción Internacional, an NGO that works with micro-finance around the world, and which also worked by Banco do Nordeste and World Bank to establish the CrediAmigo programme in NE. Real Microcredit started operating in Heliópolis and has gradually expanded to other low-income regions, and the Northeastern region in particular. Real Microcrédito now has 53,421 clients, 95% of whom work in the informal sector and most run businesses that can be categorized as commercial/retail or service/production. The range of first loans stretches from \$280-\$655 and the average loan balance, as of end 2007, is \$625.

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Banco Popular (the micro-banking affiliate of Banco do Brasil) uses companies such as Net Cash in Sao Paulo State and Brasilia DF and Pag Facil in Pernambuco to sign up, equip, train, and maintain agents on its behalf. Lemon Bank has no branches at all and relies on 16 agent management companies (including three that it purchased) to manage the majority of its 5,750 agents.

Citigroup has a different approach. It does not deal with individual microfinance customers, but rather establishes relationships with microfinance institutions.

The diagram below summarises the sources of rural microfinance.

Private bank micro-finance	Development Banks	Credit cooperatives	Microcredit companies (SCMs)	Microcredit NGOs (OSCIPs)
As above (minority share)	<ul style="list-style-type: none"> <li>• BNDES</li> <li>• Banco do Brazil (through Banco Popular do Brasil)</li> <li>• Banco do Nordeste (CrediAmigo / AgroAmigo)</li> <li>• Banco da Amazônia</li> </ul> <p>Development banks also principal – though not exclusive – channels for disbursement of PRONAF monies</p>	Non-profit cooperative financial institutions created to meet the basic financial service needs of low- and middle-income citizens	Formal for-profit financial entities. Can be owned by OSCIPs	Non-profit organizations whose social objectives must fall within a specific list (including provision of credit)

### Third sector rural finance providers

As stated above, the microfinance market in Brazil is not generally considered to be well developed. There are more than 121 microfinance institutions (MFIs) operating in the country—from banks to NGOs, including credit unions and finance companies. The depth of outreach of Brazilian MFIs is significant but their breadth is limited. MFIs are far from reaching all of the existing potential microfinance clients of the country, particularly in rural regions.

The current government is supportive of microfinance and has recently issued a series of new laws in order to attract new entrants into microfinance—mainly credit unions. In addition, the *Programa Nacional de Microcredito* (national microcredit program) forms part of the current administration's policy package aimed at reducing poverty and income inequality in Brazil. As part of this initiative, the government acts as a first-tier supplier of micro credit through state-owned banks and development agencies. A significant amount of government funds is being channeled to micro-entrepreneurs, such as family farmers, through these banks at below-market interest rates.

Currently, the entities which operate in the microfinance sector – called 'Oriented and Productive Micro-credit Institutions' [IMPOs] – encompass diversified formats, such as:

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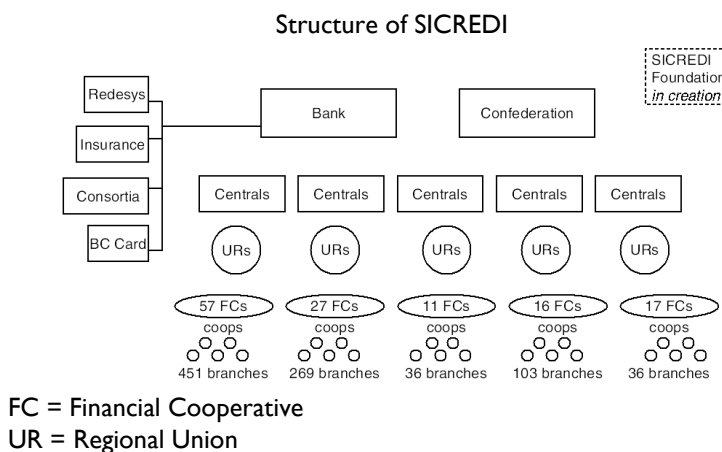
non-governmental organisations [NGOs], public interest civil society organizations [OSCIP], micro-entrepreneur credit societies [SCM], public financial institutions and credit cooperatives, as summarised below.

This section looks at the third sector organisations active in rural micro-lending – credit cooperatives and micro-credit companies and NGOs.

### *Cooperative finance*

Cooperative finance in Brazil is structured around central cooperatives which act as apex institutions for member credit cooperatives that operate at a state level and are owned by at least three member cooperatives. Central cooperative serve to review standards applied by member cooperatives in such areas as accounting, loan origination, staffing, and facilities. They facilitate the flow of funds to and from cooperatives and assume some auxiliary responsibility from the Central Bank for supervision.

Two banks have emerged from the cooperative movement, since 1995 when laws were passed allowing cooperatives to accept savings: Banco Cooperativo do Brasil (Cooperative Bank of Brasil, or BANCOOB) and Banco Cooperativo SICREDI (BANSICREDI). Both are owned by the central credit cooperatives in their networks, and act as commercial banks. Below is an indicative diagram of the structure of the second largest cooperative network, SICREDI.



Source: World Bank, ARD: 'Reaching Rural Areas with Financial Services: Lessons from Financial Cooperatives in Brazil, Burkina Faso, Kenya and Sri Lanka', 2007

SICCOB has some 769 affiliated cooperatives, whereas SICREDI is made up of some 130 cooperatives. In addition, Unicred (in Rio) operates a network of 400 credit cooperatives for medical doctors in 14 states and has a working agreement with SICREDI for access to its central clearing facilities.

By linking with a cooperative bank, credit cooperatives are able to offer a broader

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range of services. For example, members of SICOOB and SICREDI issue credit cards, offer internet banking, issue trade credits including letters of credit, provide insurance (life, non-life, and rural), and extend working capital and investment loans funded by public programs such as PRONAF and lines of credit from BNDES – FINAME (Special Agency for Industry Financing), PROPASTO (National Program of Recovery of Degraded Pastures) and PROSOLO (Program of Incentive for the Use of Soil Products). They are also able to facilitate forward sales, notably by coffee growers, through the Cédula de Produto Rural (Rural Bills of Exchange, PR) instrument.

The BNDES had a programme in place until 2008 – PROCAPRED – which aimed to promote the strengthening of credit cooperatives' equity structure through direct financing cooperative members. This scheme was suspended as of mid-2008 due to budgetary funds having been exhausted.

### *Microfinance companies and NGOs*

The microfinance landscape in Brazil was changed significantly by the Law of 1999 which created Civil Society Organizations (OSCIPS) and Microcredit Societies (SCMs). Before these changes were made in 1999, microfinance in Brazil was undertaken largely by not-for-profit organisations, and these were constrained by the 1% per month ceiling on interest rates imposed by Brazil's Usury Law. (The Usury Law was a limiting factor for microfinance loans because these are traditionally offered for short periods at higher interest rates than loans in the formal and large-scale sectors.)

OSCIPs can have a range of objectives, which are not limited to microfinance. Like NGOs, they are deemed to be non-profit organizations. Importantly, OSCIPs can sign cooperation agreements with the public sector to implement activities and projects of public interest, which implies that they could have access to public sector funds, in addition to donor funds and owner or sponsor funds. OSCIPs are not able to mobilize deposits from the public.

The second form created by the 1999 Law, the SCM, is much closer to a micro-credit society as they exist in other countries. SCMs are for-profit financial institutions that are only allowed to offer microcredit—loans up to R\$10,000 (less than US\$3,000)—and are not permitted to mobilise savings. It should also be noted that the BNDES development bank and SEBRAE (Brazilian Services to Support Micro and Small Enterprises) offer government-backed financing to MFIs (SCMs).

The Brazilian Association of Microcredit Development (ABMD), also known as Brazilian Microcredit Gateway (Portal do Microcrédito) is the umbrella organisation for the majority of microfinance organisations in the country. Besides the National Bank for Economic and Social Development (BNDES) and the Banco do Nordeste CrediAmigo programme, there are currently 24 SCMs and 67 Microfinance NGOs qualified as OSCIPs ([www.cgap.org](http://www.cgap.org)).



### 11. Access to finance for agricultural smallholders in Brazil

Government support to agriculture in Brazil is provided mostly through preferential credit to the sector. Brazil's official credit system confers special treatment on the sector, through the administered allocation of credit resources and controlled interest rates. This system has been justified on the grounds that it offsets high market interest rates, and because affordability of production credit is seen as a crucial element of supporting income generation among the rural poor.

Commercial agri-businesses typically receive their payments in hard currency (mostly US\$), which provides evidence of creditworthiness to lenders. In many cases, agri-business companies do their own lending to large-scale agricultural suppliers, either by providing credit or financing inputs (such as fertiliser) directly. Brazilian soybean farmers, for example, often find it cheaper to obtain finance from crushers.

However, smaller agricultural businesses face a structural problem in demonstrating creditworthiness. And for many of these producers, “asymmetric information” between borrowers and lenders means that there is likely to be an under-provision of credit. There are two main options for resolving this dilemma. One is government intervention. The other possibility is alternative financing arrangements (such as the provision of credit or direct inputs by the purchaser). This may be a viable possibility for some producers, but many farmers with only weak integration to markets are unlikely to be able to meet exacting demands from processors and retailers.

So, while the 1990s were marked by a growth in credit to agriculture originating from traders, processors and input manufacturers, most of this credit was directed to the more modern, larger-scale and export-oriented elements of Brazilian agriculture. According to an unofficial estimate of the Ministry of Agriculture (cited in OECD, 2005<sup>2</sup>), the “credit needs” of the agriculture sector were around R\$ 110 billion in 2003, of which approximately R\$ 31 billion, or 28% was provided through the official rural credit system. The remaining 72% would therefore have comprised non-bank private credit offered by domestic agro-business and international lenders.

However, the Government firmly recognises that land distribution itself was not enough to provide long-term benefit to smallholders led to adoption of the Programme for Strengthening of Family Agriculture (PRONAF). This programme incorporated accompanying policies targeted to the rural poor, including subsidised credit, training and extension, and the promotion of value-added activities. With the adoption of the Zero Hunger Programme in 2003, support of family farming became part of the broader objective of combating hunger and poverty in Brazil.

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<sup>2</sup> ‘OECD Review of Agricultural Policies: Brazil’, Organisation For Economic Co-Operation And Development, Paris, 2005



### The state Rural Credit system

The national state-administered rural credit system, SNCR, provides three categories of credit:

- i) marketing and storage credit;
- ii) working capital; and
- iii) investment credit.

#### *Marketing and storage credit*

What follows is an overview of the sources of state marketing and storage credit: while these credit lines are in principle open to all farmers, there is little evidence that the smallest family farmers are in a position to use these services.

The *Empréstimo do Governo Federal* (EGF) is a federal government loan for agricultural producers that provides short-term preferential credit to agricultural producers (or their co-operatives), enabling them to withhold the sale of a product for a certain period in anticipation of a higher market price. Under such a loan, the harvested crop or livestock product serves as collateral and the loan must be repaid in cash. EGF loans are available for products covered by government purchase programmes, and also for some other commodities. The loan size is determined on the basis of the amount of product pledged times the respective minimum price. A typical loan term is 180 days, but it can vary from a minimum of 90 days to a maximum of 240 days.

The pre-sale loan, *Crédito de Pré-Comercialização*, is a slight variation on the producer EGF. The difference is that the pre-sale loan can be issued before harvesting (up to 60 days), while the EGF is provided only if the crop is harvested and put in storage. The pre-sale loan is therefore for a longer term than the EGF, and its purpose is to provide the borrower with liquidity also during the harvesting period. As under the EGF, harvested and stored crops represent collateral for the pre-sale loan.

The Rural Promissory Note (NPR – *Nota Promissória Rural*) and Rural Duplicate (DR – *Duplicata Rural*) are, respectively, a written obligation of the downstream agent to buy a specified amount of agricultural product, and a written obligation of the agricultural producer to supply it. NPRs and DRs are therefore purchase contracts, and the party representing a buyer can use this document as collateral for receiving short-term bank loans for execution of these contracts within 30 days. This is therefore another instrument of preferential downstream credit, in addition to the processor EGF, designed to facilitate the purchase of agricultural products.

OECD (2005, op cit) indicates that in 1999-2004 marketing loans – as described above – were most widely applied for cotton, covering up to 46% of national production.

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Marketing credit interacts closely with purchase programmes. As borrowers of EGF and pre-sale loans do not currently have the option of settling debt through ceding the pledged product, they may have an incentive to enrol simultaneously in purchase programmes such as the sell option or the PEP. With dual enrolment, the borrower is guaranteed to receive at least the minimum price, and to be able to repay the marketing loan. This practice, in particular a combination of the EGF and the PEP, is typical of the mainstream cotton sector, which may explain why in recent years both modalities covered roughly equal shares of production of this commodity.

### *Working and investment credit*

Provision of working and investment credit is differentiated by two broad groups of beneficiaries:

- i) medium and large-scale producers and their co-operatives, forming what is called here the general system;
- ii) small agricultural producers – beneficiaries of PRONAF

Given the focus of BCI on access to finance for smallholders, this section briefly covers the working credit options for larger farmers (and in some cases also smaller farmers) before looking in more detail at the provision of financial services to family farmers.

Working capital and marketing credit are operated with similar procedures and interest rates. The difference is that working capital loans are taken before the cropping season and are used to buy inputs for planting. The loan period is around 9 months and is paid when the production is sold. Marketing loans are normally 6 months long and are used to finance product storage. Both are subjected to limits per producer as mentioned before. Both credit modalities are notified as product specific because the producer has to inform the product for which the credit will be used. However, the distribution of resources among products is not pre-defined and depends on demand from producers.

Credit line	Interest rates for crop year 2007/8
Working capital and marketing	6.75%
PROGER Rural	6.25%
MAPA/BNDES Programmes	
MODERFROTA:	
- < US\$ 1,316,000 annual gross income	7.50%
- > US\$ 1,316,000 annual gross income	9.50%
Other programs	6.75%
Source: SPA/MAPA	

Short term (working capital) loans are granted for planting or harvesting, with the repayment schedule differentiated by crop, and a unified fixed interest rate. The state-controlled interest rate for rural credit has remained at 8.75% since 1999, but controlled interest rates for working capital and marketing were reduced from 8.75% to 6.75% in the crop 2007/2008 Agriculture Plan.

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Investment credit is provided through a variety of credit programmes, with most of them implemented by the BNDES. The largest of these programmes is MODERFROTA (*Programa de Modernização da Frota de Tratores Agrícolas e Implementos Associados e Colheitadeiras*), which finances acquisitions of tractors and agricultural machinery.

Other programmes are targeted to support investments in specific industries, such as fruit, milk and meat production, or investments in soil improvement and infrastructure. The BNDES Automatic programme finances not only investments in agricultural production, but also in the processing industry, and is more flexible in the scope of activities financed.

The PROGER Investment programme is available for small scale producers who are not eligible for PRONAF credit. Recent modifications to PROGER include not only a substantial increase on the amount of resources for working capital, higher level of gross income limits for eligibility to the Programme and higher working capital and investment credit limits, but also a reduction in the annual effective interest rate, from 8% to 6.25%.

Investment credit lines **to medium- and larger-scale commercial farms** are summarised below (in particular because the aims of some credit lines for larger farms are consistent with the objectives of BCI Production Principles):

- MODERFROTA – Modernization Programme aimed at updating tractors and other agricultural machinery: the interest rate charged by BNDES to borrowers range from 7.5% for middle income producers to 9.5% for larger producers
- MODERINFRA – Incentives Programme for Irrigation and Storage: this programme is designed to assist farmers to improve the structure of its production by investing in proper irrigation. The programme is independent from other credit programmes and taking this loan does not impede the farmer from getting other types of loans. MODERINFRA funds projects up to R\$ 400,000 per farmer.
- PRODECOOP – Cooperative Development Programme for the Enhancement of Agricultural Value Added: this credit line finances machinery and equipment as well as studies and projects design to improve production within the region. Government provides preferential credit rate at 10.75% for anything from 70% to 90% of the project. The cooperative is allowed a three-year grace period and twelve for repayment.
- PRODEAGRO – Agri-business Development Programme: Credit for quality improvement in the areas of apiculture, floriculture, and aquaculture is offered through the PRODEAGRO. Credit line is up to R\$150,000 at an 8.75% interest rate (which includes a compensation of 3% to the financial institution). The borrower is allowed a 24 months grace period (with no interest paid) and a 60 months repayment period.
- MODERAGRO – Programme for the Modernization of Agriculture and the Conservation of Natural Resources: The federal government implements its goals of

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soil conservation by carrying out the MODERAGRO programme. Its main goals are to allow for pasture conservation and soil recovery through funds of up to R\$200,000. Similarly to the PRODEAGRO and most BNDES programmes interest rates are made available at 8.75%. The borrower is also allowed a 24 months grace period (with no interest paid) and a 60 months repayment period plus compensation of 3% to the financial institution which is included in the principal interest rate.

- **PROPFLORA** – The Programme of Commercial Planting and Recovery Forest: the final BNDES specific program is directed at environmental conservation. The PROPFLORA allows for credit up to R\$150,000 (and up to 35% of the total cost of the project) which is to be designed at tree planting projects. Repayment is to be done within twelve years with a 96-month grace period at 8.75% interest rate (including financial compensation of 3% to the lender agency).

The FINAME programme, also administered by BNDES, provides loans of up to 90% of purchase cost, to a maximum of US\$7m, to purchase new industrial equipment with no less than 60% Brazilian content. Interest rates are well below commercial rates, and loans have an amortisation period of 6 months – 5 years.

### PRONAF

PRONAF eligibility criteria		
Group A (Credit for land reform)	Group B (Rural microcredit)	Family Farmers (formerly Groups C, D and E) eligible for other PRONAF credit lines
Agrarian reform beneficiaries	Exploit part of land as owner, squatter, renter, or sharecropper Possess in any capacity land areas not exceeding 4 fiscal modules <sup>3</sup> Live on farm or neighbouring urban or rural settlements	
	Obtain at least 30% of family income from agricultural production or other on-farm activities	Obtain at least 70% of family income from agricultural production or other on-farm activities
	Farm operations based on family labour	Farm operations based predominantly on family labour, hired seasonal labour permitted and not more than 2 permanent hired workers
	Gross annual family income R\$ 5,000 or less (excluding social security benefits)	Gross annual family income in previous 12 months R\$ 5,000 – R\$ 110,000 (excluding social security benefits relating to rural on-farm activities)
Source: BNDES, MDA, Carta-Circular N° 32/2008 July 2008		

PRONAF is a series of credit programmes targeted specifically at small-scale family farms, and as such is perhaps the most important financing programme for BCI's

<sup>3</sup> Established under the Land Statute of 1964, a 'fiscal module' is a regionalised unit of land area, ranging from 5 hectares to 110 hectares, depending on the average size of family farms in each municipality/sub-region. A fiscal module is calculated on the basis of approximate areas of land from which similar economic returns are possible: one fiscal module is the minimum deemed sufficient to support a family. In the Northern region, the area of a fiscal module varies from 50-100 ha; in the Northeast, it is between 15-90 ha; in the Center-West, it is 5-110 ha; in South region, 5-40 ha; and in the Southeast, 5-70 ha.

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purposes. The goal of PRONAF is to transform small household agriculture into commercially sustainable “family farms”. There are tight restrictions on eligibility are designed to keep the focus on small farms and to avoid fraud. Farmers are eligible for a limited number of loans in each eligibility category, after which they are required to 'step up' a group.

### Key PRONAF credit lines, from July 2008

	Types of credit	Maximum loan size	Annual interest rate	Max. term	Grace period
Group A	Investment	R\$ 15,000 and technical assistance grant of R\$ 15,000	1.15%	10 years	Up to 5 years
Group B	Micro-credit	R\$ 1,500	0.5%	2 years	Up to 1 year
Family Farmers (formerly C,D and E) – Working Capital	Working Capital	< R\$ 5,000	1.5%	8-10 years	3-5 years
		R\$ 5,000 – R\$ 10,000	3%		
		R\$ 10,000 – R\$ 20,000	4.5%		
		R\$ 20,000 – R\$ 30,000	5.5%		
Family Farmers (formerly C,D and E) – Conventional Investment	Investment	< R\$ 7,000	1%	8-10 years	3-5 years
		R\$ 7,000 – R\$ 18,000	2%		
		R\$ 18,000 – R\$ 28,000	4%		
		R\$ 28,000 – R\$ 36,000	5%		
Family Farmers (as above) – special programmes (Women, ECO, Agroecology)	Investment	< R\$ 7,000	1%	8-10 years (ECO 8-12 years)	3-5 years
		R\$ 7,000 – R\$ 18,000	2%		
		R\$ 18,000 – R\$ 28,000	4%		
		R\$ 28,000 – R\$ 36,000	5%		
Family Farmers (as above) – Agroindustry (Agroindústria)	Investment	< R\$ 7,000 (or < R\$ 500,000 for collective loan, up to limit of R\$ 7,000 per member)	1%	8-10 years	3-5 years
		R\$ 7,000 – R\$ 18,000 (or R\$ 500,000 – R\$ 10m for collective loan, up to limit of R\$ 18,000 per member)	2%		
Family Farmers (as above) –More Food (Mais Alimentos)	Investment	R\$ 7,000 – R\$ 100,000 (cumulative with Conventional Investment)	2%	10 years	3-5 years

Source: MDA, BNDES, Carta-Circular N° 32/2008 July 2008

The PRONAF system and eligibility structure has been overhauled and streamlined for the 2008/9 crop season. As a result, there are now three groups of potential beneficiaries: ‘Group A’ (settler beneficiaries of agrarian reform), ‘Group B’ (consisting of the smallest subsistence producers eligible for micro credit) and ‘Family Farmers’, who were previously categorised in Groups C, D and E.

Group A borrowers are eligible to receive investment credit to support land improvement, construction of production facilities and infrastructure, acquisition of

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machinery, livestock, planting of permanent crops, and various other activities involved in productive exploitation of new lands.

Group B consists of the smallest subsistence producers eligible for micro credit. Credit to this group is destined to fight rural poverty by supporting income generating activity undertaken by borrowers.

Other beneficiaries (former Groups C to E) represent family farms of increasing size and degree of commercialisation. As in the general system for larger farms, these borrowers can obtain both working capital and investment loans, as well as a series of 'special purpose' programmes aimed at broader rural development objectives.

Importantly for BCI, these include: meeting the financing needs of women family farmers (*PRONAF Mulher*); agro-ecology (*PRONAF Agroecologia*); technical modernisation (*PRONAF Agroindústria*); renewable energy and environmental sustainability (*PRONAF ECO*); and food production (*PRONAF Mais Alimentos*).

### *Government insurance programmes*

Brazilian farmers can benefit from several government insurance programmes. These programmes include payments to farmers who suffer income loss as a result of natural disasters and disease outbreaks. Government-supported farmer insurance has been traditionally linked to rural credit, providing for partial redemption of producers' debt on bank loans related to damaged output. With the emergence of new insurance programmes in recent years, the forms of assistance have been diversified to include income support payments and insurance premium subsidies. PROAGRO is a traditional general insurance programme that has been in place since 1973. It offers eligible farmers partial compensation of the bank debt on working capital loans used in production of the damaged crop. Since 2005, the new Rural Insurance Premium programme (*Subvenção ao Prêmio do Seguro Rural*) grants an insurance premium subsidy to producers who conclude contracts with the insurance companies listed by the government.

In addition to these general programmes, two instruments targeted specifically to family farms have emerged recently. One is the Family Farm Insurance programme (*Seguro da Agricultura Familiar*), introduced in 2004 as a sub-programme of PROAGRO and alternatively denoted as PROAGRO-More. Compared to the general PROAGRO, which guarantees only partial redemption of producer's liability on bank loans, PROAGRO-More provides for full redemption of the farmer's bank liability in respect of lost output and also a partial compensation of lost revenue (equalling to 65% of farmer's anticipated cash receipts). PROAGRO-More covers family farms which are borrowers of working capital loans under PRONAF.

Another targeted insurance programme relevant to BCI is the Crop Guarantee (*Garantia-Safra*), effective since 2002. It is available to family farms located in Brazil's arid

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areas, including the whole of the North East region and northern parts of the states of Minas Gerais and Espírito Santo. The beneficiaries are family farms producing non-irrigated staple crops and cotton who have lost at least half of their anticipated output through natural calamity. These farmers become eligible for income payments for a period of up to six months.

### *Finance for agrarian reform settlers*

Through the World Bank-supported Land-Based Poverty Alleviation Project (*Crédito Fundiário—Combate à Pobreza Rural*), Brazil is addressing one key factor underlying poverty in the countryside, particularly in the Northeast: inadequate access to land by the rural poor. The project is implemented by beneficiary community associations with heavy participation by local, state, and national civil society organizations, including the National Confederation of Agricultural Workers (CONTAG). The project is a Federal program, administered by the Ministry of Agrarian Development, in partnership with 14 States (9 in the Northeast, 2 in the Center-East, and 3 in the South). In the project, self-selected beneficiary groups identify eligible agricultural lands for purchase and negotiate directly with the sellers.

They then obtain long-term financing for the purchase of the land (from Federal counterpart funds), and matching grants for complementary investment subprojects and technical assistance (from World Bank loan proceeds) to improve the productivity of the newly-acquired land and establish new residence there. The project has an overall financing limit per family equal to around US\$7,500 (at 2007 exchange rates), which includes the Government-financed loan for land acquisition and the World Bank-financed matching grants for on-farm investments.

Total project cost for *Crédito Fundiário* is € 340 million, of which the World Bank finances 50% (for the investment subprojects and technical assistance), and the rest is financed by the Brazilian Federal Government (for land acquisition) and beneficiary contributions (about 10% of on-farm investments). By December 2007, the Project had financed/contracted 2,366 land acquisition proposals benefiting 44,522 families on approximately 835,000 hectares of land. The Northeastern states of Piauí and Maranhão constitute 48% of total subprojects and 38% of beneficiaries. Another 157 proposals are in the contracting phase with community subproject financial institutions, representing an additional 2,944 families. On-farm investment subprojects implemented stand at 34,300 (69% of the target), and were expected to increase to 36,000 by early 2008.



### III. Rural Microfinance Promotion Practices

What follows is an overview of effective practices derived from the experience of projects working to provide access to finance for small-scale farmers, rural labourers and their communities, focusing particularly on the Northeastern region, where the largest number of small-scale cotton farmers are located in Brazil, and where climatic and socio-economic factors militate against sustainable development of cotton cultivation<sup>4</sup>.

#### Case study I: AgroAmigo, Northeast region

One of the major lines of action in promoting rural agricultural finance has been to strengthen and expand the CrediAmigo Program created in 1997, Brazil's most important experience with microcredit. Implemented by the public regional development bank Banco do Nordeste, and initiated with World Bank funding (and technical assistance from Acción Internacional), CrediAmigo is considered Latin America's largest micro-credit program, with a portfolio of 170,000 active clients.

It was in this connection and as part of the government's policy of promoting use of the banking system by the low-income primarily rural population sectors that AgroAmigo was established from among PRONAF's line resources, using the experiences of the CrediAmigo approach.

AgroAmigo is based on applying the CrediAmigo microfinance methodology approach to the rural sector, whereas CrediAmigo had focused in urban low-income populations in the same region. Starting in 2004, AgroAmigo, took shape as a 'directed productive microcredit' methodology – in other words, one in which credit was granted to meet the financial needs of small formal or informal individuals or legal entities and in which the participation of rural microcredit advisors was highly important as professionals trained to grant assisted loans, with coaching for the producers, and who also offer advisory business assistance.

AgroAmigo, which is essentially one of the forms that 'Group B' PRONAF micro-credit may assume, finances family farmers with gross family incomes of up to R\$5,000. Financing can amount to up to R\$1,500 for agricultural and non-agricultural production activities at effective concessional interest rates of up to 1% a year. The loan period may be as long as 24 months with one year of grace.

Project partners note that the cooperation of the following entities was instrumental in the design and implementation of AgroAmigo:

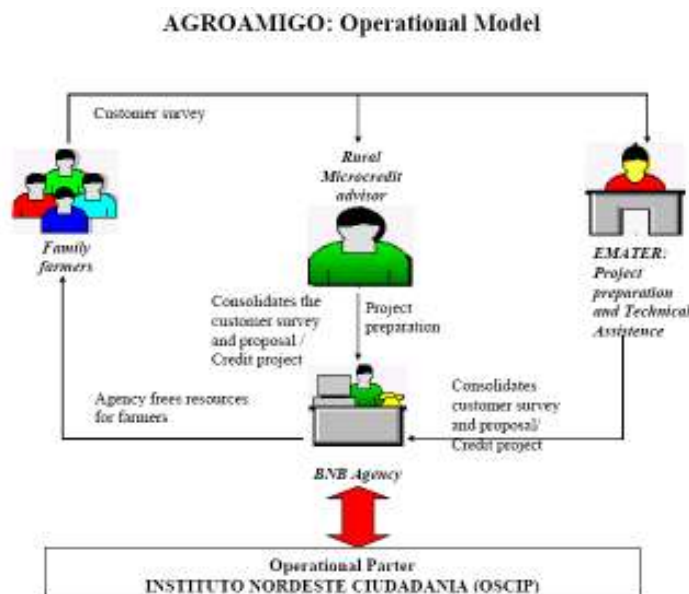
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<sup>4</sup> See Summary Overview – *Aspectos de vulnerabilidade na exploração agrícola de algodão na região Nordeste* – [www.cnpa.embrapa.br/produtos/algodao/publicacoes/trabalhos\\_cba4/012.pdf](http://www.cnpa.embrapa.br/produtos/algodao/publicacoes/trabalhos_cba4/012.pdf)

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- Ministry of Agricultural Development, which first adjusted current legislation to allow for PRONAF to incorporate microcredit concepts and whose cooperation included the financing of rural microcredit advisor training and motorcycles;
- German Technical Cooperation (GTZ) which developed the methodology for the advisors' training program and evaluated it during the pilot program;
- the Instituto Nordeste Cidadania, which selected and hired the advisors and coaches their performance in accordance with the program goals and their working obligations.

The figure below illustrates AgroAmigo's operational model, showing not only the loan agent and the BNB, but also the participation of the state extension service, Empresa de Asistencia Técnica y Extensión Rural (EMATER).



Source: BNB AgroAmigo

The key aspects of the AgroAmigo methodology are summarised below:

- Definition of the project/working area requires definition of geographic area in which the rural microcredit adviser will operate in the light of socio-economic criteria and the existence of support infrastructure. Possible local associations that could emerge from the program's implementation are also considered in identifying the area of operation
- Market mapping consists of visits to selected localities for preliminary contacts with potential clients and community leaders. The target public should be identified during this stage
- Promotion and dissemination of information about the programme, through which detailed guidance can be offered and given about the requirements and

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conditions of the programme and of other existing lines of interest. An effort will be made during this stage to keep in contact with the previously identified community leaders

- Project preparation and formalising proposals: receipt and validation of documentation, and an analysis of the project (and client) in keeping with the 5 terms (state of the business, capacity for payment, capital, collateral, and nature)
- Approval of the loan proposal and signing of the contract involves a joint effort between the adviser and the business support manager
- Disbursement of the loan includes not only letting the client know that it has been approved, but also participating in the loan's release and strengthening its terms (eg the repayment dates)
- Loan administration involves making periodic visits to check the investment that has been financed and to guide the client and providing coaching prior to its repayment
- Loan renewal and access to new financial products, for which the customer's credit record is reviewed and if it is in order the loan is renewed gradually in accordance with the client's payment capacity
- Loan portfolio management monitors goal compliance by the adviser and the agency and evaluates the number of contracts signed, the default rate and loan renewals

The Program was officially launched in November 2006, but actually started operating in the second half of 2004, following good results obtained in rural microcredit pilot projects by the Oeiras and Floriano agencies in the State of Piauí.

By the end of 2006, AgroAmigo had carried out 138,000 operations, worth US\$ 69.7 m. As of 2008, the programme serves 722 municipalities in the Northeast, Northern Minas Gerais and Espírito Santo and employs 375 rural microcredit advisers to guide farmers. The programme shows a low default rate and a profitable portfolio. Most of its loans are in the neighborhood of US\$530 at a fixed term of about two years, which is adjusted to the recipient's profile.

It should be noted that only 6% of the beneficiaries of the programme are agricultural producers, and there is no reference to cotton in the programme portfolio: the vast majority are livestock breeders. However, AgroAmigo seeks to contribute to the diversification of the activities it finances.

Despite the programme's recent implementation, the next steps are already being planned, with a view to improving its design. Among planned innovations are the implementation of a variable pay scale for rural microcredit advisers, use of Palm Pilots for more efficient information collection, the creation of specific rural microcredit units, and the incorporation of Credit Score methodology as a customer classification system for better loan targeting and operating risk reduction.

### Case Study II: IFAD experience working on rural finance in the Northeast

The International Fund for Agricultural Development (IFAD) commenced its 'North-East Rural Family Enterprise Development Support Project' in early 2007. One of the key components of the project is to promote equitable access to finance for rural microentrepreneurs.

The objective of the financial services component of the project is to increase the access of the rural poor to financial services through an expansion in the coverage of PRONAF and the strengthening of a competitive and sustainable system of local non-banking financial services. For this purpose, the project addresses existing difficulties in the formal banking system (BDB and BNB) in order to build up the still limited rural clientele, foster the design of new banking products and less restrictive bureaucratic practices and support the creation of guaranteed funding.

The financial services component of the project is being implemented through three activities:

- Credit activities seeking to expand the uptake of PRONAF credit lines (as described in section above) through a wide range of training and support initiatives. The initiatives involve precise institutional arrangements among participating government and banking institutions, BNB and the MDA have formulated a statement of intention to coordinate the national Family Agriculture Agro-Industrialization Programme. The programme envisages the training of technical personnel in agro-industrial project formulation, support for agro-industry management and the establishment of business networks.
- Expansion of the coverage of banking services among the rural poor through the strengthening of capital funds and institutional capacity. Activities include the diagnosis of existing guaranteed funding schemes and the establishment of new ones, the negotiation of agreements with public entities for the contribution of capital and the provision of training and technical assistance for capacity-building to support the guaranteed funding schemes.
- Strengthening the network of savings and credit cooperatives in the project area, particularly the capacity of these networks to mobilise local resources and to branch out credit and micro-credit services so as to reach the rural poor.

IFAD highlights the following lessons derived from the implementation experience of IFAD projects in the North-East Region of Brazil:

- the importance of the rural enterprise sector for the region in view of the region's agro-ecological limitations (namely the high risk associated with farming activities, including cotton farming)

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- the importance of the work that the Brazilian Support Service for Small and Microenterprises (SEBRAE) undertakes so as to facilitate the identification and creation of rural enterprises
- the relevance of microcredit and of the experience of non-governmental organizations specialized in financing
- the importance of strengthening local organisations and their involvement in the generation of demand; and
- the promotion of self-development, whereby individuals and groups of beneficiaries identify their own business opportunities, which favours more effective product development and greater quality control in production.

### Case study III: Crédito Fundiário

A set of basic principles have been found key for successful implementation of the Crédito Fundiário programme:

- **Community-based approach.** The community-based approach has proven cost-effective and non-conflictive. Community associations take the initiative in selecting and negotiating land purchases and in deciding priorities for productive investments. Funds for on-farm investments and technical assistance are deposited directly into community association bank accounts. Experience shows that reliance on community initiative leads to higher sustainability through self-selection by beneficiaries of the lands to be acquired and the investment subprojects to be implemented.
- **Decentralization.** The project is implemented in a decentralized manner. Each State has a Technical Unit which, in turn, works directly with Municipal Councils where the beneficiary associations are represented. Thus, key decisions are made locally and independently.
- **Involvement of agricultural workers federations:** The state-level federations of agricultural workers (FETAGs) play a major role at the State and municipal levels. Likewise, CONTAG, plays a major role at the national level, dealing with operational and broader policy issues. FETAGs participate in Municipal Councils and play a crucial role in mobilizing rural communities, certifying the eligibility of project beneficiaries, providing ongoing support through monitoring and evaluation, and ensuring transparency of the process.
- **Access to Investments.** Rather than suffering from delays in public provision of support services, community associations have immediate access to financing for on-farm investments to make their newly acquired lands productive. A lump-sum amount, with a per-family ceiling, is available through the project for infrastructure and productive investment subprojects.
- **Self-selection and eligibility.** Self-selection of beneficiaries has proven effective in pinpointing the landless rural poor; the vast majority of beneficiaries have household incomes and characteristics consistent with the target population. Similarly, most

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properties acquired under the project are small or medium size, relative to traditional land reform settlements, ranging in size from 15 to 30 families.

- Financing ceiling and linked financing. The single financing ceiling per beneficiary family (the sum of the amount of the loan and the matching grant) provides a powerful and effective incentive for beneficiaries to bargain down the price of the land, reduce their level of indebtedness, and increase the amount of grant financing for their farm.

### Glossary

BACEN	Central Bank of Brazil (Banco Central do Brasil)
BNDES	Brazilian National Bank for Economic and Social Development (Banco Nacional de Desenvolvimento Econômico e Social)
CPR	Rural Product Note (Cédula de Produto Rural)
EGF	Federal Government Loan (Empréstimo do Governo Federal)
Embrapa	Brazilian Corporation for Agricultural Research (Empresa Brasileira de Pesquisa Agropecuária)
FAT	Unemployment Insurance Fund (Fundo de Amparo ao Trabalhador)
FCO	Brazilian Constitutional Fund for Financing the Centre West Region (Fundo Constitucional de Financiamento do Centro-Oeste)
FNE	Brazilian Constitutional Fund for Financing of the North East Region (Fundo Constitucional de Financiamento do Nordeste)
FNO	Brazilian Constitutional Fund for Financing of the North Region (Fundo Constitucional de Financiamento do Norte)
IBGE	Brazilian Institute of Geography and Statistics (Instituto Brasileiro de Geografia e Estatística)
INCRA	National Institute of Colonization and Agrarian Reform (Instituto Nacional de Colonização e Reforma Agrária)
ISA	Instituto Socioambiental
MAPA	Brazilian Ministry of Agriculture and Food (Ministério da Agricultura, Pecuária e Abastecimento)
MDA	Brazilian Ministry of Agrarian Development (Ministério do Desenvolvimento Agrário)
MDIC	Brazilian Ministry of Development, Industry and Trade (Ministério do Desenvolvimento, Indústria e Comércio Exterior)
MDS	Ministry of Social Development and Combat Against Hunger (Ministério do Desenvolvimento Social e Combate à Fome)
NPR	Rural Promissory Note (Nota Promissória Rural)
OSCIP	Civil Society Organisation
PNAD	National Sample Household Survey (Pesquisa Nacional por Amostra de Domicílios)
PROCERA	Special Credit Programme for Agrarian Reform (Programa de Crédito Especial para a Reforma Agrária)
PROGER	Brazilian Program for Employment and Revenue Generation (Programa de Geração de Emprego e Renda)
PRONAF	National Program for the Strengthening of Family Agriculture (Programa Nacional de Fortalecimento da Agricultura Familiar)
SNCR	National System of Rural Credit (Sistema Nacional de Crédito Rural)