1. Country and Sector Background

The Brazilian economy slowed significantly over 2011 and 2012. Real GDP grew at a meager 0.9 percent in 2012 compared to 2.7 percent in 2011. With trend growth estimated at around 4 percent, this growth slowdown represents a major weakening of economic performance. While the slowdown was felt across the board, industrial output and investment demand were affected disproportionately. Recent indicators provide tentative signs of the recovery gathering strength. Quarterly data point to improved investment demand towards end 2012, following four quarters of consecutive contraction.

Belo Horizonte, the capital of the state of Minas Gerais, has a population of 2.4 million dwellers and total land area of only 331.4 km². The city represents only 3.5 percent of the total land area of the metropolitan region. Between 2000 and 2010, BH posted the smallest annual demographic growth rate (0.6 percent) among its neighboring cities, and its rank is declining. This is due to the limited land area and lack of vacant spaces for additional real estate development. BH has a high population density (7,291 inhabitants per square kilometer) and its small land size acts as a barrier to population growth.

Belo Horizonte has a long history of inadequate housing problems. Even before its foundation, the city recorded the existence of favelas. Since the 1980s, BH has pioneered policies to cope with the inadequate housing problem, but more needs to be done. Almost half a million people in BH still live in vilas and favelas, and urban informality has increased from 14 percent in 1991 to the current 21.5 percent. Poverty incidence is unevenly distributed in spatial terms and it is correlated with housing conditions, inequality, access to jobs and gender. The incidence of poverty in favelas is roughly 2.5 times that of those who reside elsewhere.

2. Operation Objectives

---

1In comparison, Rio de Janeiro account for 23 percent of its metropolitan region.
2BH was the 3rd largest city in the country in 1990, the 4th largest in 2000, and is currently the 6th largest.
The objective of the proposed operation is to support integrated and sustainable urban development and reduce social vulnerability in Belo Horizonte. This will be achieved by introducing innovative approaches to address urban planning, environmentally sustainable development, social inclusion and participation and sustainable governance.

3. **Rationale for Bank Involvement**

Development in Belo Horizonte has followed two contrasting paths. On the one hand, economic growth and municipal services have improved, but on the other hand, inequality and informal settlements have increased. The city’s poorest dwellers have suffered from inadequate housing and poor access to basic infrastructure and services. Proactive integrated urban development strategies are urgently needed to address social exclusion, and create effective and long-term sustainable governance to benefit all residents. Recognizing these priorities, Belo Horizonte embraced a hands-on approach by proposing new participatory decision-making mechanisms to foster direct citizen inclusion and ownership of budget allocation, policy decisions, and planning. The municipality also supports state-of-the-art resettlement policies and practices and is spearheading a very innovative approach to reach the most vulnerable families by designing a specific development action plan for each family not currently reached by existing social programs, tailored to its specific need. This operation will reward and support these policies.

The proposed operation is Brazil’s second municipal DPL, and follows the positive experience of the loan to the municipality of Rio de Janeiro. The proposed operation will also benefit from the Bank’s long-standing relationship with the state of Minas Gerais, particularly in the areas of urban and metropolitan governance at municipal and state levels. The operation is fully aligned with the Country Partnership Strategy (CPS), and will create the environment to permit the coordination of policies between the state and municipal governments through an integrated development approach.

4. **Tentative Financing**

<table>
<thead>
<tr>
<th>Source:</th>
<th>($m.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Borrower</td>
<td>0</td>
</tr>
<tr>
<td>International Bank for Reconstruction and Development</td>
<td>200</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>200</strong></td>
</tr>
</tbody>
</table>

5. **Institutional and Implementation Arrangements**

The Secretariat of Finance (SMF) will be responsible for the overall implementation of the proposed operation, for reporting on progress, and for coordinating actions. The SMF will be responsible for coordinating activities with other sector departments (urban development, housing, planning, budgetary planning, public sector management, social development, disaster risk management and environment). In this regard, two tasks are essential: (i) providing evidence justifying the disbursement of the loan; and (ii) overseeing and reporting on progress toward completion of conditions, including tracking individual conditions, facilitating the timely completion of the studies and activities required for meeting these conditions, and consolidated reporting on outcome indicators.

6. **Risks and Risk Mitigation**

The operation faces several types of risk, including political and institutional risk related to coordinating Bank interventions with those of other partners (Inter-American Development Bank- IDB, International Finance Corporation- IFC), other municipal programs, reputational risks that could arise in the event of natural disaster if people are not satisfied with Belo Horizonte’s response. There are also environmental
and social risk associated with potential impacts of the policies supported by the operation (including possible resettlement of families living in areas of high risk of landslides and flooding) as part of the government’s housing and disaster risk management strategy, potential implementation risk due to the number of municipal agencies involved in coordinating action and a small risk that the pension reform included in the operation will not be approved or could be questioned late in the process. The risks are being addressed through the close coordination and communication with the municipal government on the implementations plans of related policy reforms and strategies and the review of the municipal environmental and social safeguards system and practices during project preparation to ensure that environmental and social impacts are adequately addressed in the government’s program.

7. Poverty and Social Impacts and Environment Aspects

The policy reforms supported by this operation address key issues and needs related to the city’s historical social and spatial segregation. As such, they are expected to have significant positive social and economic impacts on the most vulnerable population, in particular, the poor living in substandard housing and informal and at-risk settlements (vilas and favelas). These policies and reforms address the main social vulnerabilities of Belo Horizonte, which are linked to access to services, land and economic opportunities, social and spatial inequality, dense urbanization, and settlement in environmentally sensitive and at risk areas. Historically, social services provided by the municipality have not reached the most vulnerable families, who have also been unable to participate in the city’s decision-making processes.

The provisions of OP 8.60 on Development Policy apply to the Belo Horizonte Urban DPL. The policies and reforms supported by this operation are of great relevance to improving overall environmental management in the municipality of Belo Horizonte. It is expected that the operation will produce net positive environmental impacts in the municipality and the metropolitan region. Environmental challenges in BH are the result of rapid urbanization rates, long-term unplanned occupation, and lack of adequate infrastructure and monitoring.

8. Contact point

World Bank
Contact: Alessandra Campanaro
Title: Infrastructure Finance Specialist
Tel: (202) 473-7526
Email: acampanaro@worldbank.org

Borrower
Contact: Marcelo Piancastelli
Title: Municipal Secretary of Finance
Tel: 31-3277-4442
Email: marcelo.piancastelli@pbh.gov.br

9. For more information contact:
The InfoShop
The World Bank
1818 H Street, NW
Washington, D.C. 20433
Telephone: (202) 458-5454
Fax: (202) 522-1500
Web: http://www.worldbank.org/infoshop