COMMENTS ON THE BOOK “BRAZIL: BOOM, BUST AND THE ROAD TO RECOVERY”

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PRAISE FOR “BRAZIL: BOOM, BUST AND THE ROAD TO RECOVERY”

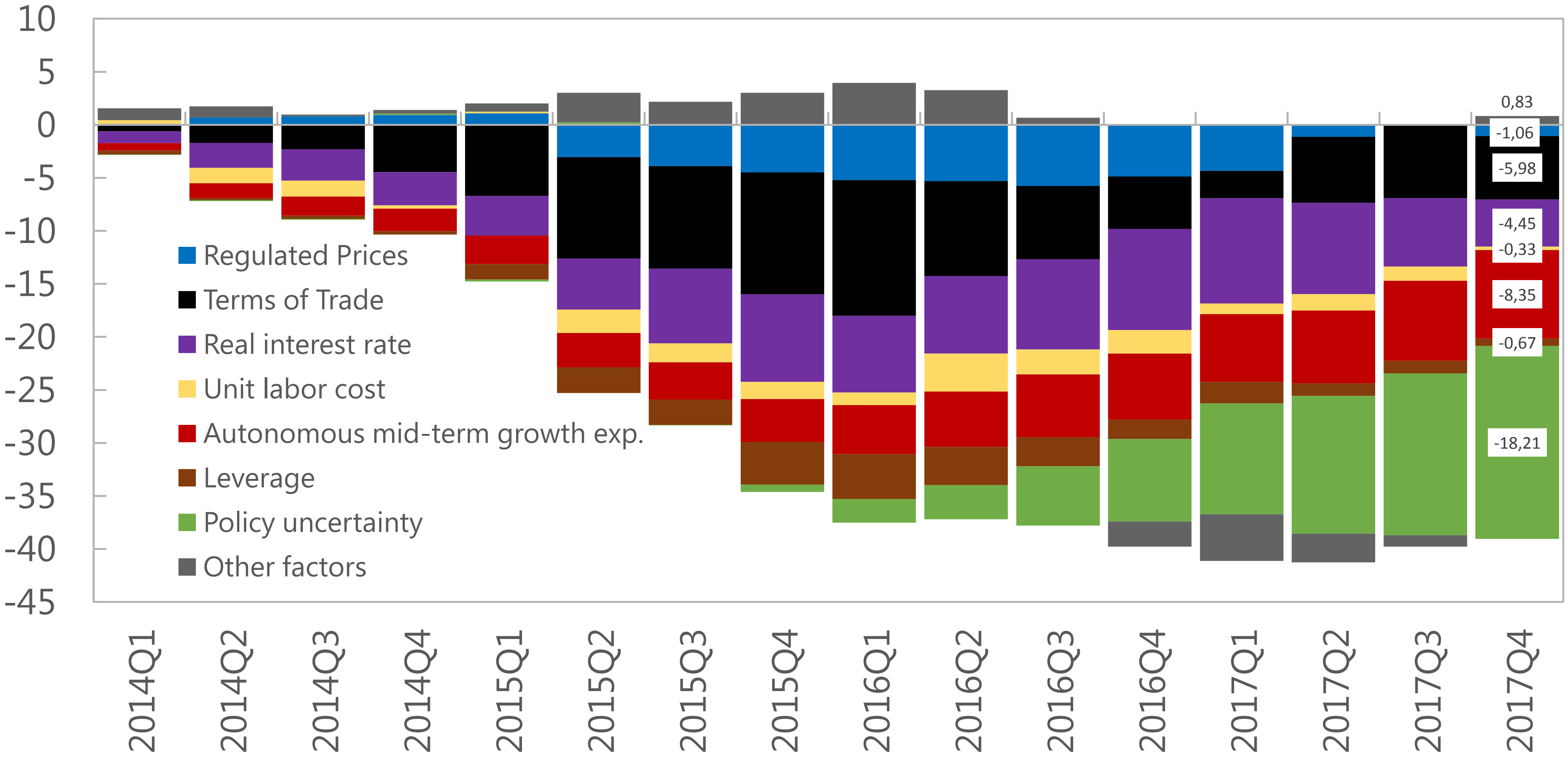
- Timely and important book in many respects
- Provides a rich analysis of Brazil’s economic performance over the past several years, examining policies that worked well and those that have not
- Draws upon and synthetizes extensive work done at the IMF and Brazil from a variety of angles, including growth, social progress, fiscal and monetary frameworks, and corruption
- Should spark healthy debate on the economic challenges facing Brazil’s new government
- I concentrate my comments on Chapter 2 that contains a synthesis of the book’s main theses
- My focus is on the interpretation of the crisis starting in 2014 and on the requisites for an economic recovery in the years ahead

BRAZIL´S RECESSION DRIVER WAS A SHARP CONTRACTION IN INVESTMENT

- Chapter 2’s diagnosis of Brazil’s “worst recession in memory” is clear enough: “The recession key driver was a sharp contraction in investment”
- From its high point in 2013:Q3, GFCF fell dramatically by nearly 26% to 2015:Q4
- GFCF reached bottom in 2016:Q4, with an overall drop of nearly 32% since 2013:Q3
- It has since recovered very moderately by some 6% to 2018:Q4
- At the end of 2018, investment was ¼ lower than in late 2013

Brazil: Decomposition of Gross Fixed Capital Formation Growth

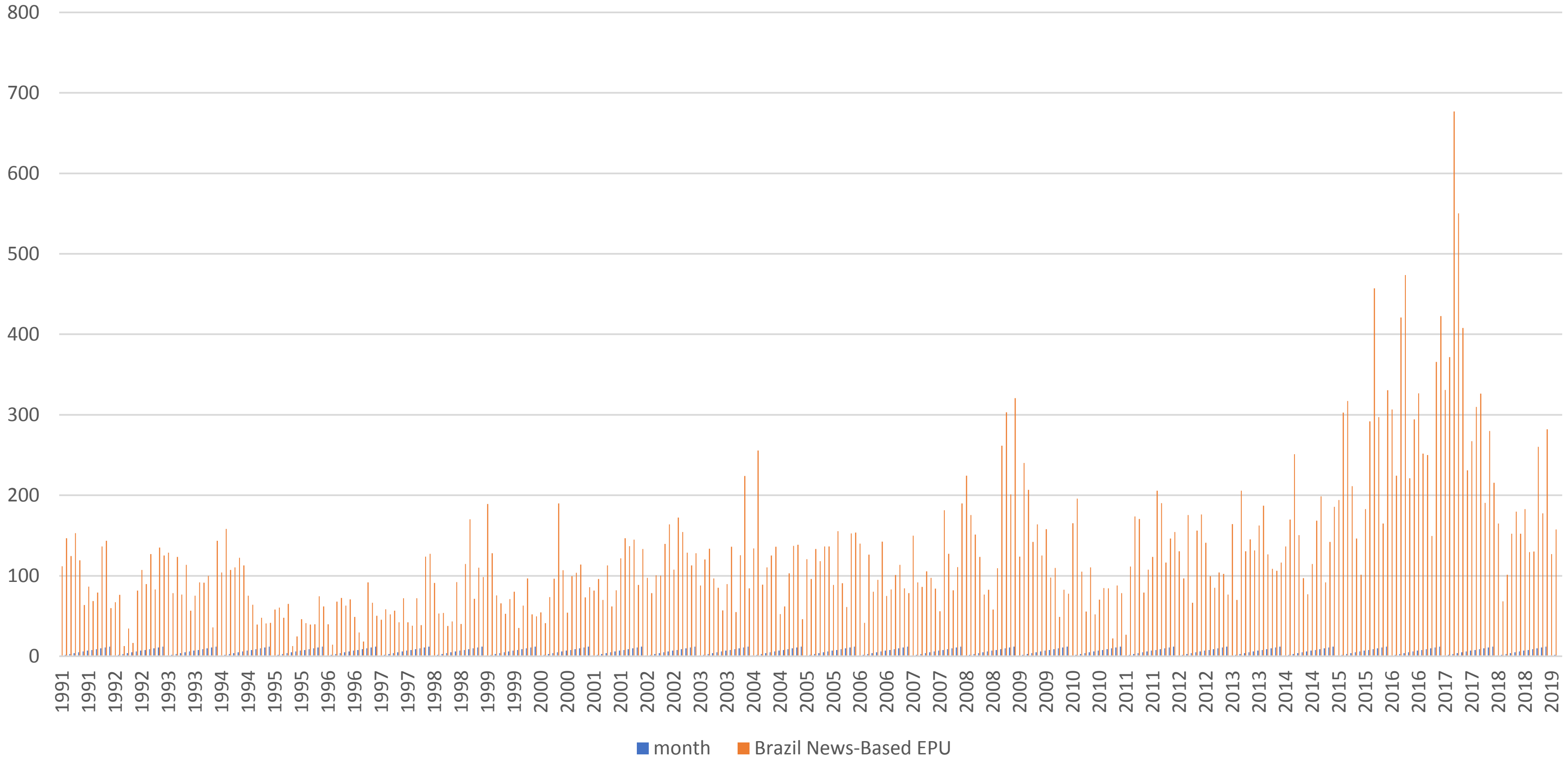
(Quarter-on-quarter growth, deviations from average, acumulated since 2014Q1)



DRIVERS OF INVESTMENT PLUNGE DIFFERED DRAMATICALLY BETWEEN 2014-15 AND 2016-17

- The main drivers of the sharp drop in GFCF from 2013:Q4 to 2015:Q4 were terms of trade deterioration and high real interest rates (plus regulated prices control, high firms' debt (leverage), and low growth expectations)
- The even lower levels of GFCF in 2017:4 were associated to economic policy uncertainty and deteriored growth expectations (plus lower terms of trade and high real interest rates)

Brazil News-Based Economic Policy Uncertainty, 01/1991-02/2019



IMPLICATIONS FOR INVESTMENT RECOVERY

- Taking the book's findings at their face value, the number one priority seems to be reducing economic policy uncertainty and improving growth expectations
- Main driver for both seems to be Legislative approval of an ambitious social security reform
- Little help can be expected from terms of trade (i.e., world economy)
- But perhaps an alternative would be opening up the economy, through a sharp reduction of tariffs on capital goods and critical inputs
- A more accomodative monetary policy would also improve the investment climate

QUESTIONS ON CURRENT MONETARY POLICY

- Should CB have reduced the short-term inflation target as it did (2018, 4.5%; 2019, 4.25%; 2020, 4.0%; 2021, 3.75%) when unemployment is so high?
- “On balance, given the current state of the economy and the need for fiscal prudence for the foreseeable future, there is little merit in lowering the inflation target at this juncture” (p. 34)
- Wouldn´t it have been more reasonable to set a long-term target of 3%, say, for 2026, and be more flexible in the trajectory towards this target?
- Should CB continue to assess the degree of easiness of its monetary policy using as reference an elusive 4.5% neutral rate?
- Or should it instead be prepared to continue easing as long as there is unemployment and inflation expectations are well-behaved?