

# Fostering competition in the Brazilian Financial Sector

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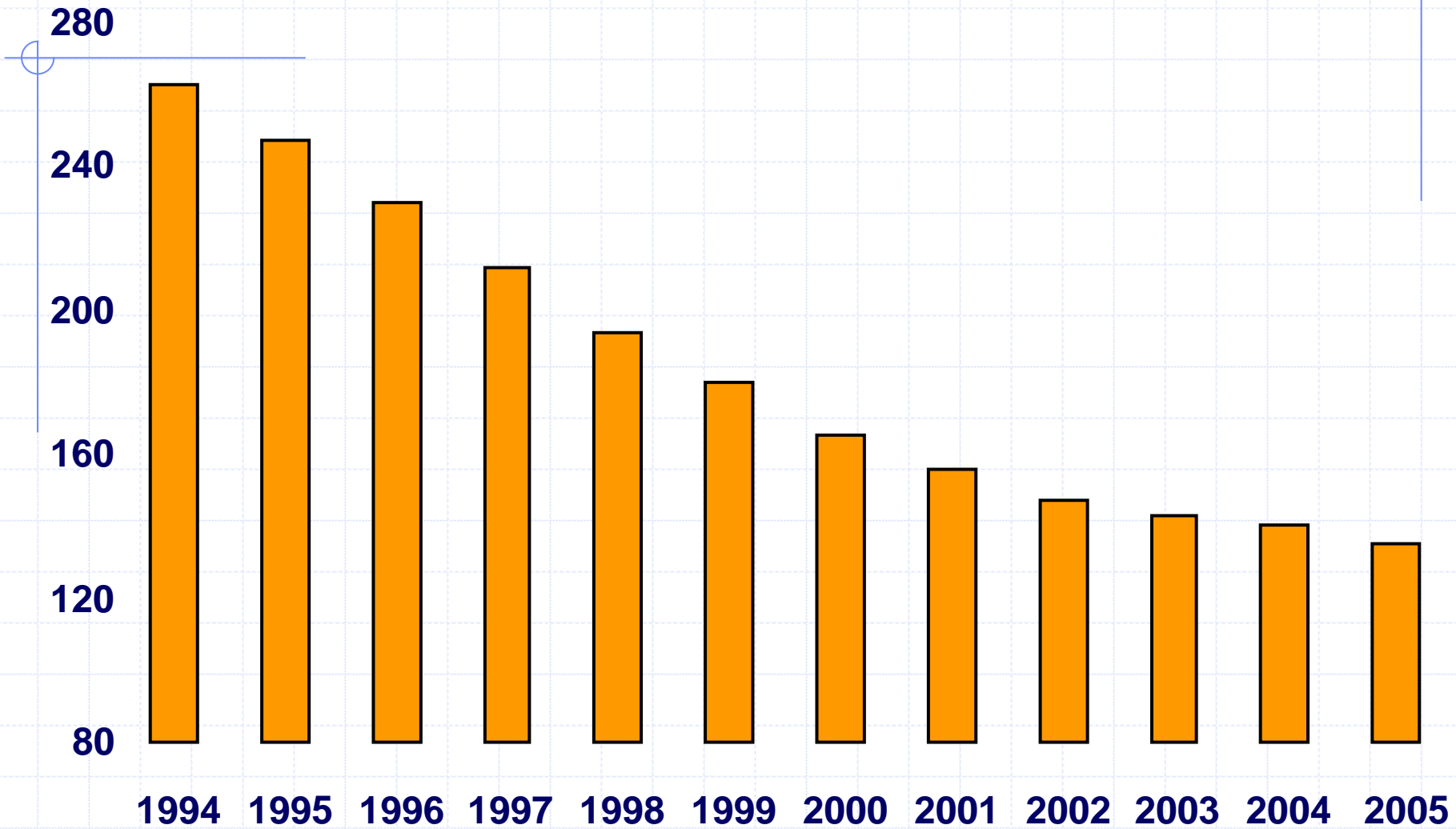
# Agenda

- ◆ Overview of competition in Brazilian banking
- ◆ Results of empirical research
- ◆ Regulatory approach

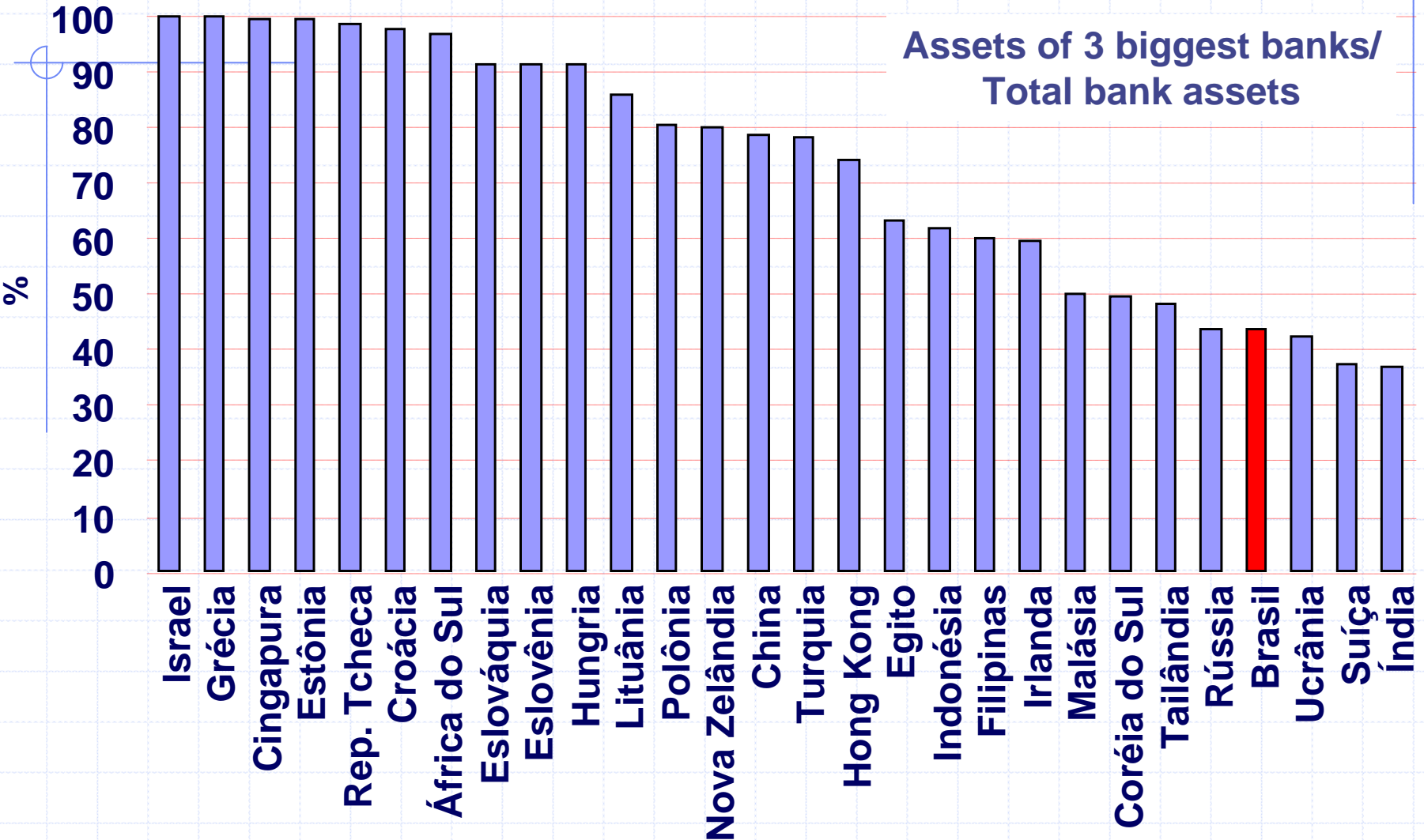
# Number of financial institutions - september 2007

- ◆ 134 multiple banks
- ◆ 20 commercial banks
- ◆ 17 investment banks
- ◆ 289 broker/dealers
- ◆ 53 finance companies
- ◆ 1465 credit unions
- ◆ 234 other financial institutions

# Number of Banks 1994-2005

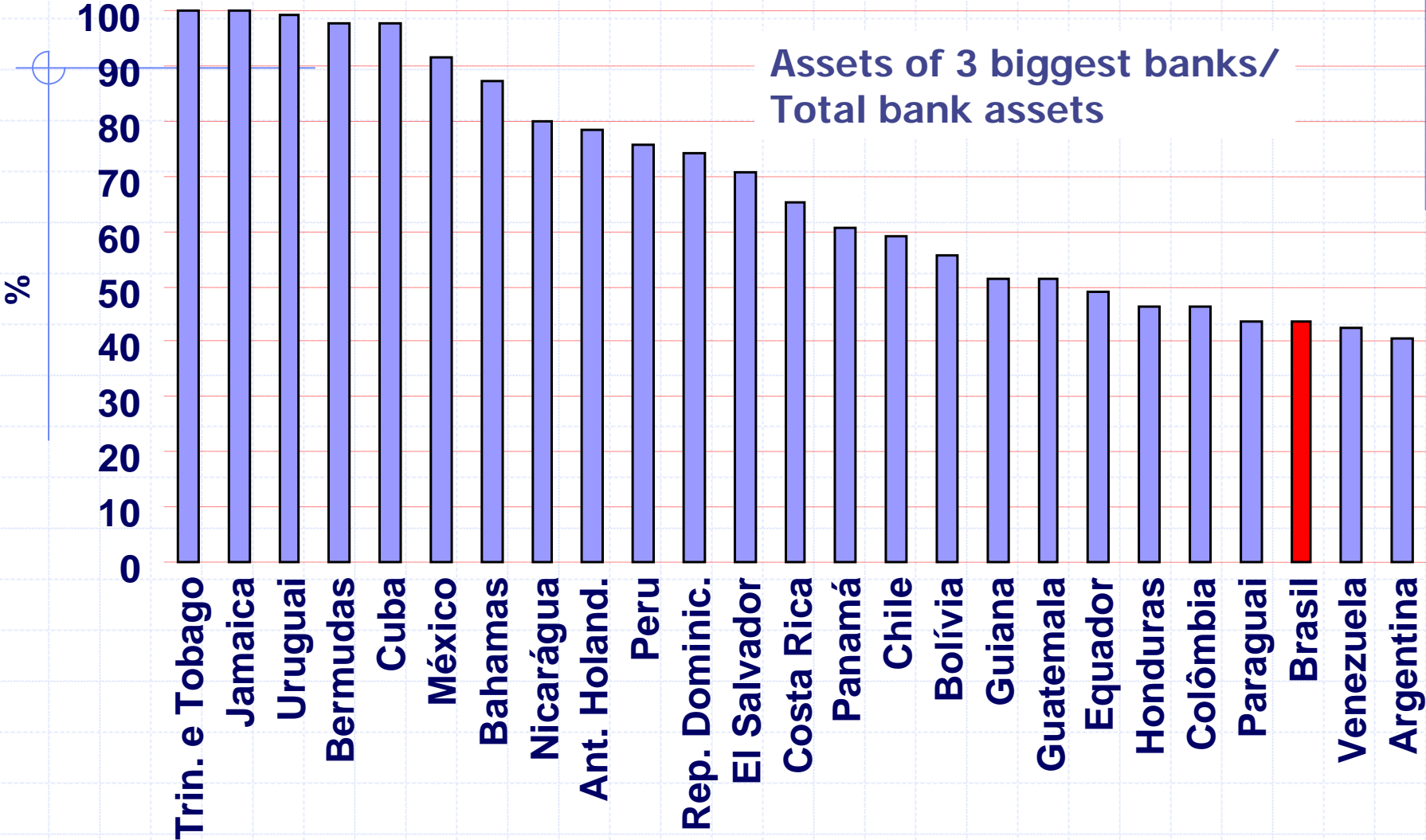


# Bank industry concentration index in 2005 – Selected countries



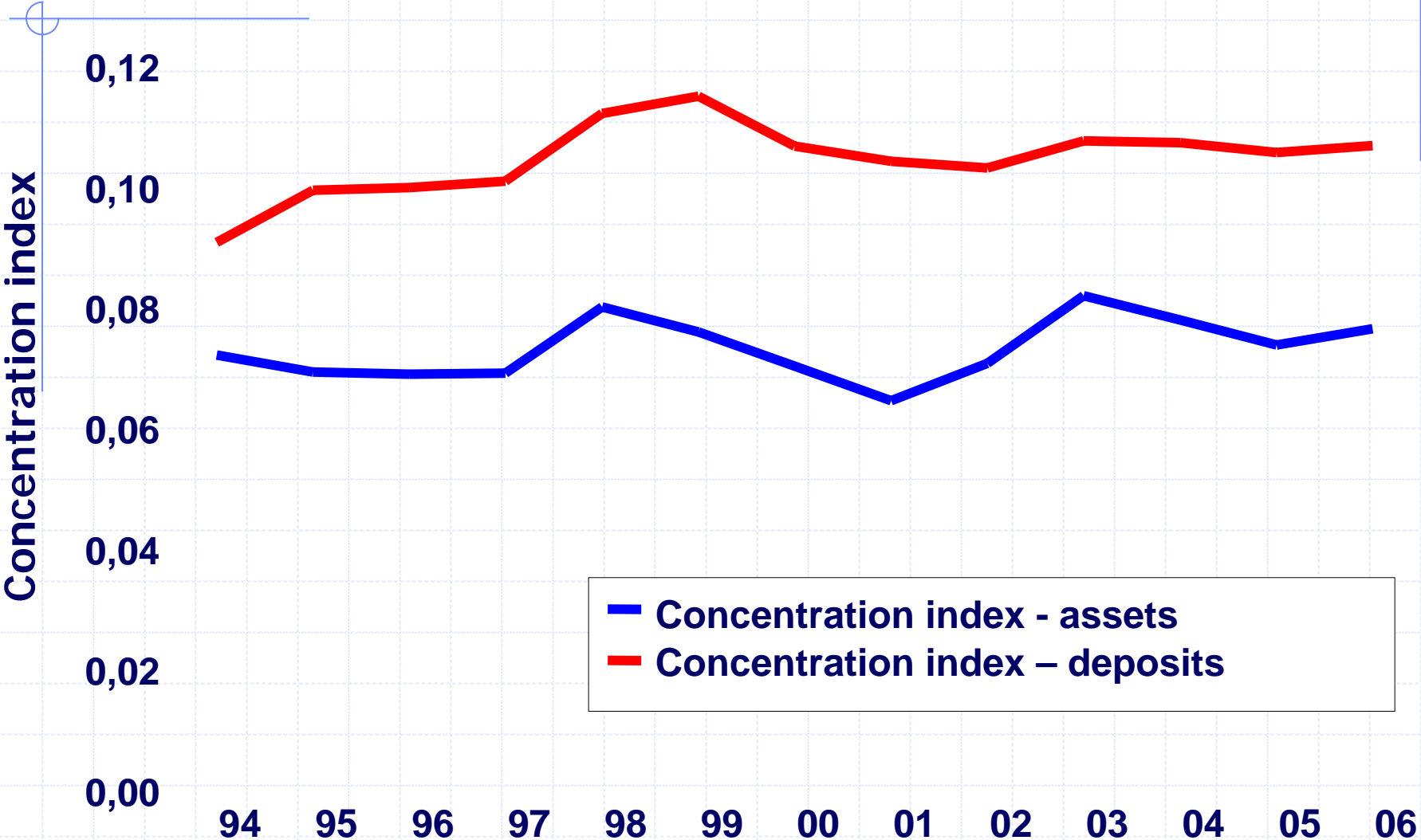
Source: World Bank - A New Database on Financial Development and Structure

# Bank industry concentration index in 2005 – Latin America and Caribbean



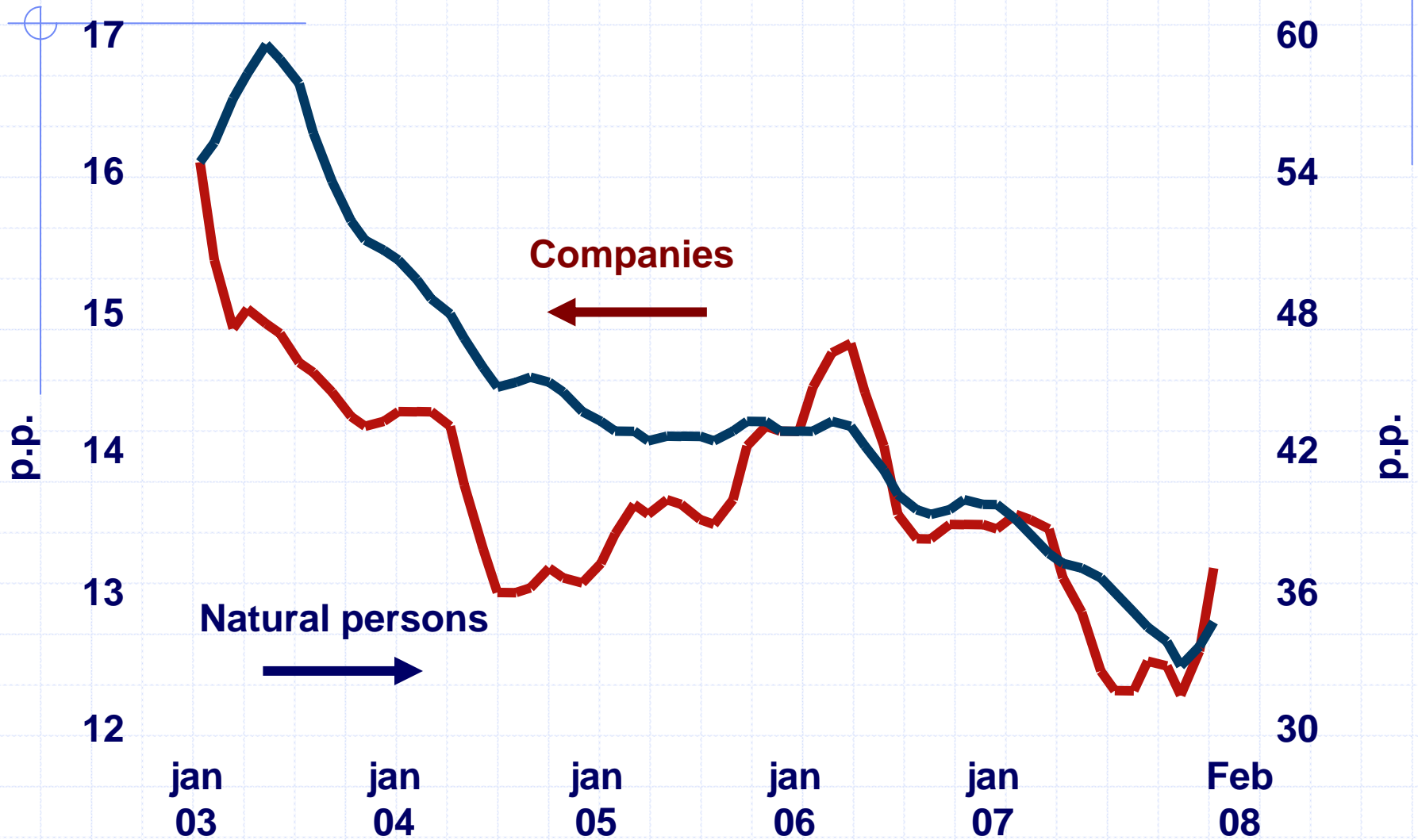
Source: World Bank - A New Database on Financial Development and Structure

# Herfindahl index for bank industry – Brazil – 1994/2006



Source: BCB

# Spreads on non-directed loans – 2003-2008



Source: BCB



# Tests of market power

Traditional IO: without asymmetry of information.

- Nakane (2002)
- Belaisch (2003)
- Petterini & Jorge Neto (2003)
- Nakane, Alencar & Kanczuk (2006)

# Tests of market power

Conclusions:

- ◆ Cartel-collusion always rejected
- ◆ Perfect competition almost always rejected
- ◆ Market structure is imperfect but there is a high degree of competition

# Market failures

- ◆ So market power is irrelevant in the bank sector? How to account for high spreads?
- ◆ Special features of financial sector:
  - Assymmetric information/ Informational Rents;
  - Service bundling;
  - Switching costs;
  - Moral hazard and adverse selection.

# Consequences for regulation

- ◆ Evidence suggests high spreads are not caused by colusive behavior, but rather to high switching costs and adverse selection
- ◆ Therefore, measures like portability and credit bureaux might be important

# 1 – Credit information system (SCR)

- ◆ Created in 1997
- ◆ Exposures to each client above R\$ 5,000 have to be informed
- ◆ All financial institutions (except the very small ones) should send information
- ◆ Access of banks to information on a particular client must be authorized by the client
- ◆ Client has direct access to her own information

## 2 - Portability

- ◆ Portability of personal file information (Res. 2.835, of 30/5/2001)
- ◆ Loan portability (Res. 3.401, of 6/9/2006)

# 3 - Increasing transparency

- ◆ Banks required to disclose monthly interest rates and all other costs in loan contracts (Circular 2.936, of 14/10/1999)
- ◆ Banks required to disclose total effective cost of loans (Res. 3.517, of 6/12/2007)
- ◆ Central Bank site on the internet: Rates, bank fees, ranking of complaints
- ◆ Regulation of bank fees (Res. 3.518, of 6/12/2007)
- ◆ Bank fees: standardized table of basic services for natural persons (Circ. 3.371, of 6/12/2007)

## 4 - Stimulating competitors

- ◆ Reduced restrictions to creation and operation of credit unions (Res. 3.442, de 28/2/2007)
- ◆ Entry of foreign banks
- ◆ IPOs of middle sized banks



## 4 - Geographic dimension of competition

- ◆ Bank correspondents (Res. 3.110, of 31/7/2003)
- ◆ 96.000 points of sale, compared to 17.000 branches
- ◆ Allows bank system to reach all municipalities

# 5 - Increasing asset liquidity

## Loan sales and securitization:

- ◆ Res. 2.836/2001: Loan sales
- ◆ Res. 2907/2001: Loan investment funds (FDICs)
- ◆ Law 10.931/2004: "Loan bonds" (CCB)

# 6 - Licencing procedures for mergers and acquisitions

- ◆ Definition of relevant markets
- ◆ Impact on concentration indexes
- ◆ Contestability
- ◆ Economies of scale and scope

# Conclusions

- ◆ Research is still needed
- ◆ Complex problem → Multiple approach
- ◆ Room for improvement
- ◆ Especially important for SMEs and the underbanked

# Muchas gracias

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