Developmental State with Neoliberal Tools:
a portrait of the Brazilian housing financial system

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Abstract

In the last decades, several countries have undertaken institutional reforms in their national housing finance systems. At the end of the 1990s, the Brazilian government followed this global trend and reformed their national housing finance system. In 1997, Congress enacted Law n. º 9.514, instituting the Real Estate Financial System (SFI) that should gradually replace the former Housing Financial System (SFH). The new SFI sought a different model of financing based on the creation of a mortgage market, which consisted of securitizing debts and fundraising via capital market. In contrast, the former SFH was a state-led arrangement that relied on direct credit policies, public subsidies and the performance of state-owned banks. This paper aims to assess the Brazilian housing reform outcomes. Regarding the legal security, the data collected pointed to the satisfactory success of these measures. However, concerning the extent to which the market relation expanded over the state domains, the achievement is different. The most apparent effect of the reform is a repositioning of state agents in the new institutional frameworks, most notably the state-owned bank in the housing market.

Keywords

developmental state, mortgage market, housing finance, institutional reform, state-owned banks

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1. Introduction

In the last decades, several countries have undertaken institutional reforms in their national housing finance systems. These changes aimed at ensuring higher legal security for investors had the intention of substituting state-led arrangements for market-oriented ones. Through the enactment of laws and regulatory frameworks, reforms established new contractual rules and eviction procedures designed to foster a mortgage market in several national economies. Data collected by Buckley, Chiquier and Lea[3] demonstrates an exponential growth of this market in countries such as China, India, Hungary and the Baltic states.

At the end of the 1990s, the Brazilian government followed this global trend and reformed their national housing finance system. Influenced by the global diffusion of mortgage market and pushed domestically by real-estate associations, Brazilian policy-makers implemented an ambitious change in the housing sector. In 1997, Congress enacted Law n. º 9.514, instituting the Real Estate Financial System (SFI) that should gradually replace the former Housing Financial System (SFH). The new SFI sought a different model of financing based on the creation of a mortgage market, which consisted of securitizing debts and fundraising via capital market. In contrast, the former SFH was a state-led arrangement that relied on direct credit policies, public subsidies and the performance of state-owned banks. The reform kept both systems working in parallel, but it envisioned a progressive replacement of SFH by SFI.

Broadly speaking, the Brazilian housing reform belongs to the same Rule of Law project wave that diffused throughout the developing world in the 1990s[4]. The Rule of Law reforms are based on the foundation that institutional fragilities and legal insecurity widely affected emerging economies and hindered their prosperity. Following the global Rule of Law template, Brazilian policymakers introduced new legal provisions to increase local credit security. One example was the introduction of the deed of trust, which is a mortgage modality that offers further contractual guarantees to creditors. In addition, the Brazilian housing reform established new civil procedural rules that limited access to courts and ensured the possibility of extrajudicial eviction against defaulters.

[3] R. Buckley L. Chiquier, and M. Lea, “Housing Finance and the Economy”, in R. Buckley, L. Chiquier, M. Lea (eds.), *Housing Finance Policy in Emerging Markets* (Washington: World Bank, 2009), pp. 3-4.
[4] T. Carothers, *The End of the Transition Paradigm*, Journal of Democracy, no. 13 (2002).

This paper aims to assess the Brazilian housing reform outcomes. Firstly, it will examine the extent to which the legal security provisions have been effective in action. Secondly, it will evaluate whether SFI effectively replaced the SFH, i.e., privatization degree achieved in housing finance.

Initially, the hypothesis that underpinned this research was that by changing contractual and procedural rules the Brazilian legal reform would ensure a higher guarantee to creditors. Accordingly, it would enable a new model of housing finance in which the mortgage market would be the prevalent feature. The findings, however, lead to a different conclusion. The paper's main claim is that even though there was an improvement in legal security, the mortgage market did not replace the SFH and the Caixa Econômica Federal (CEF), a state-owned bank, is still a key player.

The claim develops as follows, the legislative changes have strengthened credit security: there is a low volume of legal disputes and the judiciary branch tends to favor creditors. On the other hand, instead of the mortgage market substituting the state players, the reform's most visible effect is the state agents' rearrangement in the mortgage market, i.e., a coexistence between old organizations and new institutions. Three pieces of evidence sustain this conclusion: (i) the CEF is still the lead provider of housing finance; (ii) a part of mortgage market's liquidity stems from the SFH; and (iii) CEF has benefited from the new legal security mechanisms and even employs them in social programs like Programa Minha Casa, Minha Vida, (PMCMV, "My House, My Life Program"), which favors low income families.

Firstly, this paper contributes to the literature on housing finance reforms, by reaffirming that the provision of legal security to private agents may be necessary, but insufficient to foster a market-oriented model of development. Secondly, it integrates the literature on privatization and regulatory reform in developing countries, by shedding light on different juxtapositions between the state and the market that can result from institutional reforms. Ultimately, the paper collaborates with scholarly debate on reform strategies, by revealing that not only might state-owned enterprises play an active role in the privatization process, but they may also profit from the new institutional framework.

This article is organized as follows. The next section introduces a description of the methodology and research design. The third section discusses the literature on contract models, housing finance arrangements, and institutional reform strategies. The fourth describes the housing finance transition Brazil has strived for since 1997 and analyzes the extent to which the housing sector changed from a developmental state to a neoliberal arrangement. The fifth section discusses the research findings, by placing them in the debate on reform and institutional change. To conclude, the sixth section brings final considerations.

2. Research Design and Methodology

The main claim of this article is a qualitative one, but the research combines quantitative and qualitative methods. The research utilizes quantitative methods to measure the extent to which the housing reform improved the legal enforcement of mortgage contracts. The law and finance literature claims that courts' decisions might be debtor-biased and can undermine creditors' rights, thus jeopardizing the financial development[5]. For this reason, the paper takes mortgage contracts' enforcement as a proxy of the amount of institutional change achieved in this reform. To this end, the research examined ten courts: five of the Regional Federal Courts (TRFs), and five State Courts of Justice (TJs). There are five Regional Federal Courts in the country, which are responsible for deciding cases involving the CEF and there are 27 State Courts of Justice that have jurisdiction over private banks. The research of State Courts of Justice consisted of a sample gathered from only five of the 27 state courts. In order to randomize the sample, the research selected five courts of Justice, located in the same states as the Regional Federal Courts. As a whole, the sample gathered 1,007 judicial rulings.

In addition to quantitative data, the paper also employs qualitative methods to analyze the degree of privatization achieved in housing finance[6]. The goal is to understand whether the legal reform altered the prevailing state-led type of financial organization. In this sense, the paper assessed three proxies: (i) whether CEF's market share shrunk as a consequence of legal reform; (ii) whether the introduction of new rules for the mortgage market changed the type of funding that supported the housing economy; (iii) whether the new legal provisions have been confined around the SFI

[5] R. La Porta, F. Lopez-De-Silanes, A. Shleifer and R. Vishny, *Legal Determinants of External Finance*, The Journal of Finance, no. 3 [1997]; R. La Porta, F. Lopez-De-Silanes, A. Shleifer and R. Vishny, *Law and Finance*, 106 Journal of Political Economy, no. 6 (1998); P. Arida, E. Bacha and F. Lara-Resende, "Credit, interest and jurisdictional uncertainty: conjectures on the case of Brazil", in F. Giavazzi, I. Goldfajn, S. Herrera (eds.), *Inflation Targeting, Debt and the Brazilian Experience: 1999 to 2003* (Cambridge: MIT Press, 2005), pp. 265-293; A. C. Pinheiro (ed.), *Judiciário e economia no Brasil* (Rio de Janeiro: Centro Edelstein de Pesquisas Sociais, 2009).

[6] J. Gerring, *Single-Outcome Studies: a methodological primer*, 21 International Sociology no. 5 (2006).

limits or if these provisions spread beyond SFI limits. These proxies measure the resilience of old organizations (state-led arrangements) and the success of new institutions (market-based systems). Both the quantitative and qualitative proxies constitute the paper's main purpose: to portray the Brazilian housing financial system's institutional features.

3. Housing Financial Systems, Legal Tools, and Reform Strategies

From the 1990s onwards, literature has been identifying the financial reform diffusion in the housing sector of many countries.[7] This section outlines the housing reform package in three dimensions. First, it describes different financial arrangement alternatives, pointing out that the housing reform consisted of a transition from state-led arrangements to market-led ones. Second, it sets forth the types of contractual and procedural rules that are mostly associated with developing countries and market-led arrangements. Third, it summarizes the main reform strategies that policymakers have employed to pursue financial liberalization in the housing sector.

3.1. Housing Reform: from financial repression to financial liberalization

In the housing sector reform, the common target that policy makers have envisioned across the board is deepening articulation between the capital market and mortgage contracts. Accordingly, the reform goal was to shrink the so-called financial repression arrangements (state-led arrangements) and to foster financial liberalization arrangements (market-led arrangements).[8] This reform achieved an unprecedented record between 1994 and 2004, when the mortgage debt increased more than US$ 7 trillion globally.[9]

In analytical terms, financial repression and financial liberalization constitute the extremes of an institutional scale that embodies four different types of financial arrangements. These four types of arrangements result from diverse mixtures of three attributes: savings possibilities; credit modalities, and financial intermediation

[7] B. Martins, E. Lundberg and T. Takeda, *Housing Finance in Brazil: institutional improvements and recent developments*, IDB Working Paper Series, no. 269 (2011); Otto, S., *Real Estate Policy in Brazil and Some Comparisons with the United States*, Working Paper no. 549 of the Stanford Center for International Development [2015].

[8] R. Green and S. Watcher, *The Housing Finance Revolution*, Research Paper Series of the University of Pennsylvania Institute for Law and Economics [2007].

[9] Buckley, Chiquier and Lea (2009), *supra* note 3.

channels. Accordingly, there are two types of savings: voluntary and compulsory. Compulsory savings are based on a forced resource extraction, similar to what happens in tax collections, whilst voluntary savings are those obtained voluntarily, according to the savers' will. Credit also comes in two types: it can be freely allocated, where financial agents decide on its application based on risk and return assessments, or it can be directed by laws and regulations, in which case the credit allocation aims to meet policy purposes (directed credit policies)[10]. Finally, the agents responsible for the intermediation between savers and holders can be state-owned banks, savings and loans associations, private banks, or the capital market[11].

Based on the descriptions of scholars such as Lea[12], Hassler and Renaud[13]; and Green and Watcher,[14] the composition of these elements can be sorted on a continuous scale of four financial arrangements: (i) policy-directed credit and state-owned banks; (ii) policy-directed credit and mixed bank ownership; (iii) saving and loans associations/local private banks, and (iv) systems that integrate banks and capital markets. On this scale, the types of organizations are laid out between two opposite poles: the highest financial repression and the highest financial liberalization.

Table 1. Types of financial systems

policy-directed credit and state-owned banks	policy-directed credit and mixed ownership	savings and loans associations or local private banks	banks and capital markets
(+) Financial repression	⟵	⟶	(+) Financial liberalization

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[10] C. Calomiris and C. Himmelberg, "Directed Credit Programs for Agriculture and Industry: Arguments from Theory and Fact", in *Proceedings of the World Bank Annual Conference on Development Economics 1993* (Washington: World Bank, 1994).
[11] Lea (2009), *supra* note 5, pp. 29-47; L. Chiquier, O. Hassler and S. Butler, "Enforcement of Mortgage Rights", in L. Chiquier, M. Lea, *Housing Finance Policy in Emerging Markets* (Washington: World Bank, 2009), pp. 293-323; O. Hassler and B. Renaud, "State Housing Banks", in L. Chiquier, M. Lea, *Housing Finance Policy in Emerging Markets* (Washington: World Bank, 2009), pp. 243-275.
[12] Lea (2009), *supra* note 11, pp. 30-47.
[13] Hassler, Renaud (2009), *supra* note 11, pp. 249-261.
[14] Green, Watcher (2007), *supra* note 8.

The first model, policy-directed credit and state-owned banks, drives the financial intermediation by allocating forced savings through policy-directed credit. Rather than risk and return criteria, it is the policy options that mediate financial destinations. In this model savings are not only compulsory, but also the interest rates are defined at the monetary authorities' discretion, thus resulting in values that are generally lower than those of the market. Potentially, this arrangement suffers from a lower funding restriction, i.e., it holds higher financial elasticity because the funding is based on *quasi*-tax levy procedures. On the other hand, the model can undergo distorted financial allocations and, at worst, exhibit default problems stemming from misleading measures in policy criteria.[15]

The second model, policy-directed credit and mixed ownership, follows state regulation as well, but the financial intermediation combines state-owned and private banks. In this arrangement, there are both types of savings the voluntary and the compulsory. In terms of funding, the policy-directed credit and mixed ownership model tends to be as elastic as the previous model, to the extent that it also relies on an ample financial base (both forced and voluntary savings). Nevertheless, its operation can be equally vulnerable to distortions in financial allocation, due to direct credit policies. Moreover, the need of return demanded by voluntary investors can favor a regressive credit allocation, in which financial resources prioritize a client base with higher purchasing power, to the detriment of poorer consumers.[16]

Unlike the previous models, the third model, savings and loans associations or local private banks, hinges only on voluntary savings and free credit allocation. There are two kinds of intermediaries in this system: associations and banks, whose differences imply higher or lower financial restrictions. Compared to the previous models, savings and loans associations face higher financial restrictions (lower elasticity), insofar as their savings base is restricted to their associates.[17] In addition to savings and loans associations, banks also rely on voluntary savings and free allocation, but they are not restricted to a small group of associates and have a more diversified financial base. Consequently, banks tend to experience fewer financial mismatch risks

[15] Hassler, Renaud (2009), *supra* note 11.
[16] On this, see Hassler, Renaud (2009), *supra* note 11.
[17] A saving and loan association is a financial institution in which members form a credit union to collect and lend resources to associates. It is generally run by associates and its financial operations are restricted to the members. Usually it is smaller than a bank in terms of funding capacities.

than savings and loans associations.[18] Even so, banks also suffer from financial restrictions on some level, since deposits are short-term and loans (particularly housing loans) are long-term. Moreover, in this third model banks are local players, i.e. they have a restricted client portfolio, thus they also face funding constraints to some degree.

Finally, the fourth model of financial arrangement is the integration between banks and the capital market. In this model, banks lend resources to families and securitize the receivable returns by transforming the expected payments into securities that are negotiables in the capital market. Similar to the third model, the integration between banks and capital market represents a gain in financial elasticity for capital providers. The banks' loaning capability is no longer restricted to its own local clients, to the extent that part of the bank's funding comes from mortgage-backed securities that are sold in the capital market. Compared to the first and second arrangements, this fourth model can guarantee a less distorted allocation, to the extent that it does not count on policy criteria. On the other hand, it can fall into an exacerbated financialization of the housing system, which might relegate housing funding to a secondary role.

The so called housing finance revolution[19] that took place in several countries in the last years consisted of the transition from models 1, 2 or 3 to the model 4.[20] The first record of this institutional change happened in the US in the 1970s. At that time, the US's prevailing financial arrangement was situated around model 3, with savings and loans associations playing a major role in the financial system. As a response to the severe funding crisis that continuously affected savings and loans associations and impaired housing financing evolution, the US Congress approved the *Home Finance Act*.[21] This Law established the institutional frameworks that underpinned the integration between banks and the capital market, thus creating the mortgage market. In the following years, different countries such as Spain, Hungary, and Brazil tried to emulate the US's arrangement, by transplanting the integration between banks and the capital market in their local contexts. In all these countries, policymakers strived to

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[18] A financial *mismatch* is the inconsistency between the long-term deadline for return of the funding granted by financial institutions and these institutions present need for liquidity to settle their current financial operations.

[19] Green, Watcher (2007), *supra* note 8.

[20] Buckley, Chiquier, Lea (2009), *supra* note 3, pp. 3-4.

[21] P. Carrozzo, *Marketing The American Mortgage: The Emergency Home Finance Act of 1970, Standardization and the Secondary Market Revolution. Real Property*, 39 Probate and Trust Journal, American Bar Association, no. 4 (2005).

replace the state-led arrangements with market vehicles, such as mortgage-backed securities, securitizing companies, and investment funds.

In parallel to these market vehicles, the closer integration between housing finance and the capital market also implied the strengthening of the legal tools that underpin market transactions. Correspondingly, the building block for mortgage market construction was legal security improvement through the sharpening of contractual and procedural rules.

3.2. The Mortgage Market's Legal Tools

There is a strong link between the varieties of financial arrangements and the legal tools that discipline financial contracts. Despite the fact that legal security matters for all types of financial systems aforementioned, the more the arrangements drift away from financial repression and get closer to financial liberalization, the more relevant credit security attributes start to be. Particularly, in systems that integrate banks and capital market, the contract predictability is a critical variable, since the whole financial chain is structured on the expectation of receivable returns.

Moreover, the degree of a countries' economic instability also affects the condition of doing business. Macroeconomic imbalances or market failures in the microeconomic dimension might equally affect the supply and the demand of credit, particularly in the housing sector. To circumvent these problems, legal tools must be suitably designed to mitigate risks associated with the economic and institutional environment. In other words, developing countries that usually are more economically vulnerable, require specific legal tools to support the intended transition toward a mortgage market system.

The literature sustains that the housing industry presents specific financial characteristics that make it a challenging undertaking for policy makers committed to financial liberalization reforms. These specific characteristics include the extended loan maturity period, the debts value, and borrowers' profile, who are individuals or families. Recognizing these features, Carneiro and Goldfajn[22], and Carneiro and Valpassos[23] map several types of risks associated with housing finance, such as credit

[22] D. Carneiro and I. Goldfajn, *A Securitização de Hipotecas no Brasil*, Texto para discussão do Departamento de Economia PUC-RIO, no. 246 (2000), pp. 6-7.
[23] D. Carneiro and M. V. Valpassos, *Financiamento à Habitação e Instabilidade Econômica: experiências passadas, desafios e propostas para a ação futura* (Rio de Janeiro: FGV, 2003), pp. 6-7.

risk, mismatch risk, liquidity risk, and prepayment risk. All these risks are highly permeable to the economic and institutional conditions prevalent in different countries. Since developing countries are fraught with macro and micro economic failures, these risks are intensified.

To mitigate part of these risks, the literature identifies which legal tools are more suitable to the different countries' economic realities[24]. In more stable economies, less prone to macroeconomic oscillations, a typical mortgage contract has fixed interest rates, so that financial repayment conditions are defined at the moment one enters into the contract. This is the housing contractual model prevalent in the United States, in which the mortgage provides fixed-rate interests – FRM (fixed-rate mortgage)[25]. In less stable economies, in turn, the fixed interest rates can make the contract too rigid in the long-term, which is why the literature identifies adjustable-rate mortgages – ARM as being more appropriate[26]. In turn, in very vulnerable and more unstable economies, the most common type of mortgage is dual index mortgages – DIM. In this case, the indexers update the monetary value of installments, as well as the outstanding balance. The DIM model might reveal problems if both indexes (those of the installment and balance sheet) are incompatible. In this case, the monthly repayments may not be able to liquidate the incurred debts, which makes settling the outstanding balance exorbitant. This was precisely what happened to the SFH (Housing Finance System) during the Brazilian hyperinflation in the 1980s, which led the leading state-owned bank on housing finance, BNH (Housing National Bank), to bankruptcy [27].

In addition to readjustment forms, another important element of financing contracts is the procedure for eviction in case of default, which ensures contract credibility. There are two possibilities for the enforcement of a defaulted contract: judicial and extrajudicial proceedings. The literature acknowledges the first one as being prevalent in developed countries, where courts are perceived to run more effectively[28]. In these cases, it is up to the creditors to engage the debtors through the judiciary branch, thus establishing a process that will result either in settling the debt

[24] Lea (2009), *supra* note 11, pp. 50-62.
[25] Ibidem, pp. 50-52.
[26] Ibidem, pp. 52-56.
[27] J. M. Aragão, *Sistema Financeiro da Habitação – uma análise sócio-jurídica da gênese, desenvolvimento e crise do sistema* (Curitiba: Juruá, 2007).
[28] Chiquier, Hassler, Butler (2009), *supra* note 11, pp. 106-112.

or recovering the asset. This is the most common process in countries like the United States and the United Kingdom.

In developing countries, the perception that courts are inadequately run, slow and uncertain has led to the dissemination of the extrajudicial enforcement model[29]. As Chiquier, Hassler, and Butler report[30], notaries handle debt enforcement and are charged with notifying the debtor and recovering the asset. This model is prevalent in countries like Croatia, Sri-Lanka, Pakistan, and Brazil, where the judicial branch is no longer the only locus for mortgages' legal arbitrages.

Ultimately, though the ways of enforcement are typically a procedural matter, the eviction rules tend to be associated with the mortgages substantive rules. Judicial enforcement is convergent with debt contracts in which the credit holder becomes the financed asset owner, and the asset is recorded as a collateral to ensure the payment. This is the conventional mortgage, in which the house bought for someone is the loan's guarantee. In this case, the judicial process of debt collection consists of enforcing the collateral, i.e. taking the housing from the credit holder in the case of default.

However, extrajudicial enforcements converge with a different modality of mortgage in which the asset's ownership remains with the creditor (usually the bank), which grants the use of the asset to the credit holder. This modality is known in the literature as a "deed of trust" or "lease-purchase contract"[31]. Creditors understand this type of mortgage as being safer because in the case of default the creditor has only to consolidate the property that the debtor owned under a condition subsequent. Generally, ownership consolidation is obtained through extrajudicial proceedings. As Chiquier, Hassler and Butler[32] point out, adjustments of this kind have been used extensively in developing countries such as Russia, Thailand, Turkey, and Brazil. The table below outlines the varieties of mortgage contracts.

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[29] H. J. Dübel and S. Walley, "Consumer Information and Protection", in L. Chiquier, M. Lea, *Housing Finance Policy in Emerging Markets* (Washington: World Bank, 2009), p. 148. According to Dübel and Walley: "clearly, inability to enforce efficiently through the courts – and parallel absence of meaningful pre-foreclosure arrangements – is a main reason behind the predominance of lease-purchase contracts in many emerging markets. In Brazil, approximately three-quarters of new housing transactions take place through lease-purchase; in Egypt, the share is approximately 90 percent."

[30] Chiquier, Hassler, Butler (2009), *supra* note 11, pp. 106-112.

[31] The economic literature calls this contract as deed of trust" or "lease-purchase contract". Brazilian lawyers instead call it by "fiduciary sale in guarantee" or "fiduciary assignment of real estate". This paper will employ the economist's use because it seems to be more standardized. I will employ deed of trust, as it done by Lea (2009), *supra* note 11, pp. 50-62.

[32] For Chiquier, Hassler and Butler, "this device has been observed on a large scale in most emerging countries such as Brazil or Turkey, where mortgage markets have not been developed through banks, as developers need to commercialize their production" (2009), *supra* note 11, p. 101.

Table 2. Types of contracts and forms of enforcement

		Degree of Economic Stability	
Degree of Courts' Effectiveness		**Stable Economies**	**Unstable Economies**
	Effective Courts	Fixed-rate mortgage Judicial enforcement	Double-indexed mortgage Judicial enforcement
	Ineffective Courts	Fixed or Adjustable-rate mortgage Extra-Judicial enforcement	Double-indexed mortgage Extra-Judicial enforcement

Drafted by the authors

The deed of trust (or lease-purchase contract), with extrajudicial eviction and flexible conditions for interest rate adjustments are the main legal tools that rule the mortgage market in developing countries.[33] These legal tools combine flexibility to deal with macroeconomic imbalances with rigidity to mitigate market risks. The flexibility that adjustable-rate mortgages introduce circumvent losses associated with inflation or other macroeconomic imbalances. The rigidity that deed of trust and extrajudicial eviction brought alleviate economic losses derived from contractual defaults. When combined flexible and rigid conditions should enable safer market transactions and, consequently, foster the envisioned transition toward financial liberalization.

3.3.Institutional Reform Strategies

In addition to financial design changes and the establishment of suitable legal tools, the third branch of housing reform is the reform strategy itself. Although there is wide academic and policymaking knowledge on the types of legal tools that are more adequate for each financial system and national economy (developed or developing), the transition toward liberalization is far from an easy task. The massive institutional reforms that happened in the last decade have shown how difficult it is to overcome the entrenched interests galvanized in legal-political orders. The existence of switching costs and the prevalence of asymmetric returns among incumbents and entrants make the institutional arrangements seriously path dependent and permeable to the resistance

[33] Chiquier, Hassler, Butler (2009), *supra* note 11.

of privileged interest groups.[34] The awareness of these problems raises questions on what is the adequate institutional reform strategy.

In a broader sense, one can categorize institutional reforms employing the Schumpeterian typology for innovation as an analogy. Like there are radical and incremental kinds of innovations; the reform process also has abrupt and gradual possibilities. Radical innovation breaks the economic cycle and introduces new process and products. Similarly, abrupt institutional change implies a brusque disarrangement of previous institutional equilibrium, thus provoking "radical shifts"[35]. In turn, incremental innovation produces continuous smoother economic transformations, and analogously the gradual reform generates a long-standing transition of previous legal-political order[36].

Although both pathways might be pursued, the accumulated wisdom has indicated that gradual pathways tend to lead to more successful economic reforms[37]. In particular in a research on Eastern Europe's privatizations, Pistor and Turkewitz[38] highlighted that the transition from state to market did not happen in a single round, with the market abruptly substituting the state. Therefore, privatization is not a clear-cut event, but a continuous process of transformation that navigates an interval between state and private property. This interval is in itself dynamic, and the state and market can reposition themselves over time. In other words, privatization is less associated with "radical shifts", than with a steady interplay between players.

In addition, Berkowitz, Pistor, and Richard[39] also examined the success rate of the legal transplant of market-friendly Laws in Eastern European countries in the 1990s. The authors found evidence that links the reformers' rate of success to their capacity to introduce new legal devices that were familiar with the countries' legal

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[34] On path dependence see Bebchuck, L. A. and Roe, M. J. "A theory of path dependence in corporate ownership and governance", in J. N. Gordon, M. Roe (eds.), *Convergence and persistence in Corporate Governance* (Massachusetts: Cambridge University Press, 2004)
[35] T. J. Pempel, *Regime Shift: Comparative Dynamics of the Japanese Political Economy* (Ithaca, NY: Cornell University Press, 1998).
[36] W. Streeck and K. Thelen, *Beyond Continuity: Institutional Change in Advanced Political Economies* (Oxford: Oxford University Press, 2005).
[37] K. Pistor and J. Turkewitz, "Coping with Hydra – state ownership after privatization, a comparative study of the Czech Republic, Hungary, and Russia", in R. Fryman, C. Gray, A. Rapaczynski, *Corporate Governance in Central Europe and Russia*, v. 2 (Budapest, London, New York: CEU Press, 1996); M. M. Prado and M. Trebilcock, *Path Dependence, Development, and the Dynamics of Institutional Reform*, 59 University of Toronto Law Journal, no. 3 [2009]; M. Andrews, *The Limits of Institutional Reform in Development: changing rules for realistic solutions* (New York: Cambridge, 2013), pp. 35-64.
[38] Pistor, Turkewitz (1996), *supra* note 37.
[39] D. Berkowitz, K. Pistor, J. F. Richard, *Economic development, legality, and the transplant effect*, 47 European Economic Review, no. 1 (2003).

heritance. Conversely, the failure rate increased proportional to the attempt to introduce legal tools unrelated to the countries' legal history.

Similarly, Trebilcock and Prado[40] claim that policymakers should strategize reforms in a way that path dependency factors play a favorable role. To them, institutional change is a work in progress, which means that the final goal is the function of successive modifications that stimulate the next round. The first step in this process begins with a slight adaptation of the prevalent arrangement, in a way that incorporates the incumbents and the existent institutions. For instance, if state-owned banks are key players in the state-led arrangements, the economic reforms tend to be more successful based on the extent that those players are understood to be part of the solution and not part of the problem. In other words, policy makers would be more successful if they strategize the reform to include the state-owned banks in the package.

The Trebilcock and Prado[41] model resembles the regulatory dualism tactic that Gilson, Hansmann and Pargendler[42] highlight in their capital market reforms comparison. Regulatory dualism introduces a new regulatory framework in parallel to the old one, thus enabling the simultaneous enforcement of two regulatory regimes. Accordingly, while the new rules apply only to the entrants, the incumbents follow the former status. This way incumbents preserve their benefits and do not have economic reasons to align and block the reform.

In a broader analysis of the trend toward the expansion of market spaces over public domains, Streeck and Thelen[43] present different possibilities of gradual, but permanent institutional transformation. Among the varieties of incremental possibilities, the authors set forth their well-known model of "layering." Layering is a gradual reform strategy that consists of putting a new institutional layer above the prevalent arrangement. Thus, the former institutions fade away in a steady movement, while the new layer slowly takes their place. Even though it is gradual, layering is a process of permanent institutional change, since at the end of the adjustment the institutional arrangement has different compositions and functionalities.

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[40] Prado, Trebilcock (2009), *supra* note 37.

[41] Ibidem.

[42] R. Gilson, H. Hansmann and M. Pargendler, *Regulatory Dualism as a Development Strategy: Corporate Reform in Brazil, the U.S., and the EU,* Stanford Law and Economics Olin Working Paper no. 390 (2015).

[43] W. Streeck, K. Thelen (2005), *supra* note 36, p. 16-33.

All these pieces converge toward an agreement on what tend to be the most successful reform strategies. They suggest that the more incremental and closely associated with the institutional legacies the strategy is, the more successful the institutional reforms will be. Somehow, Brazilian policy makers adopted that recipe in the housing sector. The reform's demobilization of the developmental arrangement and the creation of a mortgage market followed an incremental step. The real-estate financial system (SFI) should have gradually overlapped the former housing financial system (SFH), progressively replacing it. In this gradual step, policymakers introduced adjustable-rate mortgages, lease-purchase contracts, and an extrajudicial eviction procedure, thus establishing the institutional infrastructure required a mortgage market to blossom. Part of these legal tools was already known in the Brazilian legal culture, as it is the case of lease-purchase contract. A variety of this contract was previously established in the 1960s, to structure transactions with consumer goods, such as vehicles. Thus, the introduction of this contractual modality for housing finance in the 1990s did not provoke legal irritants in the domestic legal order.

However, twenty years later, the current stage of this process reveals a different result. Instead of the SFH being gradually substituted, the former state-players dominated the new institutional framework. The CEF has been the main player in the mortgage market and has profited from the improvements in legal security. The next section will describe the Brazilian reform and will examine the extent to which the institutional arrangement transitioned from a developmental state to a neoliberal arrangement. The fifth section returns to the institutional reform debate and discusses analytically the institutional change that occurred in the housing system.

4. Brazilian Housing Reform: From Developmentalism to Neoliberalism?

Prior to the SFI, Brazilian housing finance relied on the SFH, which was instituted in 1964 through the enactment of Law n. º 4.380. The system exhibited developmental state features, relying on policy-directed credit and mixed ownership.

In terms of funding, the SFH counted on two parallel savings modalities: voluntary and compulsory savings. Voluntary savings, also governed by Law n. º 4.380, gathered resources from the Brazilian Savings and Loan System (SBPE, acronym for "Sistema Brasileiro de Poupança e Empréstimo"). On the other hand, the compulsory system, regulated by Law n. º 5.107/1.966, consisted of a tax-like extraction of resources, where companies are required to pay a percentage of a worker's income to a governmental fund (FGTS, acronym for "Fundo de Garantia por Tempo de Serviço"). Both resources constituted the funding for SFH's disbursement of housing loans.

In addition to the funding, the two other components of SFH were the financial institutions and the BNH. The financial institutions, usually banks, private or state-owned, disbursed resources to credit holders, and the BNH performed regulatory functions. Under this system, BNH had two main regulatory functions. First, it determined the amount of savings, raised voluntarily or compulsorily, that private or state-owned banks should use for housing loans. This regulation shaped the directed-credit policy and ensured the channeling of a minimum plateau of housing resources to credit holders. Second, the BNH worked as a quasi-Central Bank agency. As Aragão[44], the last BNH chairman explains, BNH played the role of lender of last resort by providing liquidity for financial institutions – which is a typical feature of Central Banks.

The SFH was considerably successful. Data collected by Royer[45] reveal that, between 1964 and 1986, this arrangement financed about 4.5 million housing units. Comparatively, the previous government-led initiatives in this area, such as Welfare Institutions (IAPs) and the "Fundação da Casa Popular" (FCP), active between 1930 and 1964, financed approximately 170,000 (new or second-hand) residential units[46].

However, in the 1980s the hyperinflation compromised the system's financial sustainability. At that time, financial rules established a dual index type of mortgage - DIM - that embodied two parallel indexes, one applied to the readjustment of the monthly payment and the other applied to the balance due. For a while, during hyperinflation, the BNH attempted to conciliate the cost of loan readjustment with the wages' loss of purchasing power. Following this policy, BNH updated the monthly payment cost to lower than it readjusted the balance due value. In the short term, the policy benefited the debtors, but they soon realized that they would not be able to liquidate the outstanding balance.

The crisis' peak came when the conflict between mortgagors and the BNH created a mass litigation, a true legal battle[47]. The courts ruled against BNH, which led the bank into bankruptcy. In a nutshell, courts decided that part of the financial rules

[44] Aragão (2007), *supra* note 27.
[45] L. Royer, *Financeirização da Política Habitacional: limites e perspectivas* (São Paulo: Faculdade de Arquitetura e Urbanismo da Universidade de São Paulo, Tese de Doutorado, 2009), p. 65.
[46] Aragão (2007), *supra* note 27.
[47] Ibidem, pp. 276-429.

defined by BNH to update contractual costs were illegal, to the extent that they violated the initial contractual agreements (*pacta sunt servanda*). These decisions employed a formal interpretation of the contracts and prohibited BNH from applying monetary correction rules, which ultimately affected the housing finance tremendously. As a consequence, BNH assumed all the inflationary losses and went bankrupt. The courts' decisions mostly protected middle class individuals, who had mortgage contracts, at the expense of the main governmental housing financial tool.[48] As a consequence the Federal Government discontinued BNH in 1986[49], leaving the SFH institutionally adrift.

For more than a decade after 1986, despite the high deficit of housing in urban areas, there was not an overarching housing financial system rearrangement. The SFH suffered successive incremental reforms aimed only at enabling minimum housing financing policy maintenance. As a part of these reactive reforms, the CEF inherited a large portion of the BNH's urban development bank attributions. The National Monetary Council, which is the Brazilian monetary authority, assumed the directed credit policy regulations, and the Central Bank, which functions under the Monetary Council's supervision, has been in charge of lend of last resort lending attributions. A more ambitious reform only took place at the end of the 1990s, when the civil construction sector mobilized political resources and led the formulation of a new framework in the sector[50].

The creation of the SFI in 1997 was meant to build an alternative institutional arrangement to substitute the SFH. Governed by Law n. º 9.514, the SFI favored financial liberalization and had the following legal characteristics: (i) articulation between real estate financing and capital market activities; (ii) freedom of contract between parties without subsidies or directed-credit policies; (iii) preference for private

[48] BNH played different roles from housing contract regulation to mortgage financing to urban development finance, which included low-income housing.
[49] S. Azevedo, *Vinte e dois anos de política de habitação popular (1964-86): criação, trajetória e extinção do BNH*, 22 Revista de Administração Pública, no. 4 (1988), pp. 108-109.
[50] E. Maricato, *Política urbana e de habitação social: um assunto pouco importante para o governo FHC*, 1 Revista Praga no. 6 [1998]; A. V. Gomes, *Direito e Financiamento: as transformações regulatórias na passagem do sistema financeiro de habitação para o sistema de financiamento imobiliário* (São Paulo: Faculdade de Direito da Universidade de São Paulo, Dissertação de Mestrado, 2015).

financial institutions over state-owned banks[51]. The creation of the SFI did not revoked the SFH, since the reform strategy was to gradually replace the latter by the former.[52].

Far from being trivial, the intent of combining real estate financing and the capital market demanded a deep reform in contractual rules. The new system required, for example, the constitution of a higher legal security standards than those available in the Civil Code. Following the worldwide policy recommendations, Law n. º 9.514/97, introduced legal devices to protect the credit market, thus setting forth a new type of mortgage and a specific procedure for eviction.

The new type of mortgage is the *deed of trust* (or lease-purchase contract) that alters bargaining power between the creditor and the credit holder. As pointed out earlier, while in conventional mortgages the credit holder has property rights over the asset, in the *deed of trust* the property rights are allocated to the creditor until the final payment of the balance due. Therefore, if the debtor defaults, the financier is already the legal proprietor, which makes the procedure of taking over the property easier .[53] In addition, Law n. º 9.514 also establishes that eviction shall be processed via extrajudicial enforcement. In the event the borrower defaults, the notary has only to consolidate the property in favor of the creditor's name.[54]

In addition, Law n. º 10.931 brought a new rule that reinforces this extrajudicial process. Article 50 imposes a sort of entry barrier in the judicial system by determining that in the judicial filings the plaintiff must clearly specify the disputed amount. In other words, if there is a dispute concerning the owed amounts throughout the financing, it is the plaintiff's burden to objectively circumscribe the disputed amounts and keep the

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[51] Carneiro, Valpassos (2003), *supra* note 23; Royer (2009), *supra* note 45; Gomes (2015), *supra* note 50; M. Fix, *Financeirização e Transformações Recentes no Circuito Imobiliário no Brasil* (São Paulo: Instituto de Economia da Universidade Estadual de Campinas, Tese de Doutorado, 2011).

[52] The following excerpt of the bill's explanatory statement, which resulted in Law n. º 9.514, summarizes the model: "This bill complies with the economy's deregulation guidelines and with the modernization of the instruments and mechanisms that finance productive activity. Its main goal is to establish the minimum required conditions for the development of a real estate finance market, for which it creates new instruments and mechanisms allowing for free credit operation in the housing sector and for the mobilization of capitals required for its revitalization. The creation of new negotiable instruments (securities), destined for secondary market operations. The creation of this new instrument accompanies the definition of the legal conditions for the effective securitization of real estate credit, provided there are rigorous safety mechanisms and investor protection. Thus, unprecedented perspectives for a secondary market of real estate credit and for private fundraising can enable strengthened housing finance". Brasil, *Lei nº 9.514 de 20 de novembro de 1997*, Law of the Housing Financial System (1997), pp. 23-24.

[53] Articles 26 and 27 of Law 9514/97.

[54] Unlike mortgage contracts within Law 4380, in fiduciary titles of real estate the amount collected at the auction settles the debt, even if the amount received by the creditor is lower than the outstanding balance – it is a *non-recourse loan* modality.

payment of the undisputed portion. Previously, litigation over a parcel of contracts led to the full blockage of financial payments, until the court's final decision. Article 50 was designed to curb the use of the judiciary branch as a debtor's protective arena.

Both Laws, Law n. º 9.514 and Law 10.931, have also introduced a new legal provision to this industry that ensured higher protection for investors – the so called "fiduciary regime". According to the fiduciary regime, individual financial contracts can be segregated from corporate assets, which enables a higher protection for investors who buy mortgages-backed securities. Article 9 of Law 9514/97, established that the bonds issued by securitizing companies stand out from the company's assets themselves, thus enabling protection to bond holder against a company's solvency problems. Additionally, Law n. º 10.931 instituted the possibility for real estate projects' to be segregated in relation to the building company's assets. Thus, the investors who buy real estate unities mortgage-backed securities are safeguarded in the case of the building company's bankruptcy[55]. The table below outlines all legal provisions.

Table 3. SFI's New Legal Provisions

	SFH (pre-reform)	**SFI**
Substantive rules	Conventional mortgage	Deed of trust
	–	Fiduciary regime
Procedural rules	Judicial eviction judicial and exceptionally extrajudicial	Extrajudicial eviction
	Courts played a central role	Higher entry barrier to court process

Drafted by the authors

All in all, the new rules aimed to increase legal security and foster the mortgage market. Coherently, the SFI's main ambition was to redesign the housing financing in a way that the securitization of receivable incomes could be the main funding source for new ventures. In this operation, a financial housing contract, signed by a bank and a credit holder, is onerously yielded to a securitizing company. Securitizing company, in turn, issues a mortgage-backed security, named CRI (real estate receivable

[55] Royer (2009), *supra* note 45, pp. 117-121

certificate), and sell it in the secondary market to investors, in special to investment funds.

To sum up, the conception of SFI was fully anchored in legal predictability and certainty of legal vindication, otherwise the investment chain in mortgage-backed securities would become unsustainable. All legal novelties, such as the deed of trust, extrajudicial eviction, and the fiduciary regimes seek to insulate investors and attract new players to the financial housing system. [56]

4.1. Improvements in Legal Security *in Action*

Based on the recognition that legal security is the SFI's cornerstone, this section assesses the extent to which the new legal tools improved the legal security *in action*. There is ample literature claiming that courts are less effective in developing countries, particularly, in Brazil[57]. According to these claims, the lack of judicial enforcement leads to financial sector underdevelopment or to negative externalities, such as higher interest rates to offset legal failures.

In the Brazilian case, authors suggest the prevalence of judicial uncertainty,[58] caused by judges' inclination to protect debtors over creditors. In other words, according to this claim, Brazilian judges behave as a "legal Robin Hood," equalizing, via legal decisions, social inequalities instead of enforcing the law. The consequence of which is legal inconsistency in court decisions that then affects the proper function of the business environment. According to these authors, the legal uncertainty explains credit shortages in the country. [59]Data from The World Bank shows that the Brazilian domestic credit market is equivalent to 60% of the Brazilian GDP, which is a small

[56] The explanatory section attached to bill that resulted in Law n. º 9.514/97 summarized the proposed funding model: "the primary funding for these operations consists of resources channeled from the financial market through suitable legal instruments such as mortgage notes and bonds, among others. Financial entities can create financial housing contracts in general following the market conditions and employing the contractual rules already defined in civil and trade law. (…) In order to leverage the secondary market for real estate credit the bill established a new type of enterprise – securitizing company, created as a public company following the model adopted successfully in other countries. This securitizing company will be run through the acquisition of real estate credit alongside the companies issuing these credits, such as those that grant loans for real estate acquisition or production." Brasil (1997), *supra* note 52, p. 24.

[57] La Porta, Lopez-De-Silanes, Shleifer, Vishny (1997), *supra* note 5; La Porta, Lopez-De-Silanes, Shleifer, Vishny (1998), *supra* note 5.

[58] P. Arida, E. Bacha, F. Lara-Resende (2005), *supra* note 5.

[59] Ibidem; Pinheiro (2009), *supra* note 5.

market compared to other developing countries. In Chile, the credit market corresponds to 112% of its GDP; in China the credit/GDP ratio is 155%.[60]

The housing finance reform tackled the problem of legal uncertainty as a vital condition of the SFI's mortgage market consolidation. This section examines whether the reform achieved this output. The section is not aimed at assessing the quality of the courts' decisions. Rather, the purpose is to measure the extent to which the courts confirmed legislative legal security to the creditors as promised.

In this regard, the first analysis concerned the amount of lawsuits found in the courts. Since housing reform laws established severe limitations to judicial branch access, the judicial cases for housing controversies was expected to be comparatively lower than in other social rights fields. This hypothesis was confirmed, the research found only 1,007 appeals in 10 tribunals after 20 years of SFI enforcement. For Brazilian statistics, the number is considered a relatively small judicial case amount, which is an indication that the legal security policy was successful at establishing "barriers to entry" in the judiciary branch.

The analysis below classified these 1,007 appeals into two main sets: (i) appeals filed by banks (creditors), i.e., appeals in which financial institutions were featured as plaintiffs in the suit and (ii) appeals filed by debtors, i.e., appeals in which banks were featured as defendants in the suit.

Financial institutions featuring either as appellants or appellee in the court appeals is an indicator of success (bank as an appellee) or failure (bank as appellant) in the first judicial decision. In other words, if the bank has appealed, the paper assumes that the first judicial decision favored the debtor; if the debtor appealed, it means that the first decision favored the banks. Accordingly, if the banks were featured more as appellees rather than as appellants, and if they had more favorable decisions in these appeals than debtors, it would confirm that the reform achieved its legal output.

The table below points out that banks overwhelmingly appear as appellees, both in injunctions and final appeals. In the injunction appeals, the banks were appellees in 341 cases, compared to 101 cases in which they were appellants. The trend is replicated in final appeals: banks appealed in 99 cases and they were the appellees in 466 cases.

60 Data available at: https://data.worldbank.org/indicator/FS.AST.PRVT.GD.ZS?end=2017&locations=BR-CL-CN-IN-US-MX&start=1990

As has been emphasized, this data indicates that banks have been more successful than debtors in first instance rulings.

Moreover, the courts' results also highlight a primacy of creditors over debtors. Among the 442 injunction appeals analyzed, banks won 287 cases, compared to 155 positive results for debtors. Among the 565 final appeals, banks won 433 cases, compared to 132 appeals favorable to debtors.

Table 4. Bank Appeals

		Injunctions				Appeals			
		Bank as Plaintiff		Bank as Defendant		Bank as Plaintiff		Bank as Defendant	
Courts	n.º	Granted	No	Granted	No	Granted	No	Granted	No
TRF 1	46	0	0	0	1	2	7	7	29
TRF2	198	4	2	2	25	6	8	16	135
TRF 3	255	9	14	4	112	1	9	3	103
TRF 4	300	4	12	60	83	7	28	18	88
TRF 5	40	2	2	1	4	3	4	4	20
TJSP	150	13	35	21	26	6	9	12	28
TJRJ	5	0	0	0	0	1	4	0	0
TJRS	6	4	0	1	0	0	0	0	1
TJDF	7	0	0	1	0	2	2	1	1
		36	65	90	251	28	71	61	405
		101		341		99		466	
Total	1007	442				565			

Drafted by the authors

In addition to a general analysis on the courts' decisions, this research also conducted a legal security assessment aimed at assessing each courts' position. In this scrutiny, the analysis below utilizes a coefficient of litigation that combines four elements:

a) Court Active Litigation Rate (CALR): obtained from the ratio between total appeals in which financial institutions are appellants and the number of appeals (injunction appeals and appeals) in the same court. This rate shows an abnormal situation; creditors should not need to appeal to the judiciary branch to assert their rights. Supposedly, the legal reform ensured better protection to creditors and their rights would be enforced by judicial decisions. This situation is abnormal because the bank should not need to appeal to assert its right.

b) Court Passive Litigation Rate (CPLR): obtained from the ratio between total appeals in which financial institutions are appellees and the number of appeals (injunction appeals and appeals) in the same court. This rate confirms the hypothesis that creditors would not need to appeal to the judiciary branch to assert their rights.

c) Active Success Rate (ASR): obtained from the ratio between total appeals (injunction appeals and appeals) which decided in favor of financial institutions as appellants, in relation to the total number of court appeals in which banks were appellants. This rate seeks to measure the number of appeals in which banks have won in court.

d) Passive Success Rate (PSR): obtained from the ratio between total appeals (injunction appeals and appeals) decided in favor of financial institutions as appellees, in relation to the total number of court appeals in which banks were appellees. This rate seeks to measure the number of appeals in which banks reverted a previously unfavorable decision.

Thus, indexes (a) and (b) measure the judicial case rate involving SFI contracts. Indexes (c) and (d) measure the success rate of lawsuits involving banks as a party, since appeal was unavoidable. The expectation was that banks success rate would be higher than their failure rate. The SFI's security coefficient is calculated as following:

SFI Security Coefficient = (CALR – CPLR) + (ASR – PSR)

In the table below, each index (a; b; c; d) ranges from zero (0) to (1). Therefore, the SFI security coefficient ranges on a scale from -2 (minus two) to 2 (two)[61]. The

[61] Since the equation's validation rule is that the CALR and CPLR be higher than zero, we know the maximum number will never precisely reach the highest values, -2 or 2; it could, mathematically and in extreme situations, at most reach a value that is very close to these limits. However, we have chosen to establish these fictional limits due to their proximity with the values prone to be reached and to simplify the interpretation of the coefficient.

closer it gets to -2, the higher the creditor security (the safer the court is for them); whilst the closer it gets to 2, the lower the creditor security (the more unsafe the court is for them). Based on this table and on the numbers obtained in the security coefficient calculation, the courts were classified into one of the following 7 security types: extremely secure; very secure; secure; relatively secure; insecure; very insecure; extremely insecure.

Table 5
Security coefficient classification scale

Range	**Classification**
[-2 to -1,5]	Extremely secure credit (lowest insecurity)
]-1,5 to -1,0]	Very secure
]-1 to 0]	Secure
]0 to 0,5]	Relatively secure
]0,5 to 1,0]	Insecure
]1,0 to 1,5]	Very insecure
]1,5 to 2]	Extremely insecure (highest insecurity)

Drafted by the authors

Table 6
Court legal security classification

Courts	**Total lawsuits**	**Legal Insecurity Coefficient**	**Classification**
TJRJ	5	0,80	Insecure
TJRS	6	-0,50	Secure
TJDF	7	0,17	Relatively secure
TRF 5	40	-0,28	Secure
TRF 1	46	-1,20	Very secure
TJSP	150	0,08	Relatively secure
TRF 2	198	-0,40	Secure
TRF 3	255	-0,27	Secure
TRF 4	300	0,09	Relatively secure

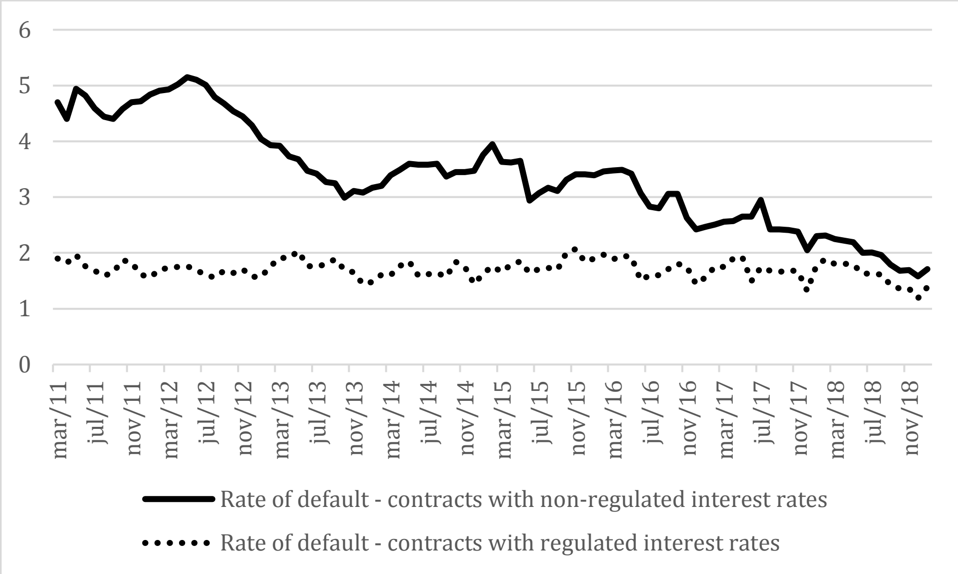
Drafted by the authors

According to the data collected, five out of nine courts ensure security for financial institutions. Four of these courts are TRFs (*Federal Regional Courts*) and one of them, TRF5, stands out as it is considered very safe. These courts altogether account for over 53% of lawsuits involving housing cases from those sampled. Since disputes involving the CEF fall under TRFs authority and not TJs (*Courts of Justice*), it is possible to claim that the CEF holds higher legal security compared to its private competitors. The only exception was TRF4, which, according to the scale, falls under the "relatively secure" classification; but with a very low coefficient number (0,09) that places it very near the "secure" range.

The TJSP (São Paulo Court of Justice) has a very low insecurity coefficient and also figures near the "secure range." The sum of TRF4 and TJSP's data show that 44% of the appeals were held in a "relatively secure" environment, very close to the "secure" range. Consequently, it can be concluded that the banks (private or state-owned) litigated with legal security in approximately 97% of the appeals involving the SFI, and from these appeals the legal security of 53% of the appeals reaches the "secure" and "very secure" ranges.

The data obtained in this sample is backed by Central Bank data concerning housing finance defaults. A contractual installment with payment(s) overdue for over 90 days is considered a non-performing loan. The data collected from the Central Bank shows a sharp drop in defaults in financing contracts with non-regulated interest rates. The data covers the last decade, but it corroborates the trend toward the improvement of credit security in housing finance.

Chart 1.
Non-Performing Loans – Directed credit resources



Source: Brazilian Central Bank

4.2. New Institutions, Old Organizations

The previous section showed how new legal tools improved the legal security and consequently created legal basis a mortgage market to blossom. This section assesses whether the mortgage market effectively flourished. In other words, it will examine the extent to which housing reform was capable of demobilizing the developmental state and instilling market relations in substitution. The SFI did not revoke the SFH, but rather the reform's purpose was to gradually dilute that duality by expanding the SFI over the SFH's market share. Thus, twenty years later, the expectation was to find the SFH phasing out and the SFI expanding.

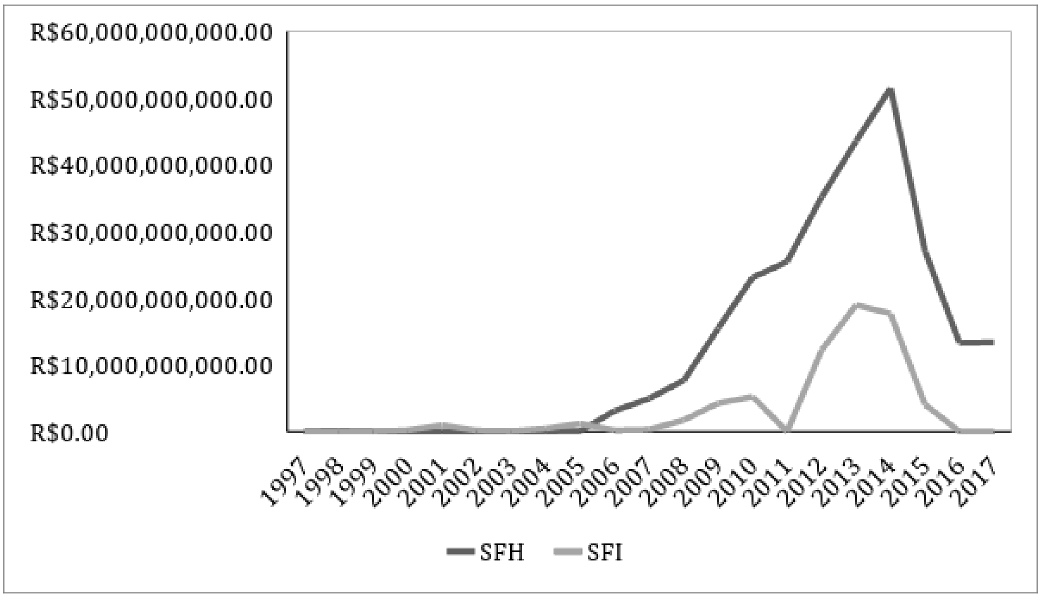
The examination of these qualitative aspects involved three parameters: (i) whether the mortgage market increased and CEF's market shares shrank as a consequence of legal reform; (ii) whether the introduction of new rules for the mortgage market changed the funding that support the housing economy; (iii) whether the new legal provisions have been confined around the SFI's limits or if these provisions spread beyond SFI's limits and reached the SFH's contracts. Items "(i)" and "(ii)" assess the resilience of old organizations and item "(iii)" evaluates the diffusion of new institutions. The hypothesis was that with the increased legal security the mortgage market would replace the CEF's lead in housing finance, while at the same time the main funding mechanism would be related to securitization (no longer state-based), and the deed of trust as well as extrajudicial eviction would be the leading legal tools for housing contracts.

On the contrary, however, the data collected indicate that the CEF still plays a prevalent role in housing credit provision. Most housing finance, whether SFH or SFI, has the state-owned bank as a creditor, which accounts for a market share equivalent to 70% of the industry as a whole[62]. An econometric research conducted by Martins, Lundberg and Takeda corroborates this interpretation[63]. The authors tested the effects of Law n. º 10.931/04 to diversify the housing financial channels. As previously described, the Law reinforced the legal security and created opportunities for private investment development in the sector. They conclude that, despite the Law, the most relevant housing finance instruments are still state-owned banks and directed -credit policies.

The volume of resources allocated in the SFH and SFI systems corroborates this evidence. The graphic below illustrates the scope of financial resources contracted within the SFH and the SFI, showing that the SFH volume is much larger than the one allocated via SFI. This means that in spite of policymakers' intentions, the housing reform was not able to substitute the previous financial system with the mortgage market. In other words, the mortgage revolution verified in other countries did not obtain the same results in the Brazilian economy, despite the implementation of similar legal reforms. The sharp decrease after 2014 was due to the Brazilian economic crisis.

[62] The information obtained in 06.02.2018 went thusly: "we inform that the CAIXA housing portfolio's market share is 69,02% in Dec/2017", CAIXA's National Operations, Housing and Processing Superintendence – Citizen Information Service. Information gathered from Citizens Information Services at CEF, via Law of Access to Information.
[63] Martins, Lundberg, Takeda (2011), *supra* note 7.

Chart 2
SFH and SFI in Financing Volume



Source: CEF

Furthermore, CEF's market share has increased since 2009 with the implementation of the My House, My Life Program (PMCMV). Set forth by Law n. º 11.977, PMCMV is a broad social program focused on low-income families with a monthly income limited to US$ 2,000.[64] CEF is this program's operating agent, thus financing and subsidizing poor mortgagors. The amount of CEF's subsidy varies according to the beneficiaries' income. For the poorest, CEF subsidized almost the entire housing (program's range 1) but the amount of subsidy diminishes as the beneficiaries' income increase.[65] The resources for these subsidies come from FGTS (compulsory savings) financial availabilities[66] and also from the governmental budget[67].

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[64] In 2017, PMCMV underwent changes and the limit was expanded to US$ 3,000.

[65] The PMCMV is divided into 3 ranges according to the beneficiary family income. In range 1, the CEF hires the enforcement of the real estate project and subsidizes up to 90% of its acquisition. The beneficiary pays a monthly installment for ten years where the amount monthly due does not exceed U$ 100,00 without interest. In range 2 (originally, families with income from 3 to 6 minimum wages; currently up to US$ 2,000 monthly) and in range 3 (income from 6 to 10 minimum wages, currently up to US$ 3,000 monthly), families pay higher installment, but they can count on subsidized interest rates. See, on PMCMV, C. Acosta, *O programa federal brasileiro "Minha Casa, Minha Vida" é um regulador-sombra das normas urbanísticas municipais?* (São Paulo: Escola de Direito de São Paulo da Fundação Getulio Vargas, Dissertação de Mestrado, 2015).

[66] Royer (2009), *supra* note 45.

[67] Ibidem. See also Ministry of Cities Information, available at https://www.cidades.gov.br/habitacao-cidades/programa-minha-casa-minha-vida-pmcmv. Also see R. Rolnik, R. Bischof, D. Klintowitz and J. Reis, *Como produzir moradia bem localizada com os recursos do Programa Minha Casa Minha Vida? Implementando os instrumentos do Estatuto da Cidade!* (Brasília: Ministério das Cidades, 2010).

In fact, the PMCMV not only was a social program, but also was a governmental anti-cyclical remedy adopted to stimulate the Brazilian economy in the subprime crisis aftermath .[68] CEF and other state-owned banks played a crucial role in the Brazilian economy to circumvent the negative effects of global turmoil. The research conducted by Barros, Silva, and Oliveira found that state-owned and private banks performed quite differently in global crisis: while the private banks contracted their credit offer, the state-owned banks expanded their loans and played a countercyclical role. As a whole, state engagement increased across several sectors during that period, which some author describes as new developmentalism or new state activism.[69] Thus, part of CEF's augmentation could be explained as a circumstantial event and closely associated with the governmental response to a global depression. However, this is not the whole story, because CEF has been the market leader regardless of new state activism. Even before the crisis, SFH was higher than SFI and CEF was the key player in both systems.[70]

The PMCMV's performance is comparable to the results reached by the BNH in the 1970s. Between March 2009 and September 2015, the PMCMV either financed or subsidized 2.4 million units.[71] The program has been compared to the BNH's performance not only for its quantitative merits, but also for its impact on urbanistic problems. Just like housing developments that took place in the 1960s and 1970s, PMCMV properties are located in areas with limited public resources. Above all, the program points to CEF's prominence a decade after SFI's creation.

Regarding funding mechanisms, they also indicate the prevalence of SFH's instruments, such as compulsory savings (FGTS) and directed-credit policies. Since 1998, due to the resolution n. º 2519 and n. º 2.623/99 established by National Monetary Council, the mortgage market relies partially on directed credit resources. In order to augment the mortgage market liquidity, a resolution authorized state-owned and private

[68] See on this, Abraão, G. O. *Programa Minha Casa Minha Vida: política habitacional ou pacote anticíclico?* (Campinas: Universidade Estadual de Campinas, 2014, available at: http://www.bibliotecadigital.unicamp.br/document/?down=000943860).
[69] L. C. Bresser-Pereira, *Reflecting on new developmentalism and classical developmentalism*, Review of Keynesian Economics, vol. 4, issue 3, 2016; D. Trubek, D. Coutinho, and M. Schapiro, *Toward a New Law and Development: New State Activism in Brazil and the Challenge for Legal Institutions*. In: C. Muller; T. Wang. (Org.). The World Bank Legal Review Volume 4: Legal Innovation and Empowerment for Development. 4ed.Washington: World Bank, (2013).
[70] This evidence aligns with interpretations on the long-standing basis of Brazilian developmentalism. CEF leadership is a part of a whole political economy arrangement in which the state is a relevant player. On this see M. Taylor, *The unchanging core of Brazilian State Capitalism, 1985-2015*, School of International Service Research Paper, no. 8 [2015].
[71] Data available at: http://www.brasil.gov.br/infraestrutura/2015/09/minha-casa-minha-vida-entregou-2-4-milhoes-de-moradias.

banks to count CRI (mortgage-backed security) investments as if they were housing loans for directed-credit purposes. In other words, whatever banks spend on CRI is computed as a compulsory allocation of housing resources[72]. Strictly speaking, the idea underlying the SFI's constitution was to allow debt securitization to provide resources to the housing industry, as is the case, in the North-American market[73]. The CMN rule n. º 2.623/99, however, represents a communication vessel between the old state-owned system and the new market-oriented one. In 2001, the interaction between the SFI and the SFH's financial bases was expanded. The FGTS' Board of Curators, through resolution n. º 375/01, authorized the FGTS to invest the fund's resources in CRI acquisition [74]. Thus, the CRI market gained further elasticity with the input from these state-based sources.

The housing reform also introduced a new segment to the funding: the securitizing companies in charge of issuing CRIs. This sector consists of nine major companies, which together account for approximately 90% of issuance; they are: Cibrasec; RB Capital; Brazilian Securities; Gaia; Ápice; Barigui; PDG; Habitasec; Novasec.[75] Among those cited, the two largest issuing entities are Cibrasec and RB Capital, which are responsible for about 50% of issuances.[76]

CEF and other state-owned banks are also players in this market, acting as partners with the main securitizing companies. Cibrasec, the first company established in this segment has state-owned banks as their shareholders, such as: Banco do Brasil; BB Banco de Investimentos S.A.; Caixa Participações S.A (Caixapar); Banco do Estado do Rio Grande do Sul (Banrisul); Banco de Brasília (BRB) and Banco do Estado do Espírito Santo. The Banco Panamericano was acquired by CEF and has corporate stakes in the Brazilian Finance Real Estate and Brazilian Securities.

Finally, the third element of this qualitative analysis is the spread or restriction of new contract models. As has previously been mentioned, Law n. º 9.514 introduced new legal mortgage options, but it did not make them mandatory. The legal framework prescribes that housing finance can be handled both within the terms of Law n. º 9.514 or within the terms of conventional mortgage legislation ruling.

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[72] Royer (2009), *supra* note 45; Gomes (2015), *supra* note 50, p. 110.
[73] Carrozzo (2005), *supra* note 21, pp. 765-805.
[74] Royer (2009), *supra* note 45; Gomes (2015), *supra* note 50, p. 110.
[75] Data obtained at CVM (Brazilian Securities and Exchange Commission) regarding 1999 and 2016.
[76] Data obtained at CVM (Brazilian Securities and Exchange Commission) regarding 1999 and 2016.

Nevertheless, deed of trust is now the standard contract widespread throughout all market income brackets, even for social programs such as the My House, My Life Program. CEF, which accounts for the largest market share in the housing sector, corroborates this by reporting that, currently, the bank only employs deed of trust for all of its housing contracts.[77]

Overall, the evidence points out that, despite credit security, there was not a full-fledged substitution of the state-led financial system for a market-led one. The three parameters of the analysis suggest that the gradual privatization glimpsed in the proposed model was not fully achieved. CEF is still the main housing finance agent and the SFH's finance instruments are interlinked to the SFI. On the other hand, the CEF absorbed the SFI contractual model, which granted safer operating conditions, thus reinforcing its incumbent's competitive advantages.

5. Developmental State and Neoliberal Tools

The housing reform that policymakers had envisioned embodied a gradual, but persistent transition from a state-led arrangement to a market-oriented configuration. Similar to other countries, Brazilian reformers strived to transplant the US mortgage market legal infrastructure. The primary objective was to replace the regulated savings, the credit-directed policies, and state-owned banks with voluntary savings, freely allocated credit, and a mortgage market closely associated with the capital market. The means to these ends would be the legal reform and the corresponding introduction of legal devices that could improve legal security, which arguably was a necessary condition for the mortgage market revolution.

However, as time went by, the results of this enterprise achieved different rates of success. The legal reform both in books and in action have prospered. Investment funds and banks, either state-owned or private-owned, have more secure legal tools to lend their financial resources. In addition, capital market players can also count with a broader basket of legal-backed securities to channel their investment such as the CRI, LCI, or CCI.

Notwithstanding all these institutional changes, the leading housing finance figures are still the same players inherited from the developmental period. The CEF is

[77] Information gathered from Citizens Information Services at CEF, via Law of Access to Information. The CEF response was the following: "Currently, there are no other real estate credit contract forms, for natural person clients, other than deed of trust".

the market leader and a portion of mortgage market funding comes from regulated and compulsory savings. Moreover, the state players have also benefited from the new legal tools. Compared to private banks, the courts' decisions indicate that the CEF has become more legally protected. The CEF is the only financial agent that operates under "very secure" conditions (table 6). In addition, CEF has profited from new investment opportunities introduced with the market reform. Since the 1990s, the Bank has been able to sell its financial contracts to securitizing companies as well as offer investment opportunities in mortgage-backed securities to its clients. A portrait of this institutional scene reveals a coexistence of developmental state players with neoliberal tools.

This claim diverges from the two prevailing views on the financial housing reform, those that come from the optimists and those that come from the pessimists. The optimists who are mostly economists have envisaged the transition from SFH to SFI as an inexorable condition to the housing finance. They fully believed that the improvement in legal security and the disentangling of regulatory nodes would foster suitable conditions for the mortgage market. For authors such as Carneiro and Valpassos[78], Carneiro and Goldfajn[79], Aragão[80], and Otto[81] credit security and financial liberalization would pave the way for the mortgage market to be accessible even to low-income consumers[82]. To put it differently, for optimists, market mechanisms would universalize housing access. On the other hand, the pessimists, who are mostly urbanists, have denounced the excessive financialization embodied in the institutional reform. For authors such as Royer[83], Fix[84], and Rolnik[85], the reform represented the colonization of global finance over local housing.

The claim of a coexistence diverges from both views because it emphasizes that the more salient reform outcome is the combination between new institutions with old organizations, instead of any kind of full-fledged institutional change. Although optimists and pessimists have clear different views on housing reform, they equally converge in the interpretation that housing reform provoked a sweeping institutional change. Nevertheless, the data examined favored a more nuanced understanding of the

[78] Carneiro, Valpassos (2003), *supra* note 23.
[79] Carneiro, Goldfajn (2000), *supra* note 22.
[80] Aragão (2007), *supra* note 27.
[81] Otto (2015), *supra* note 7.
[82] Carneiro, Valpassos (2003), *supra* note 23.
[83] Royer (2009), *supra* note 45.
[84] Fix (2011), *supra* note 51.
[85] Rolnik (2012), *supra* note 67.

case study. It is not clear that the housing system transitioned from a scenario of financial repression to one of financial liberalization. The most conspicuous characteristic of this arrangement is the coexistence between the developmental state and new neoliberal tools.

The prevalence of CEF in the financial system and the adoption of globally diffused legal tools, such as deed of trust or extrajudicial eviction, are pieces of evidence that confirm recent developments in regulation and privatization literature. Rather than describing the Regulatory State as a substitute for the Developmental State, authors such as Walter[86] (2006; 2008); Jayasuriya[87], Dubash and Morgan[88] and Levi-Faur[89] acknowledge that in developing countries the Regulatory State coexists with dirigiste properties, such as industrial policies, state-owned banks, and state-owned enterprises. Specifically, in the financial-monetary system, Walter[90] (2006; 2008) argues that although developing countries in East Asia have converged to global-neoliberal standards, they have maintained local institutional traits, in particular, developmental leverages over monetary and financial regulation.

The coexistence of developmental state and neoliberal tools also sheds light on institutional reform debates, mainly those that involve privatization and market-oriented changes. The current case study partially corroborates and partially challenge that literature, in particular those claims on the advantages of gradual changes and path dependency. The case corroborates the literature by describing the incumbents as part of the reform's viability and not as its necessary obstacle. Thus, it converges to the policy implication raised by authors such as Trebilcock and Prado,[91] and Gilson, Hansmann and Pargendler[92], according to whom policymakers should strategize reforms in a way that the institutional legacies should be considered in the reform

[86] A. Walter, *From developmental state to regulatory state? Japan's new financial regulatory system*, 4 The Pacific Review, no. 19 (2006); A. Walter, *Governing Finance: East Asia's Adoption of International Standards* (Ithaca: Cornell University Press, 2008).
[87] Jayasuriya, K., "Regulatory State with Dirigiste Characteristics: Variegated Pathways of Regulatory Governance", in N. K. Dubash and B. Morgan (eds.), *The Rise of the Regulatory State of the South: Infrastructure and Development in Emerging Economies* (Oxford: Oxford University Press, 2013).
[88] N. K. Dubash and B. Morgan, "The Rise of the Regulatory State of the South", in N. K. Dubash and B. Morgan (eds.), *The Rise of the Regulatory State of the South: Infrastructure and Development in Emerging Economies* (Oxford: Oxford University Press, 2013).
[89] D. Levi-Faur, "The Regulatory State and the Developmental State: Towards Polymorphic Comparative Capitalism", in N. K. Dubash and B. Morgan (eds.), *The Rise of the Regulatory State of the South: Infrastructure and Development in Emerging Economies* (Oxford: Oxford University Press, 2013).
[90] Walter (2006), *supra* note 86; Walter (2008), *supra* note 86.
[91] Prado, Trebilcock (2009), *supra* note 37.
[92] Gilson, Hansmann, Pargendler (2015), *supra* note 42.

agenda. The CEF example illustrates that state actors might benefit from institutional reforms, including privatization, and they might be potential supporter of institutional changes.

However, the case study also challenges some predictions of this literature by revealing an outcome that consists of a coexistence between the new and the old layers. The expectation with gradual reforms is one that the new layer would replace the old one. The Brazilian housing reform, in turn, reveals a different kind of process. Policymakers have set forth the SFI as a new layer, but the SFH has not faded away. At the same time, it does not seem accurate to describe that outcome as a simple reform failure. There were deep transformations in the Brazilian financial systems, which also affected the state players. Instead of a linear institutional reform, the case suggests a sort of institutional change in which the new arrangement mirrors a merger-like composition between the new institutions and the old organizations.

6. Final Remarks

The reform that instituted the SFI twenty years ago envisaged the integration of banks and capital markets through a gradual, layered reform. Inspired by the mortgage revolution that stemmed from the *Emergency Finance Home Act*, enacted in the 1970s in the United States, the SFI intended to strengthen credit legal security mechanisms and thus form the institutional bases needed to transform real estate contracts into capital market commodities. To this end, the reform relied on the introduction of legal innovations such as (i) new rules for mortgage contracts; (ii) fiduciary business rules, and (iii) the introduction of entry barriers to the judiciary branch.

Regarding the legal security, the data collected pointed to the satisfactory success of these measures. First, the lawsuits found are a considerably small quantity for the Brazilian panorama, which shows that the strategy of limiting the judicial access was successful. Second, in this sample, creditors succeeded more than the debtors, which suggests that the judiciary system upheld the policy behind the law. Finally, the Central Bank's data concerning housing finance defaults points to a substantial decrease in the number of non-performing loans, which indicates higher credit security.

However, concerning the extent to which the market relation expanded over the state domains, the achievement is different. The more robust legal security has not provided a complete financial transition from the developmental model to a neoliberal one. The integration between banks and capital markets has not become the prevalent layout. Both in contract numbers and in resource volume, the state-led arrangement (SFH) is still the key player in housing finance. It has had a higher market share than the SFI in the last two decades. Furthermore, CEF is the most prevalent financial provider of housing credit, and it also plays an active role in fostering the securitizing company market. On top of that, the regulatory resources inherited by the SFH, like directed credit, are relevant sources for the CRI market, helping to ensure liquidity in CEF's operations.

Therefore, the most apparent effect of the reform is a repositioning of old organizations in the new institutional frameworks, most notably CEF in the housing market. This conclusion sheds light on the institutional reforms and privatization debate by suggesting that credit security might be an over-valued variable in political agendas. Moreover, the paper emphasizes that state-owned banks could be players in the privatization processes, which allows them to influence the transformation process results. Privatization is not necessarily a clear-cut transition between two models, rather a political process subject to different organizations, different factors of resilience, and institutional coexistences.

Ultimately, one wonders if the "Developmental State with Neoliberal Tools" is a definitive outcome for this arrangement or only a long transitory composition that lasted for two decades. Although it is impossible to predict the future, it is feasible to recognize three potential scenarios. The first one is a possible stasis of the current coexistence, which would be in accordance with recent evidence on the interplay between Developmental and Regulatory State in the global south. The second possibility is a stronger colonization of market forces over policy purposes. Finally, the third one is the dominance of discretion-based mechanism over market incentives.

A possible driving force toward a market colonization over developmental state are the investors interests on the directed-credit resources. As explained before, banks (private or state-owned) must meet a minimum threshold of disbursement for housing purposes. These disbursement has interest rate caps and tend to benefit low income credit holders. If the regulation openly counts investment in mortgage-backed securities as if it were credit directed to housing, it might introduce a competition for these resources. As a result, the amounts that are currently channeled through direct-credit policies could be allocated away from the poor and destined to the acquisition of a broad variety of mortgage-backed securities, including those ones not directly associated with housing. In this case, the Developmental State will be out of the scene.

The second scenario could be where state mechanisms override the market. A possible driving force to this achievement is the vulnerability of the economy. As a peripheral country, Brazil is permanently exposed to external economic shocks that can compromise the soundness of its economy. In such a situation, the legal security ensured to private investors might be insufficient to keep the financial system at equilibrium. Depending on the extension of the crisis, the state might have to override the market and take over some part of the business environment. In this case, the Developmental State would become the sole provider of a monologue.

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