



CASE STUDY

Helping Students Afford the Career of their Dreams

IDEAL INVEST: Making University Accessible through
Student Loans in Brazil

March 2016



IFC

**International
Finance Corporation**
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ABOUT IFC

International Finance Corporation, a member of the World Bank Group, is the largest global development institution focused exclusively on leveraging the power of the private sector to tackle the world's most pressing development challenges. Working with private enterprises in more than 100 countries, IFC uses its capital, expertise and influence to help eliminate extreme poverty and promote shared prosperity.

ABOUT THE CASE STUDY

Expanding access to quality and affordable education is a central element to eliminating extreme poverty and promoting shared prosperity. In developing countries, private education providers play a critical role in the delivery of education, skills, and training that is affordable and relevant to the needs of the labor markets. The IFC education practice is developing several case studies that showcase success stories in the IFC education portfolio around scale, skills, and affordability. The case studies highlight how IFC clients have contributed to meeting IFC's strategic goals in education of: (1) developing skills and enhancing employability of graduates and trainees and (2) increasing reach and impact at all levels of education.

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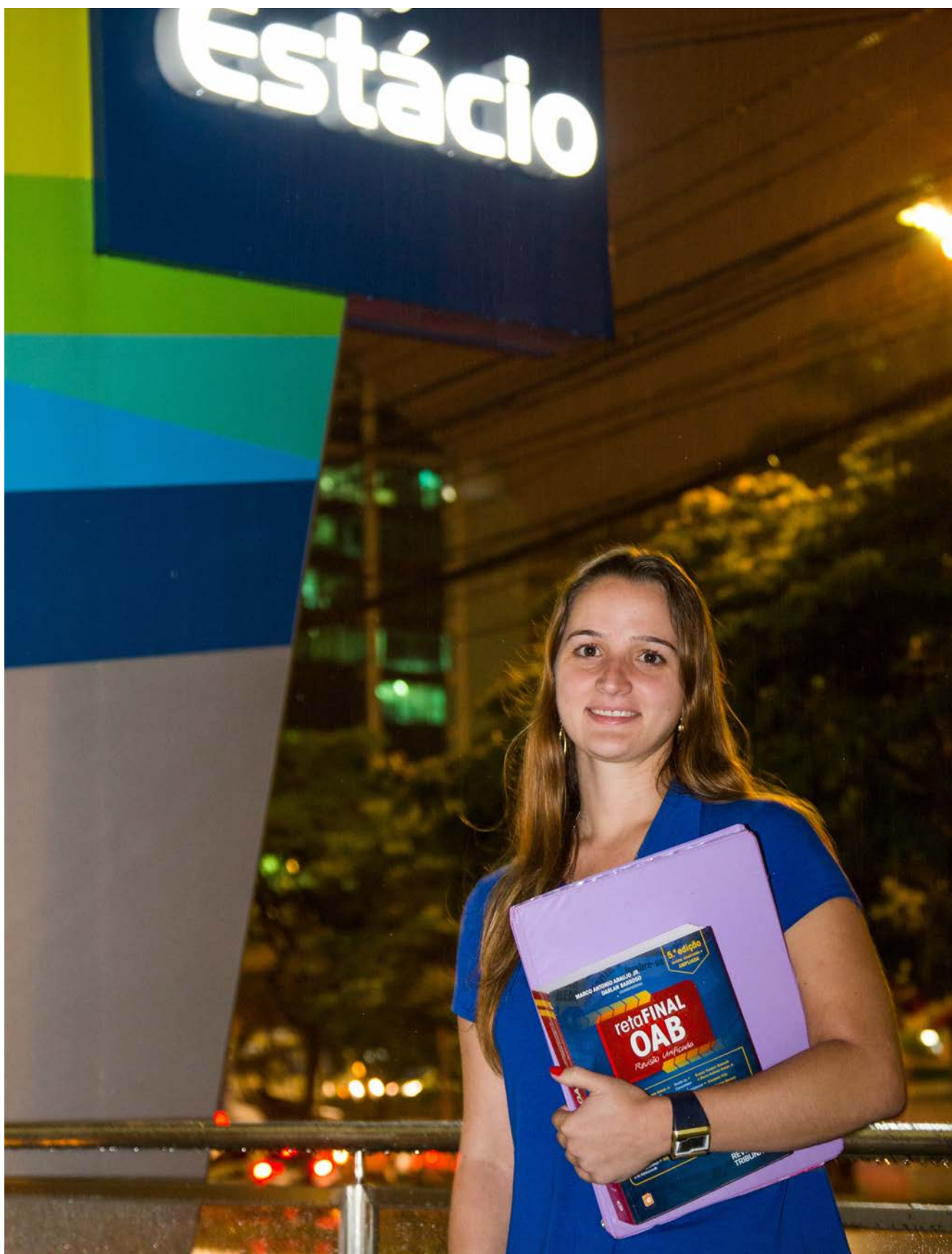


Photo © Ideal Invest

Camila Brandão Macedo is studying to be a lawyer at Estácio University and works as an intern in the legal department of a multi-national company.

DREAMS DO COME TRUE

Camila Brandão Macedo dreamt of becoming a lawyer, but she did not know how she could pay for it. Her father was a driver and her mother was a public school teacher. On their modest incomes, they found it hard to provide for the dreams and aspirations of their four children. Realizing that pursuing a legal career was beyond her means, Camila decided, at the age of 17, to get a degree in tourism since that was cheaper and within her financial reach. After two years of working in the tourism industry, her financial situation improved, and she enrolled in the legal program at Estacio University. She continued working in the tourism industry to pay for tuition and living expenses.

Mid-way through the law program, she was required to start a two-year internship to gain legal experience; however, the internship paid her less and she was not able to keep her tourism job. This cut her income in half to about R\$1,350 (US\$345)¹ a month. As her income decreased, her dream appeared to be in jeopardy, and she struggled to pay for tuition, school books, transportation, and food. She sought help from the “Fundo de Financiamento ao Estudante do Ensino Superior” (FIES) or the Fund for Financing Higher Education Students, but in the midst of austerity measures, the Brazilian government had scaled back the loan program and she was unable to get a loan. Then, a university official told her about the “PRAVALER” student loan program. This tip was a game changer for Camila.

PRAVALER “Sem Juros” (“Zero Interest”) gave Camila the flexibility to pay about R\$290 (US\$74) a month, which is half of her tuition. The loan allows her to pay part of the tuition while she is enrolled in school and the other half after graduation. The program helped her to stay on track. Camila remarked, “PRAVALER was the only viable alternative to continue studying without spending so much of my salary on monthly tuition.” She wished she had learned about PRAVALER before! She could have pursued her dream nine years earlier!

¹ The foreign exchange rate on March 3, 2016 was USD1 to BRL 3.91. www.oanda.com.



The PRAVALER student loan program helped Camila Brandão Macedo to stay on track.



“We can offer zero interest because the institution bears part of the cost to help the students.” Carlos Furlan, Ideal Invest CEO

Today, Camila continues working as an intern in the legal department of a multi-national fuel distribution company, and she feels much more fulfilled. She hopes to be hired by the company as a full time employee after her graduation. “I feel like it’s the beginning of a promising career. I love what I do, and I have the opportunity to work in the career that I always dreamed of.”

Carlos Furlan, CEO of Ideal Invest, S.A. (“Ideal”) explains the benefits of the program: “Ideal partners with selected universities to offer student loans at a zero interest rate. We can offer zero interest because the institution bears part of the cost to help the students.” Through their student loan program, the company is allowing thousands of Brazilian students to afford the degree of their dreams.

Ideal Invest, is a private, for-profit, banking correspondent company (a company that facilitates the loan origination process for banks) that is engaged in the provision of student loans for undergraduates, graduates, and students in technical programs. The company was established in 2001 and in 2006 it launched “PRAVALER,” its flagship student loan product. As of December 2015, the company had forged partnerships with about 475 universities, and since the beginning of its operations, has extended loans worth more than R\$1.5 billion (US\$383 million) to more than 60,000 students. Today, Ideal Invest is the leading provider of private student loans in Brazil.

The profile of students is also impressive. Seventy percent of Ideal’s students are the first in their family to obtain degrees and 55 percent of students are women. Students tend to enroll when they are older; the average age of a student is 24 years old. About 60 percent work while they are in school but earnings are typically about R\$1,000 (US\$255) a month, thus PRAVALER helps make tuition more affordable.

In an effort to bolster access to higher education through private institutions, in 2007, the government unveiled its Education Development Plan, which increased demand for student loans. As

a result, Ideal needed additional capital to grow the company. In October 2009, IFC played a catalytic role by investing R\$12 million, or the equivalent at that time of US\$7 million, in equity in the company. The investment came at a critical moment as the company was serving about 10,000 students and was poised for growth. IFC’s involvement coincided with turbulent times as the global economic crisis was unraveling. Ideal weathered the financial storm and went on to survive the strong competition that eventually came from FIES, but Ideal’s success was hard earned.

KEY SUCCESS FACTORS

Through challenging times, the key factors that contributed to the company's success were a focus on sustainability, affordability and partnerships:

SUSTAINABILITY

Long-term sustainability is at the forefront of thinking and drives every decision the company makes. To manage the risk, Ideal has developed a program of “responsible lending” in which the incentives are aligned for all the actors: the students, the universities, and Ideal Invest. Since Ideal bears all the risk of loss in the event of a default, it is only sustainable if the other two parties have “skin in the game.” Ideal is very selective with the students that receive its funds. All students must have a guarantor, and together, they must pass Ideal's proprietary credit risk analysis. Once approved and after the funds are disbursed, students start paying back a portion of the principal loan amount immediately. With the introduction of its latest product lines, the university puts its own capital on the line to finance more students.

AFFORDABILITY

PRAVALER helps students to afford a higher level of ambition by allowing them to choose the careers and institutions that are their first choice instead of choosing the careers they can afford without the loan. Students will have better employment prospects after graduation and are better positioned to achieve their professional ambitions. They pay about half the cost of tuition when they are in school and finance the balance. The repayment term is between 2 and 2.5 times the length of study. Ideal found that many Brazilian students were more comfortable with the shorter loan tenors. For the typical four-year program, the student would have completely repaid the

student loan in 8 to 10 years. The interest on many of the loans is subsidized by the institution, translating into significant savings for the student. Depending on the product, the interest rate can be as low as zero percent. Alternatively, they are competitive with other loans currently in the Brazilian market.

PARTNERSHIPS

Partners have been critical to Ideal's success. Several partners have been there at every step of the process from securing financing to selling the product. The financial partners have provided the necessary capital and priceless insights and advice. Similarly, universities and Ideal complement each other with a symbiotic relationship that benefits both parties. Ideal advances the cost of the tuition for the entire semester for a sizable number of students. This provides the university with a stable and predictable cash flow stream, allowing for greater planning of their working capital. In turn, the universities subsidize the interest on the student loan, transferring the savings to the students. In addition, the university helps to market PRAVALER to students.



Photo © Rodrigo Soldon/Wikipedia Commons

By 2014, Brazil had become one of the largest tertiary education markets in the world. Above, Rio de Janeiro's downtown.

COUNTRY CONTEXT

Brazil is one of the largest economies in the world, with a population of 206 million and a GDP of US\$2.3 trillion (2014).² In recent years, it was distinguished by its fast-growing economy and growing international influence. The Brazilian economy is diversified into several sectors, such as agriculture, mining, manufacturing, and services. Notwithstanding a recent period of rapid economic growth, the economy is currently grappling with a deep economic contraction and high inflation, which was 10.7 percent in 2015. These factors contribute to high cost of capital. From 1999 to 2015, the base lending rate, the SELIC, which is similar to the United States Federal Funds target rate, was an average of 15.7 percent. Interest rates for car loans were between 16 and 23 percent, while consumer loans ranged from 25 to 36 percent per year.

To fuel the economic engine of growth, Brazil has relied on a labor force of over 106 million people. It had an unemployment rate of 7.6 percent in January 2016.³ Nevertheless, Brazilian productivity levels have been low and enhancement of the quality of human capital through post-secondary education is important to increase its international competitiveness. Furthermore, while 26 million people were lifted out of poverty between 2003 and 2013, Brazil still faces high levels of income inequality and has a GINI coefficient of .53.⁴ For many, the path out of poverty is through post-secondary education.

Recognizing that it could not provide tertiary education to all Brazilians through public institutions alone, in 1997, the Brazilian government undertook a variety of reforms that encouraged private sector growth. The strategy worked and by the year 2000 there were 2 million students enrolled in private institutions. The market continued to experience dramatic growth, and today, private sector tertiary institutions account for 75 percent of student enrollment. By 2014, Brazil had become one of the largest tertiary education markets in the world with 7.8 million students. It has a market potential of 35 million students.

“The surge in enrollment in Brazil is due in large part to the widespread recognition that university graduates earn, on average, two and a half times more than students who don’t finish college,” explains Jon Marcus.

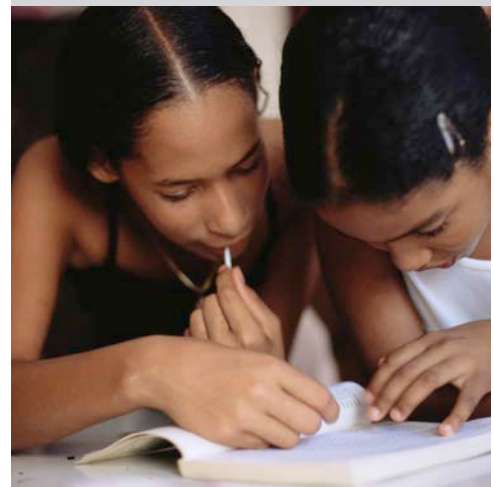


Photo © The World Bank

² <http://data.worldbank.org/country/brazil>

³ Instituto Brasileiro de Geografia e Estatística,(IBGE), Indicadores IBGE, Pesquisa Mensal de Emprego, Janeiro 2016.

⁴ The Gini Coefficient is a measure of income inequality. A Gini coefficient of 0 represents perfect income equality, while 1 implies perfect income inequality. <http://data.worldbank.org/indicator/SI.POV.GINI> February 2, 2016.



Photo © The World Bank

For many Brazilians the path out of poverty is through post-secondary education.

“The surge in enrollment in Brazil is due in large part to the widespread recognition that university graduates earn, on average, two and a half times more than students who don’t finish college—a bigger difference than that of any of the 34-member countries of the Organization of Economic Cooperation and Development (OECD).”⁵ While enrollment has increased, affordability remains a challenge with tuition costs that represent roughly one quarter of the average monthly salary. “The average monthly tuition of R\$500 (US\$128) is high ... when compared to the average monthly salary of R\$2,000 (US\$510).” To make tuition affordable, universities offered a monthly payment plan, but that was still out of reach for many.

To facilitate affordability, the government began by expanding the scholarship and the FIES student loan programs to help students cover the costs of study. In the boom years, about 30 percent of 5.3 million students benefited from government support.⁶ But in the recent era of austerity measures, FIES has been substantially scaled back from its peak of 730,000 total seats in 2014. In January 2016, the Ministry of Education announced that FIES had a student loan capacity for up to 250,000 seats for the first half of 2016, which could increase in the second half of 2016, but this still leaves a gap in access. Meanwhile, the private student loan market has been largely underdeveloped, except for a key player—Ideal Invest.

⁵ Marcus, Jon, “Brazil: Where the Free Universities Largely Serve the Wealthy,” *The Atlantic*, April 8, 2015.

⁶ Horch, Dan, “As Demand for Education Rises in Brazil, for Profit Colleges fill the Gap,” *The New York Times*, June 19, 2014.

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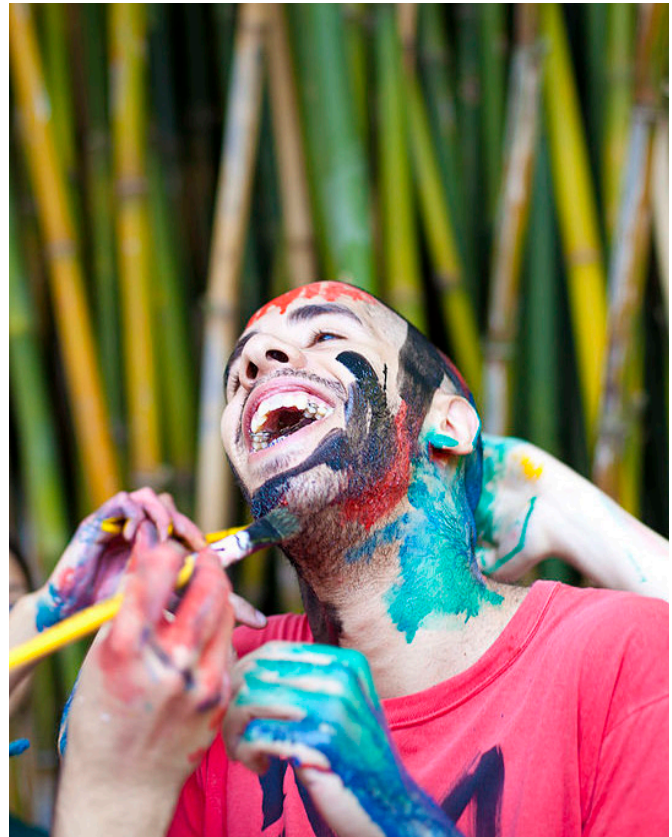


Photo © Ze Carlos Barretta/Wikipedia Commons

A Brazilian student has his face painted on the first day of college.



Photo © Saulo Cruz

Brazil has 7.8 million students and private sector tertiary institutions account for 75 percent of student enrollment.



Photo © The World Bank

While 26 million people were lifted out of poverty between 2003 and 2013, Brazil still faces high levels of income inequality.

ONE MAN'S JOURNEY TO HELP STUDENTS WHO CANNOT AFFORD TUITION

Since childhood, Oliver Mizne's parents invested in high quality education for their son. It was a worthwhile expense because he went on to get a degree from an Ivy League school in the United States. While he was still quite young, he secured a very good position at an investment bank. As luck would have it, the bank was sold and Oliver walked away with what became seed capital for a future venture. Reflecting on what to do next, he thought to himself, "Wow! This education thing really does work!"

He started thinking, "I was really lucky but what happens if your parents can't afford university? What happens if the degree a young, aspiring Brazilian really wants costs R\$1,000 (US\$255) a month and the family can only afford half of that? Or what happens if a student's family cannot afford the R\$500 (US\$128) per month?" He thought, "What a loss this is if the person does not have the means to pay." Oliver decided that he would help students out of this predicament. He concluded, "students would pay me the price that they could afford now and pay me the rest later!" His goal was to allow students to dream, as long as he could cover his costs in a sustainable manner.

In 2001, when Oliver founded the company, he settled on the name "Ideal Invest," to help everyone remember that while it is an investment company, "we're here for a larger ideal, helping students and their families. It's easy to get lost in the pursuit of profit and forget what you're here to do in the first place, so the name helps remind everyone that there's a larger goal behind the company." Ideal Invest initially began by offering working capital financing to private universities secured by tuition receivables but, in 2006, serendipity stepped in. The dean of a university invited Oliver to a function and put him on the spot. He made a surprise announcement to the audience that "we are going to work with Oliver on our first student loan partnership." A true entrepreneur, Oliver immediately jumped on the opportunity. A couple of other universities expressed an interest and within 6 months, 70 universities had signed up.

Since there was no "real" private student loan provider in the market, he had to create a new student loan product from scratch. Students who went to the bank to get a "student loan" were really offered a consumer loan, with a small value of about R\$800 (US\$204), a short tenor of 30 to 90 days, and with high interest rates. Oliver explained, "it was not really a student loan. If students went to the government, the previous generation of FIES was very hard to get. There was a lot of bureaucracy and not many openings." Oliver decided that "we needed a 'real' student loan: um crédito universitário PRAVALER!" "PRAVALER" means "for real" in Portuguese. The logo emphasizes that "it is easier" to afford tuition because students can pay in installments!

"We're here for a larger ideal of helping students and their families." Oliver Mizne, Ideal Invest founder.



Photo © Ideal Invest



Photo © Ideal Invest

The logo "PRAVALER," which means "for real" in Portuguese, ensures that students know that "it is so easy" to get an university loan.

PRAVALER: INNOVATIVE STUDENT LOAN PRODUCTS

Because Oliver invested his own personal capital, and that of his family and friends, he wanted to make sure that everyone involved in the lending ecosystem had a vested interest in the results. He believed that all parties needed to have “skin in the game,” to mitigate risk because Ideal bears 100 percent of the default loss. Even though Ideal is essentially in the business of financing a public good, the Brazilian government does not assume any risk of default on the student loan. As such, Ideal developed key business principles of “attracting the right clients” and strategically “aligning the incentives.”

1. ATTRACTING THE RIGHT CLIENTS

The size of the market is massive. In 2013 there were 2,090 private universities. To date, Ideal has partnered with about 475 private institutions yielding an institutional market penetration rate of about 25 percent. Notwithstanding, Ideal is not trying to reach the whole market. The company emphasizes that growth must be carefully managed. Since its own capital is at stake, Ideal is very judicious selecting the institutions it will partner with and the students it will lend to.

The PRAVALER product has evolved since its initial release 10 years ago, but the key principles remain. Students must meet certain criteria to be eligible for the student loan. All students must have a co-signer who acts as the guarantor. The student and guarantor must be able to demonstrate combined earnings of at least 2.5 times the value of the university’s monthly tuition. Students and guarantors must not have negative entries on their credit record, as provided by the credit bureau. If the student meets all the eligibility criteria, then Ideal will do a more in-depth credit analysis with its own tools.

Over the last 10 years, Ideal has continuously refined its credit scoring model, which is now in its fifth version. It is the only credit scoring model in Brazil that is specifically designed to evaluate credit risk for student loans. Over the years, Ideal has learned important lessons on the reasons students pay or do not repay the loans. Issues such as the distance students will travel to and from school, the degrees they select, the specific courses they take, and the quality of their educational institution all factor into the likelihood that they will repay on time. This information guides Ideal’s lending decisions.

In addition, Ideal uses both credit and repayment behavior scoring methods to evaluate risk. The student has to apply for a new loan at the beginning of each semester. At that time, Ideal re-analyzes the probability of default before extending a new loan. This thorough vetting of prospective borrowers has contributed to a low non-performing loan rate of 4.5 percent.

Ideal developed key business principles of “attracting the right clients” and strategically “aligning the incentives.”



Similarly, Ideal is selective with the institutions it partners with. Ideal has partnership agreements with about 475 institutions. Ideal looks at various factors in determining whether it will work with a given institution including the quality of the institution, its financial performance, the executive knowledge base, the quality of the academic programs, and employment prospects for graduates from that institution.

2. ALIGNING THE INCENTIVES

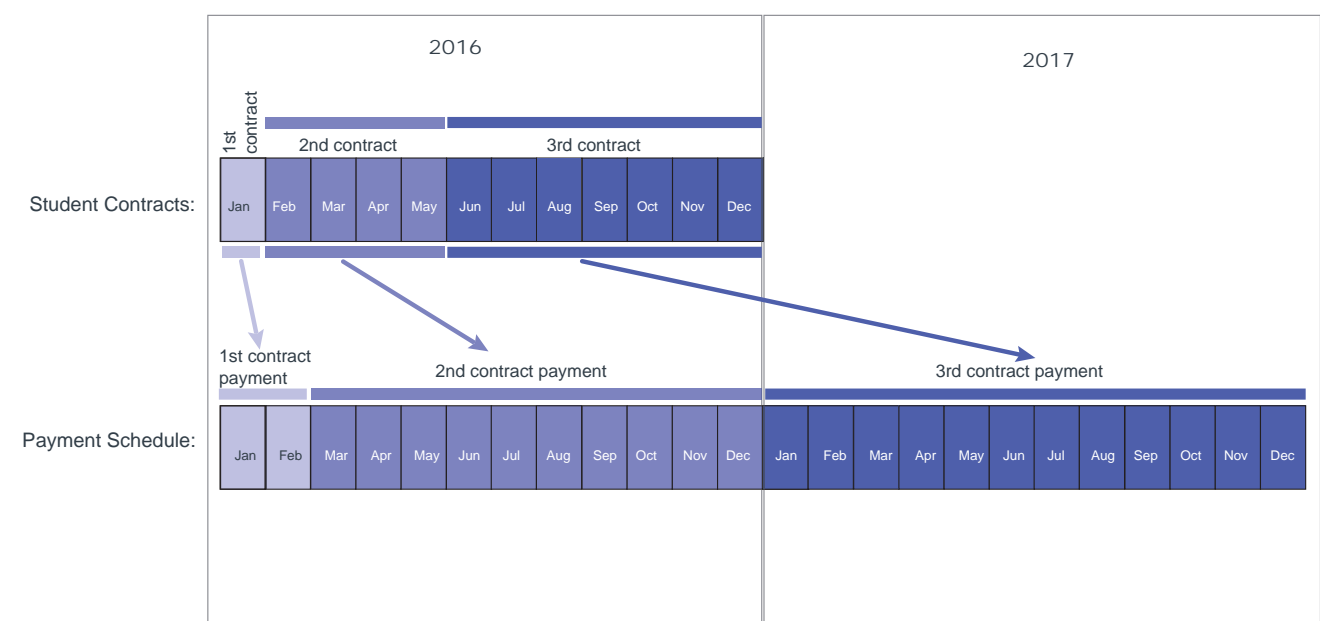
Next, Ideal works to ensure that the incentives are aligned for students and universities. Ideal found that students were dropping out at the first sign of difficulty, partly because they did not enroll in their first choice program. Now that students can afford to pay for their preferred degree, the drop-out rate has decreased.

In an effort to bring greater transparency and to help students make informed decisions, when evaluating different institutions, Ideal provides students with a tool on their website that compares tuition costs of similar programs at different universities.⁷ In addition, since universities offer different PRAVALER products, with Ideal’s loan simulator, students can run different cost scenarios and evaluate how tuition at each institution would fit into their budget. This allows students to pick the best program for their situation.

Once a student enrolls at a university, the student will actually sign a package of two student loan contracts: the first one corresponds to the first month’s tuition. The student will have 2 months to repay this loan. The second contract is for the balance of the tuition for the semester. This set-up allows Ideal to detect any potential problems very early on in the process. If the student defaults on the first contract, Ideal automatically cancels the second one. With longer repayment terms, a student will have between 2 and 2.5 times the length of study to repay the loan. (See Figure 1)

⁷ Please see Ideal Invest’s website: <http://www.credituniversitario.com.br/>

FIGURE 1: EXAMPLE OF STUDENT CONTRACTS AND PAYMENT SCHEDULE
SOURCE: Ideal Invest





Ideal has partnership agreements with about 475 institutions. São Judas Tadeu University (above) is one of them.

For universities, the partnership with Ideal improves their overall financial performance. Ideal helps institutions to increase in-take levels, thereby generating more revenues. Universities have fewer empty seats and can fill courses more easily because the students can now afford a degree. Since students enroll in the program that is their first choice, they are more motivated and are less likely to give up. This decreases the number of students who drop out and makes the cash flow more stable for the institution.

In Brazil, students will typically pay the university tuition on a monthly basis but with PRAVALER, Ideal Invest will advance the cost of tuition for the entire 6 months to the university. The product shifts all of the risk that a student will default from the university to Ideal. This improves the financial position of the institution since it collects a larger sum of its working capital in bulk at the beginning of the semester. With volume, the institution can enjoy greater stability and predictability to facilitate planning. It can allow the university to strategically manage investments and growth.

THE NEXT GENERATION OF PRAVALER

Given the positive experience with PRAVALER, some universities wanted to extend the program to students who who could not get a traditional student loan from Ideal. Universities agreed to accept the risk and put up their own capital to help more students. Today, Ideal has three product lines, which are distinguished by the source of capital:

“PRAVALER ANTECIPAÇÃO” indicates the capital is fronted by Ideal Invest.

“PRAVALER GESTÃO” leverages 100 percent of the university’s own capital. It was introduced in September 2015. In this scenario, rather than advancing 6 months of tuition to the university, Ideal acts as a pass through, and only administers the loan. It transfers each monthly payment to the university as soon as the student makes the payment. For this product line, Ideal sells the university their expertise in managing the student loan program, analyzes the student’s probability of default, markets the loans to the students and collects the payments. If a student defaults, Ideal will attempt to collect the debt for 6 months and thereafter the university bears the loss. At the end of the day, Ideal only receives their commission if the student pays. Thus, even though this product is funded by the university’s capital, the incentives remain aligned in the process of selecting students that have the capacity to pay.

“PRAVALER COMPARTILHADO” where the risk is shared between Ideal Invest and the partner institution. For the first half of program, the capital is fronted by Ideal Invest and for the second half, by university.

The major difference between the product lines is on the back-end of the product—specifically, the source of capital and the acceptable levels of risk. The student does not perceive any difference between the product lines because Ideal offers the same products to students for all product lines. Students also undergo the same screening process.

In April 2015, Ideal began to offer five different student loan products marketed under the “PRAVALER” brand: “Sem Juros” (Zero Interest), “Simples” (Simple), “Mais” (More), “Fácil” (Easy), and “Controle” (Controlled). Three out of five products have a lower monthly payment on the first loan contract and are followed by a step-up feature that marginally increases the interest and the amount of tuition paid by about 10 to 15 percent per month.

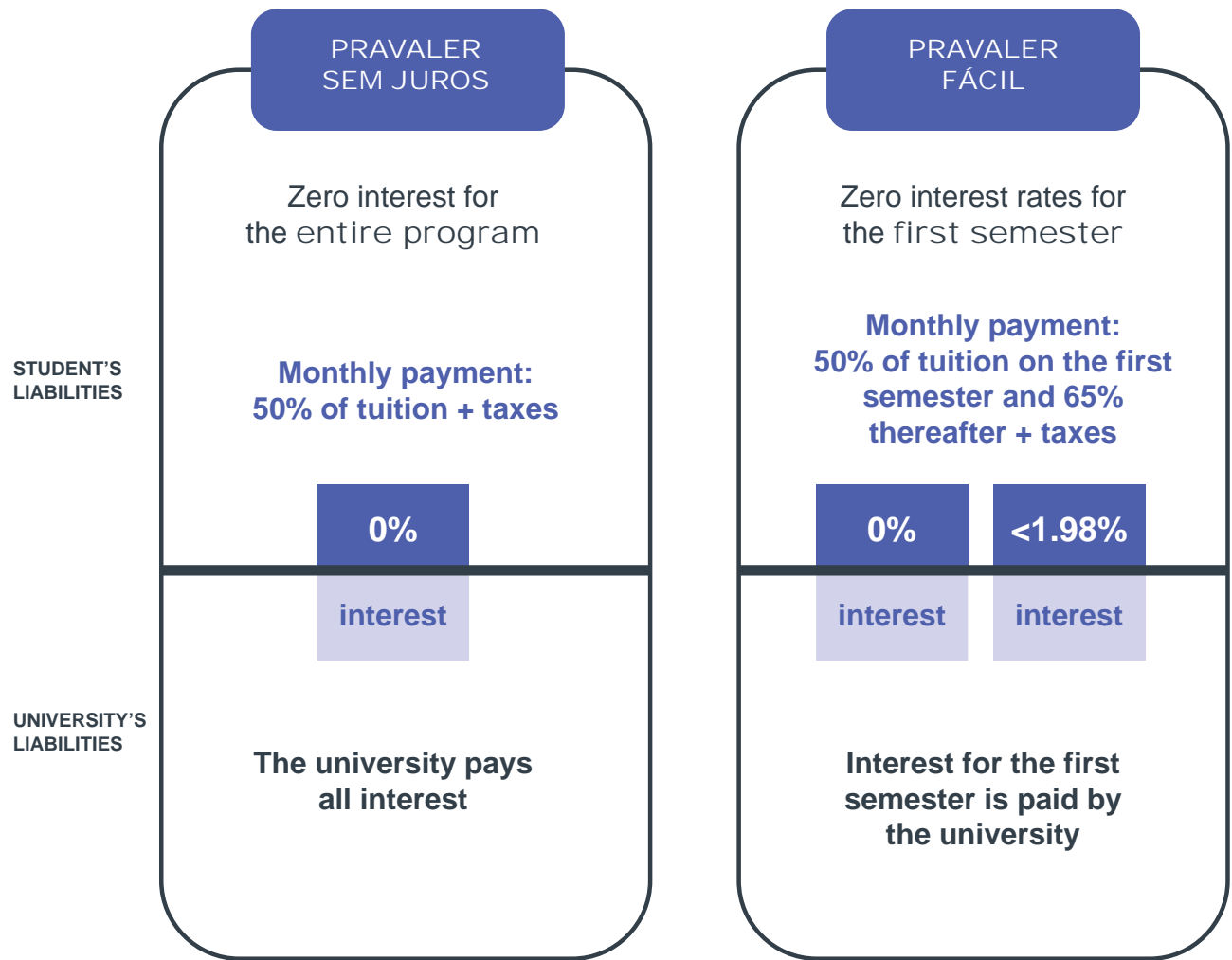
Each product offers a variable mix of cost sharing on the interest rate. At the end of the day, the Annual Percentage Rate (APR) is shared between the student and the university on a sliding scale. For instance, if the total APR is 30 percent, the university will pay part and the student will pay the balance. Ideal negotiates with each institution the amount of interest that the university will pay. The final figure is based on a risk analysis of the university and the historical repayment behavior of the students in the existing portfolio at that institution.

In operational terms, when Ideal transfers the tuition funds to the university, it deducts the appropriate amount of interest, as well as Ideal Invest’s commission fee. The university receives the balance. In effect, the interest that the university subsidizes becomes a discount on the cost of tuition that the student pays.

Since the university has a stake in the associated costs, the university determines which PRAVALER product it will offer its students. Universities will offer the product that they believe has the best value for money in terms of cost and attractiveness to students. In general, universities will make available only one PRAVALER product.

PRAVALER “Sem Juros” is the most popular product in Ideal’s portfolio because it offers zero interest to the student for the entire life of the loan for that contract period, resulting in substantial savings for the student. It is also renewable in subsequent semesters if the student maintains a good repayment performance. Similarly, PRAVALER “Fácil,” the second most popular program in Ideal’s portfolio, offers the introductory zero interest program for the first semester, but then the interest increases in subsequent semesters. The cost sharing arrangement between the student and the university is still available, but at a higher interest rate for the student and a lower interest rate for the university. (*See Figure 2*)

FIGURE 2: THE TOP TWO MOST POPULAR PRAVALER PRODUCTS
SOURCE: Ideal Invest



Students pay a few additional costs associated with the loan, such as inflation and taxes. For 2016, inflation is estimated to be 7 percent and the student pays this to Ideal given the current inflationary environment. In addition, in Brazil, many financial operations including loans are taxed and students are required to pay the “Imposto sobre operações financeiras,” (IOF), which is a tax on credit transfers. It varies between 1.5 percent and 3 percent per year. In contrast, students who take out FIES loans do not pay any taxes.

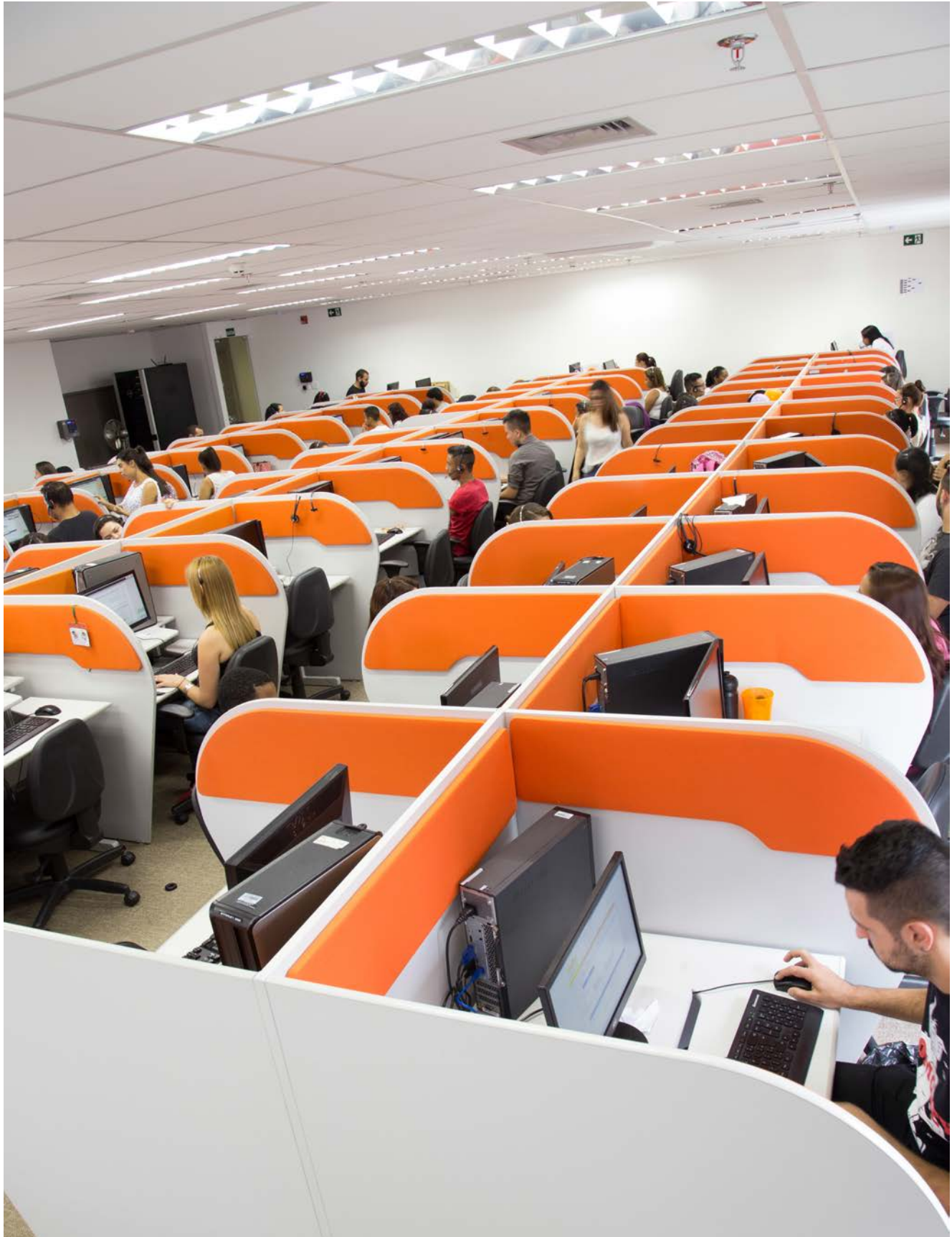


Photo © Ideal Invest

Ideal's corporate structure allows the company to have full control over the process of funding and servicing of its student loan portfolio.

A CHALLENGING MARKET: HOW THE BUSINESS MODEL POSITIONED THE COMPANY

Ideal's mission is to be recognized as the best financial solutions company that enables access to education for youth and adults in Brazil, while being an essential partner with educational institutions, and generating economic value for all stakeholders. To accomplish these goals, Ideal needed to design a funding mechanism that would allow it to raise capital and issue student loans. The cost of capital in Brazil is very high, with an average base rate of 15.7 percent between 1999 and 2015. This made it very challenging for the company to create loans that promoted access and were financially sustainable for the student. With Oliver's background in investment banking, Ideal devised a strategy to raise capital by issuing market-backed securities. This played a role in the legal organization of the company.

It was not easy to establish the corporate structure because there was no model to follow in Brazil. Ideal was the first non-bank, private company to enter into the student-loan market. Ideal did not want to become a bank because it wanted to focus exclusively on promoting access to higher education. While becoming a bank would have opened the door to offering more financial products, it would have also gone beyond their objective, and been more complex and costly. In the end, it would have proved to be more expensive for the student, thus Ideal's management chose a simpler corporate structure.

Ideal Invest decided to organize itself as a banking correspondent and an asset manager that is allowed to originate and actively manage its portfolio of student loans. Ideal's corporate structure is often used in Brazil by specialized credit providers and allows the company to have full control over the process of funding and servicing of its student loan portfolio. As a consequence, it is regulated by both the Central Bank and the "Comissão de Valores Mobiliários," the Brazilian equivalent of the United States Securities Exchange Commission.

When Ideal was starting, there was a new law in Brazil that allowed asset managers to run receivables funds. Ideal became one of the first companies to operate a receivables fund. Shortly before the company started the student loan part of the business, a regulation was introduced that allowed a banking correspondent company to represent a bank in any banking product, including identifying prospects for loan origination by a bank, without becoming a bank itself. Today, Ideal assists the student with the contract process and the bank originates the student loan. Simultaneously, the bank sells the student loan to Ideal's special purpose vehicle (SPV), the "Fundo de Investimentos em Direitos Creditórios" (FIDC), or the Fund for Investments in Credit Rights, which is an asset-backed securities vehicle. With the capital Ideal raises



Photo © Clayton Souza / Estadão

Vagner Aparecido
da Costa used
PRAVALER
program as an
alternative to FIES.

through the FIDC in the Brazilian capital markets, the FIDC buys from the Bank the student loans that the bank originated. Through the FIDC, Ideal is able to continue to capitalize and grow the company by securitizing the loans. The FIDC also allows Ideal to actively manage the student loan portfolio that was acquired by the special purpose vehicle, including the servicing and collection of loans.

With the corporate structure in place, it was time to lay strong foundations. Oliver received the following wise advice from a friend: “Instead of thinking like a small company that will one day be big, think of yourself as a large company from the beginning—this will position you for the future.” In 2002, Ideal called Standard and Poors (S&P) and requested a rating. He thought: “Investors may not know our company but they know S&P.” Oliver put 40 percent of the fund proceeds toward the rating because he thought it was important to structure things properly from the outset. Today, Ideal has had a long history with the credit ratings and the experience taught them a lot. Ideal’s last credit rating was brAA- in December 2015, which is at the top end of the scale.

In terms of revenues, Ideal draws income from three sources: (1) the PRAVALER loans and commission fees, (2) capital gains on the FIDC special purpose vehicle and (3) the services it provides to the universities. In many respects, Ideal acts as an outsourced financial aid office to the universities by providing expertise in managing the student loan program, analyzing the student’s probability of default, and collecting debts.

Ideal manages its entire operation from its office in Sao Paulo. The asset light nature of its business allows Ideal to be very strategic with its staffing and marketing expenses allowing the company to invest more heavily in cultivating and training its employees. They have a total staff of about 200 full-time employees that includes 10 regional managers and a sales force of about 30 sales people. Sales representatives rotate around university campuses. By leveraging its network of university partners, Ideal can contain staffing costs, while still marketing PRAVALER to over 500 different cities across Brazil.



Photo © Ideal Invest

Ideal hires seasonal workers to reach out and talk to students and explain how they can pay for their studies with PRAVALER.

Ideal hires seasonal workers to reach out and talk to students and explain how they can pay for their studies with PRAVALER. This happens during key periods, such as the day that students take the “Exame Nacional do Ensino Médio” (ENEM), the entrance exam for most universities, and during university enrollment days during the winter and summer intake cycles. Ideal uses a call center to help students complete the application process. The call center will reach out to a student that did not complete the application process, will answer questions and help the student with the process.

Ideal invests in training and monitoring of its staff to make sure they are comfortable answering a range of questions that might arise from students. Oliver and Carlos knew that most people would not actually read the provisions of the loan agreement in detail so they wanted to be sure that Ideal was explicit in explaining the terms in a visible and simple way. Customer service consultants on the ground have the tools they need to be able to clearly explain the details of contracting a student loan and Ideal provides some relevant counseling to students prior to signing the loan. Finally, Ideal leverages technology to streamline the sign-up processes and cut costs. The entire loan application process is done on-line.

In terms of competition, over the last 15 years, the student loan sector in Brazil has been very challenging and Ideal’s main competitor has been the Brazilian government. In the 1990s, the federal government realized that given the size of the market, it could not afford to effectively expand the free public university system that was in place. The government decided that it was more cost effective to promote the growth of the private tertiary education market. Between 1996 and 2004, private sector education grew by 152 percent, but it was experiencing several challenges, including high dropout rates and vacant seats. The Brazilian government intervened by increasing public demand-side funding for higher education, which was distributed via several public policies.⁸ Beginning in 1999, it began to channel federal government resources through PROUNI, the government scholarship program, and FIES.

When Ideal moved into the student lending market with PRAVALER in 2006, there was limited competition in the market. That started to change slowly in 2007 when the government released its newest plan, the “Plano de Desenvolvimento da Educação,” or the Education Development Plan. This effort was intended to bolster its education policy and ramp up accessibility. By year end, FIES had grown to about 50,000 contracts that

Sales representatives rotate around university campuses to reach out and talk to students and explain how they can pay for their studies with PRAVALER.



Photo © Ideal Invest

⁸ Danilo de Melo Costa, *A New Era for Higher Education in Brazil*, *University World News*, July 11, 2014. Issue No.: 328. <http://www.universityworldnews.com/article.php?story=20140710115554910>

Ideal moved into the student lending market with PRAVALER in 2006.



required co-signers. Through these efforts, FIES helped to cultivate a culture of funding higher education in Brazil that was previously non-existent.

It was in 2009 that Ideal realized how big the untapped market was. In January, Ideal received 20,000 applications, and that was just the beginning; the demand continued to grow. To fund all of them, Ideal would need about R\$1 billion (US\$255 million)—but this was far greater than the capacity they had at the time.

In 2010, the government announced a new National Education Plan and introduced a new structure to accelerate enrollments, including allowing loans without co-signers. The new terms were very attractive to students, who did not have to achieve a minimum score on the ENEM to be eligible at that time. The loans were highly subsidized; they carried an interest rate of 3.4 percent per year and students had an 18-month grace period following graduation to begin repayment. Students had three times the length of the degree program to repay the loans. Institutions also paid a commission fee to the government to help offset some of the costs.

The reforms of 2010 made it very difficult for Ideal to compete head to head with FIES because at that time the annual percentage rate on a PRAVALER loan was 25 percent. The reform opened the flood gates and students flocked to FIES. By the end of 2010, FIES had signed 150,000 new contracts—one hundred thousand more new contracts than it had achieved three years earlier. The competition was fierce and Ideal suffered a few years of losses.

As FIES was growing exponentially, Ideal was of the view that the rapid pace of growth of FIES was unsustainable. They used the time to transition to a new CEO, develop the next generation of PRAVALER, and prepare to scale up. In 2013, Oliver decided that it was a good time to implement succession plans. Oliver became Chairman of the Board and Carlos Furlan, who had been at the company since 2003, was tapped to become the new CEO. The company implemented its strategic plan and made a variety of improvements. It reduced the cost of capital, maximized the use of capital, streamlined products, provided training to more staff, diversified marketing strategies, and enhanced scalability. These improvements helped them to become more efficient and profitable.

Meanwhile, the Brazilian government continued with its expansion strategy and invested R\$13 billion (US\$3.3 billion) in student loans in 2014. Notwithstanding the cost, it was cheaper for the government, by about 50 percent, to finance student loans, rather than funding additional supply of seats in the public education system. By 2014, FIES was offering 732,200 new contracts per year, representing 26 percent of enrolled students and it had an existing portfolio of 1.9 million contracts. But that pace of growth was not sustainable given the economic contraction that began at the end of 2014. As part of the government effort to control the large fiscal deficit, several cost cutting measures in different sectors of the economy were introduced. In December 2014, the government made a surprising announcement that it was scaling down the number of new FIES contracts per year, starting in January 2015. That year it issued about 300,000 contracts.



Photo © Agência Brasil, Public Brazilian News Agency

Brazilian students taking the National Secondary Education Examination (ENEM) must now score a minimum of 450 to be eligible for FIES

Shortly after this change, several university presidents started to call Carlos directly on his mobile phone, eager to do business. Finally, the tables were turning back for Ideal and they were ready. In 2015, all the universities started offering the subsidized PRAVALER loans, including all of the listed education companies in Brazil. By March 2015, the number of students Ideal approved was 5 times higher than in the same period in 2014.

For the second semester of 2015, the Ministry of Education continued to scale back the program and introduced several key changes. Students now need a minimum score of 450 on the ENEM to qualify. Students household's income must be up to 2.5 times the minimum wage per month. There is a formula to calculate how much tuition can be financed. The interest rate increased from 3.4 percent to 6.5 percent per year. Students must make minimum payments of R\$150 (US\$40) per quarter while in school and during the 18 month grace period, although depending on the tuition price and the amount financed this payment can be increased. It is interesting to note some of the changes that the Ministry of Education introduced share some similarities with the PRAVALER product, such as the requirement to make some payments while in school.

Notwithstanding the growth Ideal is currently experiencing as a result of the change in government policy, Ideal recognizes that policies are designed to respond to different public necessities and it is quite difficult for a small, private company to be in a position to provide a comparable level of response to public needs. As such, Ideal believes that in the long term Ideal should be considered as a company that provides an alternative benefit to students, rather than as a direct competitor to FIES.

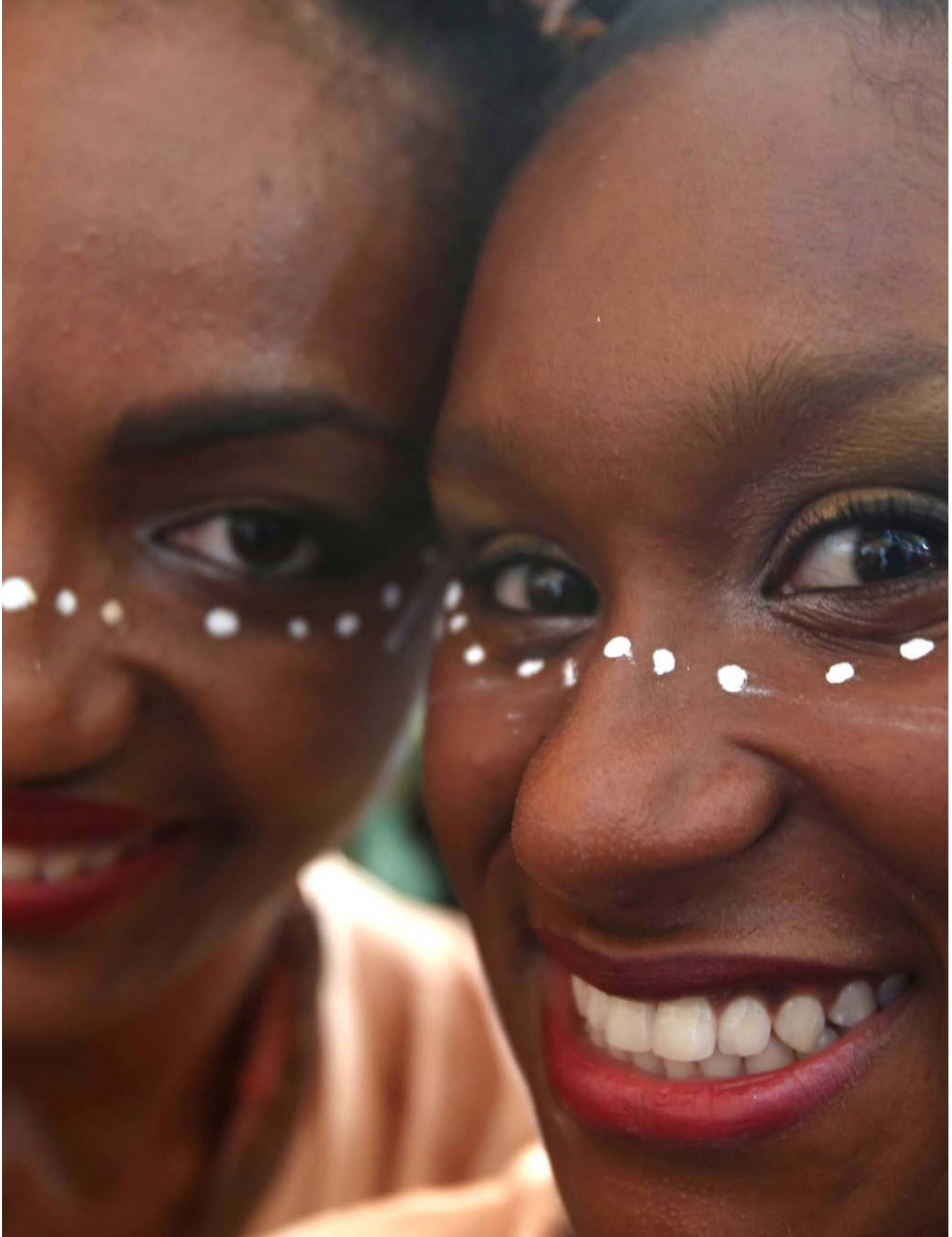


Photo © The World Bank

Seventy percent of Ideal Invest's borrowers are first generation college students in their families.

THE ROLE OF IFC

In 2004, demand for student loans exceeded Oliver's seed funds and he began raising capital with family, friends, angel investors and Brazilian private equity firms. It was around this time that Ideal began talking and sharing information with IFC, but several rounds of intermittent, periodic conversations were needed until the timing was ripe in 2007.

Negotiations were originally for a loan, but it was strategically important for Ideal to continue to fund its securitization vehicle. Further, at the time, IFC loans were not available in local currency—they were only in U.S. dollars and that was not attractive for the company. Equity was attractive because Ideal had a US\$7 million convertible debenture it had to pay back. In 2009, in the midst of the global financial crisis, Ideal “passed all of IFC’s exams” and in November, the deal was closed with IFC taking an R\$12 million, approximately US\$7 million at the time, equity stake in the company. IFC’s equity investment was timely and played a catalytic role in Ideal’s ability to raise more capital. Between 2009 and 2010 Ideal raised an additional R\$45 million (US\$11 million).

IFC was interested in doing business with Ideal because improving access to finance for students who could not afford the cost of post-secondary education on an out-of-pocket basis was squarely aligned with IFC’s Education strategy. It was also one of the World Bank’s main strategic goals for the country as outlined in the Country Assistance Strategy for Brazil that was in effect in 2007.

IFC was interested in the development impact the project could have. If successful, Ideal would expand equitable access to tertiary education for students looking for flexible and affordable funding alternatives. At the time of the investment, 60 percent of Ideal’s borrowers were first generation college students in their families; it has grown to 70 percent at present. In addition, Ideal would make tuition flows more predictable for participating universities and help reduce drop-out rates. Since Ideal was pioneering market-backed securities to raise capital for education loans, they could have a demonstration effect if successful. Finally, IFC would support the growth of an innovative local entrepreneur who was servicing unmet demand with a sustainable business model.

Ideal was interested in doing business with IFC because IFC would come in with an equity investment at a time when it really made a difference. IFC was the first investor outside Brazil to take an equity stake in the company. IFC’s investment in Ideal was a critical endorsement by a well-known global brand. Carlos mused: “With all of IFC’s due diligence, IFC still decided to invest—it was an important step for us.” Ideal passed the



Photo © Plato Training Center, Turkey

IFC brought a broader perspective to help Ideal understand best practices and developments in the sector elsewhere in the world.

test. This was very important to be able to attract other investors and it helped to reduce the cost of capital.

IFC also brought a broader perspective to help Ideal understand best practices and developments in the sector in other parts of the world. Svava Bjarnason, the Senior Education Specialist, provided an example in the United States where she showed the negative effect of not having guarantors on the student loan portfolio. That cemented Ideal's decision to keep co-signers for the life of the loan. IFC facilitated a visit with "Compartamos," in Mexico, where Ideal gained useful insights. Ideal was also able to increase their network with student loan companies across the globe including EduLoan in South Africa, and Lumni in Chile. Carlos reflected: "It was wonderful because IFC was bringing international knowledge to us!"

THE FUTURE FOR IDEAL

In the next five years, Ideal wants to position itself as a midsize company and it is currently raising R\$200 million (US\$51 million) in capital to continue to scale growth. Today, Ideal finances about one-third of the demand it receives through PRAVALER and it would like to expand its reach further by implementing its strategic plan.

First, Ideal wants to reach more students by broadening the types of products it offers to students. It also wants to find more ways to make student loans more affordable for students.

Second, Ideal sees an opportunity to expand the number of universities that are partners. With about 2,000 institutions in the market and an overall market penetration of about 25 percent there are many opportunities for expansion. The company also wants to expand the PRAVALER product lines so that more students can finance their education.

Third, Ideal wants to improve the student experience by expanding its role of "outsourced financial aid office." It wants to have more engagement with students and ensure that students have the best experience possible. It also plans to expand its university dashboard display that compares costs across different institutions. To reach its target audience, it will ramp up its marketing through several channels such as Facebook, Google, and prime time television.

Finally, to meet their expansion objectives, Ideal will continue to invest in cultivating its team so that they have the right talent in place to meet the challenges of the future and position themselves for a possible international expansion.

Seventy percent of Ideal's students are the first in their family to obtain degrees and 55 percent of students are women.

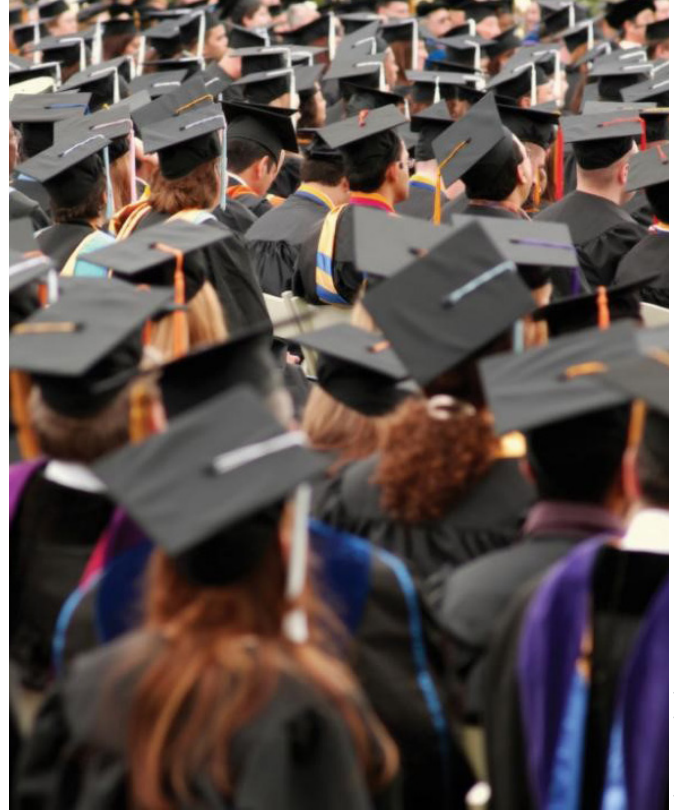


Photo © Ideal Invest

Today, Ideal finances about one-third of the demand it receives.



Photo © Ideal Invest

Ideal wants to have more engagement with students and ensure that students have the best possible experience.



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REPLICABILITY IN OTHER MARKETS

Affordability is an important barrier inhibiting access for students in many emerging markets. How can others replicate the success of Ideal Invest, such that student loans can help students afford tuition and help get the degree of their dreams? The Ideal Invest experience would suggest the following broader lessons:

Mission

- *Stick to your mission of enabling affordable access to education for students, being essential to educational institution partners, and generating economic value for all stakeholders.*
- *Have a long-term vision.*
- *Do not try to solve every problem in your country.*

Leadership

- *Ensure that top management has “skin in the game,” investing their own wealth in the company. This will drive smarter decisions.*
- *Make sure the incentives are aligned for all stakeholders.*
- *Think like a big company, even when you are still small.*
- *Be in the business of saying “no.” You do not have to provide a loan to everyone.*
- *Ensure that management has “street smarts.” There is a lot of fraud.*

Partnerships

- *University partnerships are critical to expanding access to student loans for thousands of students.*
 1. *By subsidizing the interest on the loan, universities have helped make the product affordable.*
 2. *For PRAVALER GESTÃO, universities put their own capital on the line to help reach more students. They take all the risk of default.*
 3. *For PRAVALER COMPARTILHADO, universities and Ideal both share the risk of default.*
- *Align incentives for partners and ensure that there is financial sustainability for all partners.*
- *Partners have been present at every step of the journey. Recognize they are the enablers and Ideal would not exist without partners.*

Talent Management

- *Succession planning. Cultivate the next generation of leadership by preparing the management bench with strong candidates.*
 - *Invest in staff and ensure you have a good team to get you through the long term.*
 - *Recruit staff that share the same values.*
-

Corporate Culture

- Six values to instill in every employee:
 1. *Work like an owner.* We work with autonomy and proactivity, positioning ourselves clearly and taking responsibility for the consequences. We invest time looking for solutions.
 2. *Honesty and transparency.* We act with honesty and integrity, treating people with respect, in an open and transparent environment. We don't hide things in footnotes. We are honest and up front with borrowers.
 3. *Work for the client.* We work with humility and respect to exceed the expectations of our clients: universities, students and investors. It is important to stay connected to the student's situation. For instance, in the portfolio review, Ideal detected that some students were going to run into financial difficulty in the future. They called each student and restructured their loans, granting more time and a lower interest rate before it went into non-performing status.
 4. *Bring results.* We deliver challenging targets consistently, even though we do not control all components, acting with a sense of urgency and improving productivity.
 5. *Award staff by meritocracy.* We attract, retain, develop and recognize the best people based on performance and alignment of culture and values.
 6. *Keep it simple.* We respond quickly and objectively to opportunities and changes, and innovate with simple processes. For example, we know that most borrowers will not read the terms of the contract, so we give more information up front, early in the process. We make sure the incentives are explained at the beginning. We explain how things will work clearly. You don't want the student to be disappointed because they thought the loan would work in a different way.

Financial Sustainability

- *Make sure you have a responsible lending product.* Stay away from easy money. The cheapest loan may help gain market share, but that is irrelevant if there is no company to continue into the future.
- *Attract the right clients.* Develop an in-depth understanding of student repayment behavior and the characteristics of different students. Know who will pay and who will not. Analyze risk through a specialized credit scoring system.
- *Ensure that students make payments monthly, even if it is small.* It is an indication that they are not out of money.
- *Manage growth sustainably.* It is okay to lose market share. Do not compromise the financial health of the company.
- *Be disciplined.* Ideal grew at a pace of about 15 to 20 percent over eight years. Play it safe, or demand will accelerate growth down a slippery slope without any oversight.

Governance Structure

- *Have an effective governance structure; not just one that will check all the compliance boxes.*
 - *Bear in mind that the Board is not well positioned to detect many problems.* Management needs to constantly anticipate the next problem.
 - *Do not award seats on the board to every investor to thank them for their financial support.* Rearrange the Board when things are not working.
 - *Ensure people can speak freely.*
 - *Rotate the audit committee periodically.* Bring two people in from outside and change them every two years.
-

Enabling Environment

- *It is not necessary to become a financial institution. It is too expensive and would increase the cost of commission for students and universities.*
 - *Consider raising capital in the markets.*
 - *Lobby the government to cover the first loss up to a specified level. If the government would take 10 percent of the first loss, Ideal's money would go a lot further because it would lower operational costs.*
 - *Lobby the government for equalizing rules.*
 1. *In the public student loan market students do not pay no taxes. Meanwhile, students in the private student loan market must pay the IOF tax, which charges interest between 1.5 percent and 3 percent per year.*
 2. *Investors pay 15 percent of income taxes on the FIDC special purpose vehicle, yet for mortgages, investors do not pay the equivalent tax.*
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Photo © IThe World Bank

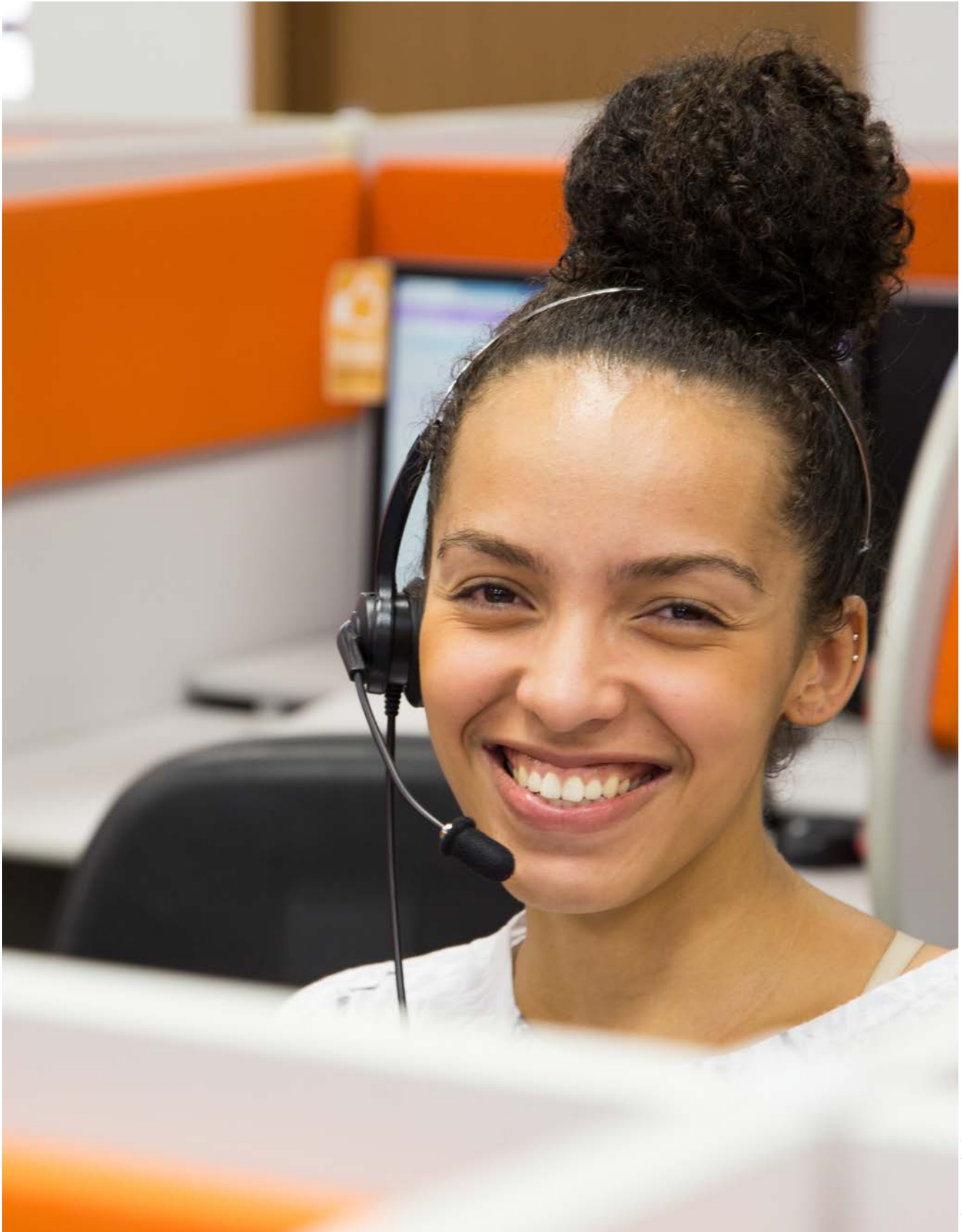


Photo © Ideal Invest

Ideal Invest proved that a small, private company can successfully create a sustainable business in the student loan industry, without becoming a bank.

CONCLUSION

Through Oliver and Carlos' creativity, entrepreneurial spirit, and steadfast commitment to help students and their families afford a university education, thousands of Brazilian students like Camila are pursuing the degree of their dreams. Young Brazilians will have better employment prospects after graduation and will be better positioned to increase their earning capacity. Ideal Invest has played a catalytic role in breaking the generational barriers that perpetuate the cycle of poverty for students and their children.

Ideal Invest proved that a small, private company can successfully create a sustainable business in the student loan industry, without becoming a bank. Through their efforts, Ideal Invest has become the largest source of private student lending in Brazil. By grounding decisions on sustainability and adopting a responsible lending philosophy, the company has positioned itself for the long term. By aligning the incentives and expanding their reach through partnerships, Ideal has helped institutions improve their cash flows, fill empty seats, and reduce the drop-out rate. With a larger number of students who are benefiting from tertiary education, the Brazilian work force is benefiting from better prepared individuals who will continue to improve the economic competitiveness of the nation.

QUESTIONS FOR DISCUSSION

1. In the United States, the government takes the first risk of loss up to about 10 percent. This acts as a financial incentive to entice private sector players to offer loans to more students. Ideal has approached the Brazilian government with a similar proposal, which would allow Ideal to reach a greater number of students, but the concept has not gained much traction. What other approaches could Ideal adopt to minimize the risk of default?
2. Ideal devised the FIDC special purpose vehicle to raise capital through asset-backed securities. How else can companies set up capitalization mechanisms that are cost effective, without government subsidies? Could crowd sourcing prove to be an effective revenue stream?
3. As a banking correspondent and an asset manager, Ideal must comply with two regulators that have complex compliance requirements that add to operating costs. What other corporate structures exist in your country that would cut operating expenses if they existed in Brazil?
4. By subsidizing the interest rate on the loan, universities end up providing a discount to students. Would it be cost effective for the university to simply provide the discount to the students directly instead of through the loan? Or is a student loan more effective in reaching a greater number of students?
5. Should all students be able to get a student loan? The responsible lending model precludes universal access to student loans. Only the most qualified students have historically been able to get a loan from Ideal, although the threshold is changing with PRAVALER GESTÃO and PRAVALER COMPARTILHADO. How else can Ideal reach the most vulnerable students to increase equitable access and help break the cycle of poverty?
6. How else could Ideal position itself to compete against FIES once the Brazilian economy recovers?

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