

## An impressive list of policy achievements

Jonathan Wheatley

Back in the bad old days around the turn of the century, when Fernando Henrique Cardoso, the former president, was routinely harangued by Workers' party militants with cries of "FHC out, IMF out", the economic agendas of Brazil's government and opposition could hardly have been further apart.

Now, as in so many mature societies, it often seems difficult to slide a white paper between them. Mr Cardoso's policies, until quite recently accused by his successor President Luiz Inácio Lula da Silva of bequeathing the country a "cursed inheritance", are now credited with having laid the basis of Brazil's current stability. Many investors who, on the eve of Mr Lula da Silva's first election victory in 2002, dumped Brazilian assets in panic that he would overspend the country into debt default, now regard his Workers' party administration as the bastion of that same stability.

Few in government or opposition doubt that Brazil owes much of its current prosperity to orthodox economic policies such as a floating exchange rate, inflation targeting and fiscal restraint.

The danger, many observers say, is that now those policies are established and their benefits are being enjoyed, policymakers may regard their job as done. But just as Brazil's prosperity is the result of reforms carried out over the past 15 years, they argue, its future prosperity depends on keeping the reform agenda moving.

"In the current climate of global stagflation, the only way to keep Brazil out of trouble is to address the issues that have been swept under the carpet by this government and the previous one," says Winston Fritsch, a former secretary for economic policy at the finance ministry and now head of investment banking at Lehman Brothers in São Paulo. He says action must be taken on the central issues of tax reform, an overhaul of restrictive labour laws, and cutting government spending.

Yet ministers can counter such arguments with an impressive list of achievements. Guido Mantega, finance minister, says Brazil has made a "qualitative leap", from growth that averaged 1.6 per cent between 1990 and 2003 to an average since then of more than 4 per cent. More importantly, he says, the stop-and-go growth pattern of the past has been replaced by consistency.

Asked if the government still has an agenda of reforms, he points out that spending on payroll is lower as a share of gross domestic product than it was in 2002, the last year of Mr Cardoso's government, and that the deficit in the pensions system, while it rose to the end of 2006, has since fallen back.

Paulo Bernardo, planning minister, says the focus has switched from macroeconomic issues to microeconomic ones. He points to new regulations on credit that have driven a rapid expansion of lending.

Other examples are the recent breaking of the state monopoly on reinsurance to allow private-sector participation, and forthcoming bills to improve the quality of anti-trust regulation. A recent change of environment minister, he says, is likely to speed the process of granting licences to infrastructure projects, one of the main obstacles to investment.

Yet Mr Bernardo admits to concern over a lack of macroeconomic reform. "I am in favour of coming back to pensions reform in the future," he says. The same applies to labour reform and to cutting government spending. The government would like to move forward with the reforms," he says. "But we have to involve the opposition in their formulation. [Cutting spending] is not easy to do, there is still a very strong culture in Brazil of thinking that you need to earmark spending to priority areas like health, education and welfare. But this creates demands for more money. It's true that this is a problem for Brazil's development."

Henrique Meirelles, president of the central bank, says the proposed creation of a sovereign wealth fund demonstrates the government's concern over the impact of public spending on stability. The fund will initially set aside half a percentage point of GDP - about R\$14bn - to be invested in public debt as a counter-cyclical contingency fund. This is the equivalent of increasing the size of the primary budget surplus (before debt payments) from 3.8 to 4.3 per cent of GDP.

Many critics say that, since the surplus is already running at more than 4.5 per cent over the past 12 months, the benefit of the implied cut in public spending will not accrue. Mr Meirelles agrees, but says the increased surplus is still important.

"Yes, the increase has already taken place," he says. "But there was a concern that, if the surplus had gone back to 3.8 per cent by the end of this year, there would have been a big stimulus [to inflation], and that's not going to happen. "He says the central bank is keeping a close watch on the expansion of credit -and on the sharp fall in unemployment, down to 8 per cent from 12 per cent four years ago.

Mr Meirelles was about to enter politics as a member of Mr Cardoso's centrist party, the PSDB, when he was invited to head the central bank from 2003.

The fact that he is still in the job as one of the most determined defenders of orthodox monetary policy after six years of Mr Lula da Silva's administration is as clear a sign as any of Brazil's new policy consensus. Yet he agrees that fiscal policy lags behind monetary policy in creating the conditions for sustained growth. "We would welcome a little more help," he says.

# BRAZIL



## Constitution

Official name  
Federative Republic of Brazil

## Form of state

Federative republic

## The executive

The president, who is elected for a term of four years, chooses a cabinet, which he heads; he holds considerable discretionary powers

## Head of state

Elected president

## National legislature

Bicameral national Congress; 81-seat Senate, comprising the representatives of 26 states, plus the federal district of Brasilia; 513-member directly elected Chamber of Deputies

## Regional legislatures

Each of the 26 states and the district of Brasilia have a legislature and an administration

## Legal system

Each state has its own judicial system; the country has a system of courts for dealing with disputes between states

and matters outside the jurisdiction of state courts

## National elections

Municipal elections every four years, with the next ones due in October 2010

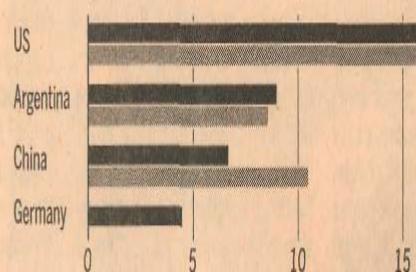
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## National government

Luiz Inácio Lula da Silva took office for a second term on January 1 2007

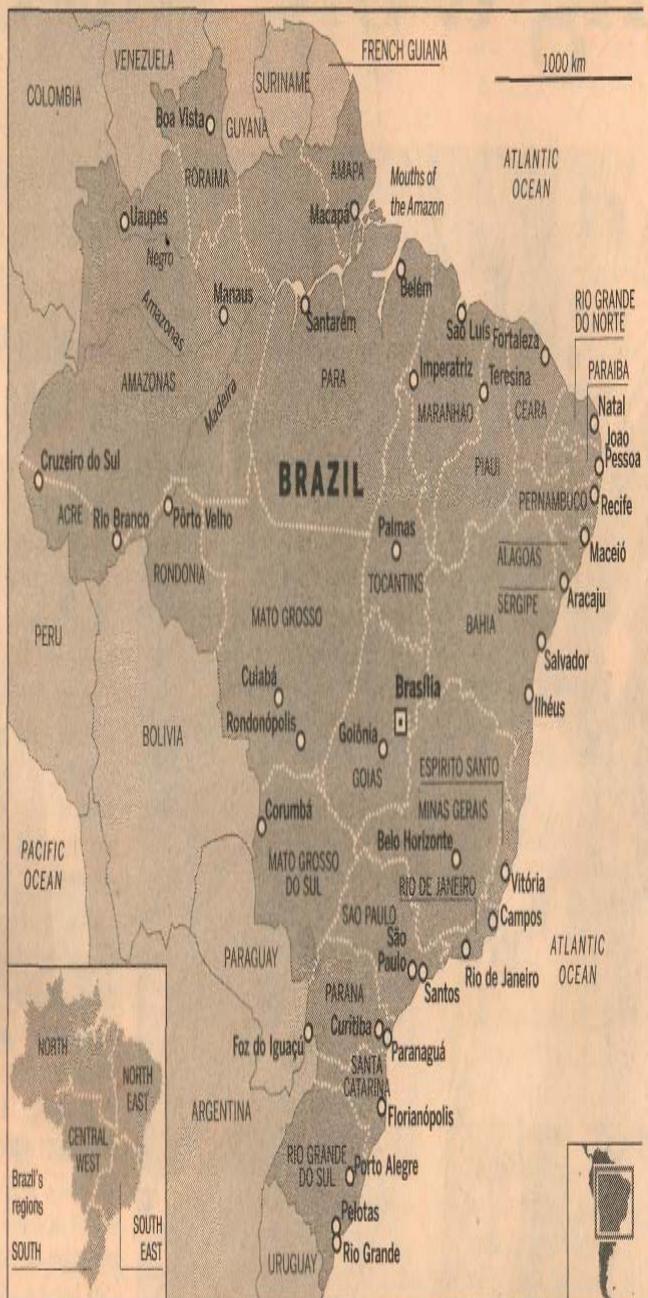
## Main trading partners

Share of total trade to world 2007 (%)



## Economic summary

	2008*	2009*
Total GDP (Real bn)	2,808	3,032
Total GDP (\$bn)	1,668.6	1,737.9
Real GDP growth (annual % change)	4.6	3.6
GDP per head (\$PPP)	10,254	10,702
Inflation (annual % change in CPI)	6.0	4.6
Agricultural output (annual % change)	4.3	3.0
Industrial production (annual % change)	4.4	3.8
Money supply, M1 (annual % change)	22.7	15.0
Foreign exchange reserves (\$bn)	237.8	273.9
Unemployment rate (% of labour force)	8.8	8.7
Budget balance (% of GDP)	-1.6	-1.9
Current account balance (\$bn)	-18.4	-19.2
Merchandise exports (\$bn)	189.5	212.0
Merchandise imports (\$bn)	164.0	190.7
Trade balance (\$bn)	25.5	21.3



Area	8,547,400 sq km	Exchange rate:	Population (2007)	183.9m
Language:	Portuguese	2007 average R\$1.9475=\$1	Main towns	
Currencies:	Real (R\$)	Latest figure R\$1.6057=\$1	Brasília (capital)	2,456,000
Standard and Poor's BBB-	Moody's Ba1	Fitch IBCA BBB-	São Paulo	10,887,000
			Rio de Janeiro	6,093,000
			* Forecast	Source: EIU