

Brazil's new president

Coming down to earth

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Dilma Rousseff takes over a booming economy—and rising inflation and interest rates, lack of investment in infrastructure and a fiscally incontinent legislature

AS SHE steps into Brazil's presidency on **January 1st**, Dilma Rousseff can be cautiously pleased with herself. In choosing her 37 ministers she has made a reasonable job of satisfying the competing demands of her party and coalition, regional and ideological blocks and her own desire for a third of them to be women (she managed nine). In making Antônio Palocci, a former finance minister, her chief of staff she showed self-confidence: some thought she would balk at putting such a powerful political figure in a central role. Both that choice and her promotion of Alexandre Tombini from the Central Bank's board to its presidency pleased investors looking for signals of economic orthodoxy. She has even managed to remain gracious towards her predecessor, Luiz Inácio Lula da Silva, despite her political mentor's running commentary on her progress.

In the run-up to her inauguration, Ms Rousseff also received pointed reminders of the difficulties ahead. In a statesmanlike victory speech on October 31st she stressed that her priorities over the next four years were to eliminate extreme poverty and improve the quality of health care and education while maintaining economic stability and low inflation.

She has said she wants real interest rates, currently higher than those in any other big economy, to fall from 5% to 2% by 2014. But inflation crept up to 5.6% in November. The finance minister, Guido Mantega, who is keeping his job under Ms Rousseff, raised bank-reserve and capital requirements in a bid to cool the economy while forestalling rate hikes. Though the Central Bank duly stayed its hand, its quarterly inflation report, released on December 22nd, made it clear that the reprieve is temporary. Many economists expect a half-point rise in the benchmark Selic rate (now 10.75%) in January, and a further two or three such rises during the year.

That will put more upward pressure on a currency that more than doubled in value against the dollar during Lula's eight years as president. Tony Volpon of Nomura Securities, a stockbroker, reckons Brazil's treasury is losing around 40 billion reais (\$24 billion) a year as it sells Brazilian bonds to foreigners while investing the proceeds in dollar instruments yielding ten percentage points less. In October Mr Mantega tripled a tax on foreign investment in fixed-income securities to try to hold back the flood. But the real has fin-

ished the year no lower.

If interest rates, and the currency they undergird, are to fall as Ms Rousseff wants, she will have to slow the hectic increase in federal spending. The bill for payroll and pensions has risen far faster than inflation in recent years, with the task of keeping inflation under control left entirely to monetary policy. In the past three years the government has ramped up the resources of the national development bank, **BNDES**, by at least 20 billion reais, allowing it to expand lending for infrastructure projects and a host of other ventures less obviously deserving of state support. According to **IPEA**, a government-linked research outfit, the **BNDES'S** subsidised interest rates cost taxpayers up to 21 billion reais a year.

Ms Rousseff has spoken of the need to end such fiscal incontinence: she wants to cut net government debt, now 42% of GDP over her term. She is resisting pressure from her Workers' Party and its allies for a big rise in the minimum wage. At the end of November Mr Mantega said that he would provide the **BNDES** with only half as much extra funding in 2011 as it has had this year. To encourage the private sector to take up the slack he will slash taxes on bonds to pay for new, government-approved infrastructure projects. But as long as such high returns are available on short-term government paper, even a tax break may not make longer-term, riskier investments look sufficiently appetising.

Lula chose Ms Rousseff as his successor partly because more obvious alternatives were ruled out by various scandals. But he also saw in her someone who could turn big plans into reality. Brazil has long spent too little on infrastructure, and economic growth is making the shortfall ever more painfully apparent. As a local energy offi-

cial, Ms Rousseff kept the lights on after a drought in 2001 led to electricity rationing. She went on to run the government's giant infrastructure programme, known as **PAC**: during her election campaign Lula dubbed her the "mother of **PAC**".

If she fails on this front, she knows it will be with the world watching. Brazil is to host the football World Cup in 2014. By then it will also be clear whether work for the Olympic games to be held in Rio de Janeiro two years later is on track. Airports are the most pressing concern: passenger numbers grew by 8% during 2009, and further strong growth is expected. But most of the main airports are already operating above capacity. They are managed by **Infraero**, an air-force dominated state company that is a Brazilian byword for bureaucratic obstruction and incompetence. Of the more than 5 billion reais **Infraero** has earmarked for investment in the run-up to 2014, more than half is on projects that are already behind schedule.

Ms Rousseff considered taking **Infraero** away from the ministry of defence and giving it to the minister for ports. That would have made it easier to bring in private money, and perhaps private management too. But a narrowly averted strike over pay by airline staff in the run-up to Christmas delayed, and may block, the switch.

The biggest obstacle to Ms Rousseff's plans to spend less day to day, in order to invest in the infrastructure for which she hopes to be remembered, will be her fellow politicians. If she did not already know that, she was given a reminder on December 15th, when members of Congress voted themselves a 6% pay rise. Many state governments and municipalities have already followed suit. If all do, the total cost will run to around 22 billion reais a year. In a rare misjudgment of the public mood, Lula laughingly lamented his bad luck to be leaving just before the largesse arrived. "They are joking about our money," ran one newspaper headline. In the airports, protesters carried banners asking why politicians can get huge pay rises, but they cannot. Their strike may still go ahead in the new year, bringing Ms Rousseff down to earth with a bump.



Dilma starts to move out from Lula's shadow