

## Reaping the rewards of indolence

*Some of the unreformed aspects of Brazil's economy are now helping to limit the damage from the world downturn—but its prudence in recent years is helping too.*



Reuters

Any list of the things that hold back Brazil's economy would until recently have included overbearing state influence in the financial sector. The government controls Banco do Brasil, a huge retail bank, and Caixa Econômica, the largest mortgage lender, plus the BNDES, a big development bank that feeds cheap credit to favoured companies. Hugely expensive bank loans are a handicap, too. And yet under changed circumstances such lamentable policies suddenly look far-sighted, and have given the global downturn an unusual tinge in Brazil.

Other countries are trying to work out how to run banks and direct credit to where politicians think it is needed. This is something Brazil did even when it was unfashionable. It is a sign of the times that a recent research note on Brazil from Goldman Sachs listed state involvement in banking as a plus. As for the private banks, the huge reserve requirements and taxes on funding that push up the price of their loans discouraged them from the wild risks that have brought down some peers in Europe and America. So far, credit in Brazil has been lightly chewed, not crunched.

Although the country has been spared the worst of the financial crisis, the economy is weakening. Redundancies have shot up, reversing the job growth of recent years in the formal economy (see chart). Embraer, a maker of jets, laid off 20% of its workers on February 19th. Vale, a mining giant, has cut 1,300 jobs and put more than 5,000 other workers on forced leave. Industrial production in December dropped 12%, the biggest fall in 17 years of record-keeping by the federal statistics agency.



This sharp slowdown will make for a grim year. Marcelo Carvalho, an economist at Morgan Stanley, has been forecasting no growth in 2009 and his view is fast becoming mainstream.

Brazil is likely to be as late out of the downturn as it was late in. If the past is a guide, its industrial production has followed China's exports up and down, with a lag of one quarter.

Yet by comparison with Brazil's recent past, and also with what other countries are experiencing, the economy is in fair shape. The IMF forecasts that only the developing countries in Asia (which are poorer than Brazil), Africa (ditto) and the Middle East will do better in 2009. Given Brazil's previous tendency to go into cardiac arrest whenever economies elsewhere became stressed, this is impressive. Argentina's crisis in 2001 and the Asian and Russian crises of 1997-98 were painful and disruptive for Brazil. The country's hypersensitivity to the vagaries of the world economy stretches back to at least the 1930s, when Brazil suffered a military coup during the Depression.

The reasons for its improvement are largely to do with public-sector debt, which was once a weak point but has been brought down below 40% of GDP. Foreign-currency borrowings have mostly been exchanged for real-denominated ones, so slumps in the currency no longer hurt the government's balance-sheet. Brazil has built up \$200 billion of reserves to defend the real. Its current-account deficit is small. Most important, this crisis is not pushing up inflation—Brazil's congenital weakness. That in turn has allowed the central bank to cut rates (making public debt cheaper to service). This is the first time Brazil has been able to run a counter-cyclical monetary policy.

Yet worries persist that the fiscal prudence of recent years will not last. Government spending grew as fast as tax revenues during the boom times. Now, revenues are dropping but there is no moderation in spending. Raul Velloso, a consultant, points out that public spending typically surges in the year before a presidential election. One is due in 2010, which makes restraint now unlikely. As a result, the primary budget surplus (ie, before interest payments) is set to shrivel or disappear.

In normal times this would scare bondholders, who view the primary surplus as a guarantee that they will get paid. In practice they may panic less now that government finances around the world are showing the same deterioration, or worse.

**The Economist, New York, 5 mar. 2009, The Americas, online. Disponível em <[www.economist.com](http://www.economist.com)>. Acesso em 12 de mar. 2009.**