



# **Comments on Brazil: Boom, Bust and the Road to Recovery**

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# Overview of the book

- Many interesting contributions from IMF staff, policymakers and academics.
- Divided in five key areas:
  - Growth;
  - Social Progress;
  - Fiscal Framework;
  - Monetary and Financial Frameworks; and
  - Fighting Corruption.
- The choice of areas is very appropriate.
- It is comforting, but nevertheless surprising, that an IMF book about a country does not have a topic about the external sector, the very *raison-d'être* of the Fund.

# Overview of the book

- Chapter 1, by the editors, overviews the book.
- Chapter 2, by the editors + Cuevas and Werner, reviews the last two decades and elaborates on the challenges faced.
- They propose five large areas of reforms:
  - Fixing the unsustainable fiscal position;
  - Opening up the economy;
  - Closing infrastructure gaps;
  - Improving the efficiency of credit allocation;
  - Improving the functioning of the state.
- Their interest start with the end of hyperinflation, with the Plano Real.
- The analysis is very precise, pinpointing the challenges we face.
- I would add two minor points to keep the record straight.

# Overview of the book

- First quibble is about the Real Plan.
- The authors rightfully say: “(...) *the launch of the Plano Real in 1994, a set of measures to stabilize the economy, was a turning point in policymaking in Brazil.*” (page 3)
- Since this is an IMF book, one would like to see some reference explaining why the Fund did not support the Plano Real, at its inception.

# Overview of the book

- The second quibble is about the Bolsa Família.
- The authors rightfully praise the successful CCTP.
- However, they fail to mention that Bolsa Família was created through the unification and enlargement of previous programs: Bolsa Escola, Cadastro Único, Bolsa Alimentação, Auxílio Gás and Fome Zero.
- This continuity between two different administrations, FHC and Lula, is a great feature that should be much encouraged.

# Growth

- Castellar and Lins (Chapter 3) attribute Brazil's poor growth performance to three possible explanations:
  - Failure to complete market-oriented reforms;
  - Adoption of industrial policies focused on protecting inefficient incumbents; and
  - The expansion of policies aimed at favoring small, unproductive firms.
- They propose six major concurrent policies:
  - Fiscal reform;
  - Tax reform;
  - Improvement of business regulations;
  - Privatization;
  - Trade integration/less tariffs; and
  - Competition enhancement.

# Growth

- De Mello, Duarte and Dutz (Chapter 4) show that large increases in productivity can **not** be achieved by the reallocation of the workforce toward more productive sectors.
- This is evidence of that whatever causes inefficiency in the Brazilian economy is pervasive to all sectors: *“Brazil’s productivity problem is not what its firms produce but how they produce it.”* (page 56)
- They emphasize the need of regulatory reforms that promote a more business-friendly environment that spurs innovation, including:
  - Opening up the economy to international trade;
  - Rationalizing past policies intended to promote specific sectors and industries; and
  - Improving the functioning of credit markets.

# Growth

- Biljanovska and Sandri (Chapter 5) undertake a cost-benefit analysis of reforms; which reforms would improve productivity more and would be have the highest public support?
- The conclusion is that to limit state intervention in credit markets would generate the largest productivity gains with the most public support.
- Other recommended reforms are: legal system, openness and labor market.

# Growth

- Estevão Filho and Alcaraz (Chapter 6) advocate opening up the closed Brazilian economy, via:
  - Unilateral import tariffs reductions, especially on IT and K goods;
  - Elimination of local content rules; and
  - Deeper trade agreements with more and larger trade partners.
- Góes, Messa, Pio, Leoni and Montes (Chapter 7) use a CGE model to gauge the effects of trade liberalization on labor markets.
- They advocate active labor market policies and training programs to mitigate the transition costs.

# Growth

- These five chapters provide a nice set of analyses and proposals of policies to enhance growth and productivity.
- For my taste, I would like to see a chapter addressing the key issue of inefficient education in Brazil.

# Social Progress

- Góes and Karpowicz (Chapter 8) address the inequality in inequality reduction.
- During the period 2004-14, inequality declined both within and between states, falling more in the more unequal states.
- Strong growth of the incomes of the poor was the main driver of the fall of inequality within states.
- Between states inequality fell because poorer states grew more.
- Big question: what were the effects of the big recession and slow recovery of the last five years?

# Social Progress

- Balakrishnan, Toscani and Vargas (Chapter 9) put Brazilian progress in reducing inequality and poverty in contrast with the social results obtained in other LA countries.
- They show that Brazil follow a usual pattern of commodity exporters in LA: social progress reflects real labor income gains for low-skilled workers and government transfers.
- With the end of the commodity boom, they suggest targeted social transfers, as well as increasing the flexibility of labor markets policies to retool workers and improve education.
- Big question: what were the effects of the big recession and slow recovery of the last five years on inequality and poverty? Next book...

# Fiscal Framework

- Given that Brazil is fiscally-sick—almost all chapters in the book talk about “curing the fiscal malaise” —, this is arguably the most important part of the book.
- It starts with Medas (Chapter 10) giving an overview of our attempts to set a fiscal framework after the end of hyperinflation, and suggesting ways to make it effective.
- The criticisms to the current framework focus on the budgetary rigidity (excessive revenue earmarking and mandatory spending\*), which limits the countercyclical function of fiscal policy and generates a deficit bias.
- He suggests the introduction of medium-term expenditure framework (MTEFs), the modernization of the public financial management framework and the design of new fiscal rules that contains a debt target, including the federal level, unlike now.

# Fiscal Framework

- Cuevas et al. (Chapter 11) tackle the very timely issue of pension reform, estimating the impact of several measures.
- Bornhorst et al. (Chapter 12) address the very important theme of the subnational fiscal crisis.
- Finally, Karpowicz and Soto (Chapter 13) present a comparative analysis of the public-sector wage bill in Brazil, and estimate the fiscal impacts of very harsh measures.
- Taken together, these are probably the most important issues nowadays, and we should debate them at length today.

# Monetary and Financial Framework

- Perrelli and Roache (Chapter 14) use theory and econometrics to try to explain the neutral interest rate in Brazil.
- They find that inflation gaps, financial deepening, public debt and sovereign risk are the main drivers of the neutral rate.
- They also find that public-sector lending, via BNDES, increase the procyclicality of the neutral rate.

# Monetary and Financial Framework

- Matheson (Chapter 15) put (hopefully) the final nail in the coffin of the idea that lower interest rates may lead to lower inflation.
- Unfortunately, the demand for coffins and nails have been increasing, with some new unfortunate ideas showing up recently.
- Byskov (Chapter 16) argues that the massive government intervention in credit markets has not achieved its goals of helping growth, with substantial fiscal costs, while also harming the transmission of monetary policy.

# Monetary and Financial Framework

- Finally, Carrière-Swallow and Yépez (Chapter 17) elaborate a few suggestions on how to improve transparency and communication of the BCB.
- In my opinion, the main missing point in this part of the book is the topic of the very high loan spreads.
- And, since yesterday, when Minister Guedes brought the convertibility of the BRL to the fore, this topic became a must for a subsequent volume.

# Fighting Corruption

- The final section is devoted to fighting corruption and improving governance.
- Gonçalves and Srinivasan (Chapter 18) provide large estimates of the effect of lowering the perceptions of corruption on growth.
- À la Rosenstein-Rodan, they advocate an institutional big-push to uproot corruption.
- Berkhout (Chapter 19) reviews two decades of Brazilian efforts to fight money laundering, terrorism financing and corruption, and elaborates suggestions for further improvement.

# Fighting Corruption

- Two chapters—Pinotti (Chapter 20) and Merli (Chapter 21)—compare the *Lava Jato* with *Mani Pulite*.
- We can only hope that the lessons from history will provide a different outcome for Brazil.
- As the STF is currently voting which justice branch should judge “caixa 2” crimes, these lessons become even more important.

# Conclusion

- Very informative book, with lots of interesting data.
- Thank you for having me here.