



Will Brazil Go Right or Left?

The Shattering of the Political Center and the Implications for Brazil's Economic and Political Outlook

EXECUTIVE SUMMARY

Following the first round of the election on October 7, Brazil faces a stark choice in the presidential runoff between far-right Congressman Jair Bolsonaro and the leftist former Mayor of São Paulo Fernando Haddad. The presidential race has been characterized by an environment of fear and political intolerance. Yet the critical challenges that will confront the victor demand moderation and an ability to appeal to the majority of Brazilians who fall closer to the middle than the extremes of the political spectrum. Given the deteriorating fiscal situation, the next government will need to act quickly to reassure Brazilians and the world that it is up to the task — a task made all the more challenging by the deep partisan divide and widespread popular frustration with the failed political system and political leaders.

The Brazil Institute hosted a discussion on potential economic and political scenarios based on the two final presidential candidates and considered what might lie ahead for the country after the end of this divisive election cycle. Panelists Fernando Rodrigues (Poder360), Monica de Bolle (Johns Hopkins SAIS), and Antonio Britto (Brazil Institute Advisory Board) agreed that Bolsonaro is most likely to win the October 28th runoff against Haddad. The true question is what will come next: will Bolsonaro prove able to govern a divided country and fragmented political system? Rodrigues and Britto argued that Bolsonaro, if elected, will have a honeymoon phase in which he has support in Congress and the capacity to get things done, although both warned that it may not last. De Bolle noted that it remains unclear whether Bolsonaro will push for substantial fiscal and economic reforms (as his economic adviser Paulo Guedes advocates) or if he will propose watered-down measures that would likely prove ineffective at resolving Brazil's challenges.

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5th Floor, Woodrow Wilson Center

P*aulo Sotero*, Director of the Brazil Institute, began the conversation with a discussion of the results of the first-round elections and spoke about the future outlook for Brazilian politics. Sotero described the upcoming second round as a clear choice between right and left, following a fragmented first-round race. The objective of the panel, Sotero explained, was to understand the deeper meaning of the political tsunami that hit Brazil in the current election.

Recognizing the uncertainty of the moment, he noted that although the wide field of first-round candidates has been narrowed down to two, no one is sure where either outcome might lead. Brazil's former party system

has seemingly imploded and the task at hand involves reconciling the current political reality—an old system that is no longer capable of addressing the country's many challenges—with society's demands for renewed economic growth and improved quality of life.

Sotero also noted that presidential candidate Fernando Haddad underestimated what would be required to turn the political momentum in his favor and win the votes of the Brazilian people. Haddad's main strategy shift after finishing second in the first round involved simply switching the colors of his campaign ads from Workers' Party red to the yellow and green of the Brazilian flag, dropping former President Lula's image from campaign material, and visiting the jailed former leader less frequently. Sotero ended his remarks by noting that front runner Jair Bolsonaro promised to adhere to the current Constitution after his vice-presidential running mate's stated his aspirations to rewrite the 1988 document.

Fernando Rodrigues, Executive Director of Poder360, began his analysis of Brazil's current political situation with some historical context. He argued that it is important to keep in mind that Brazil's democracy is still in its infancy, barely three decades from the end of the military dictatorship. The last presidential election, which resulted in Dilma Rousseff's reelection in 2014, marked only the seventh consecutive direct election under the current Constitution—nonetheless a record number for Brazil. The culture of democracy is not as deeply embedded nor are democratic institutions as well fortified as in more mature democracies.

Yet Rodrigues stressed that Brazil's democracy has proven resistant to significant challenges despite its relative youth. In 1992—just four years after the transition to democracy was codified in the 1988 Constitution—Brazil weathered the impeachment of its second post-dictatorship President, Fernando Collor. In



Paulo Sotero



Fernando Rodrigues.

2002, left-leaning labor leader Luiz Inácio Lula da Silva was elected president of Brazil and financial markets responded negatively, fearing a populist swing to the left. Time proved those fears exaggerated, however, and Brazilian democracy remained strong with Lula at the helm. Rodrigues asserted that the “feeling of defeat” currently plaguing many journalists, voters, and onlookers is nothing new and can be overcome, as it has been in the past. Rodrigues predicted that Brazil’s democratic institutions will continue to function regardless of the election results, even with both candidates riding the ideological extremes and Brazilian society on edge.

Rodrigues also hypothesized about Bolsonaro’s prospects for governance, should the current frontrunner win on October 28. He estimated that Bolsonaro would probably have a majority in the lower house, with 300 to 350 deputies supporting him. That support could be almost unconditional due to the coalition’s structure, regardless of Bolsonaro’s choices or positions—just as Collor found consistent support in his coalition to pass even obviously poor quality policies, which later led to an economic recession.

Rodrigues also dispelled the perception that Bolsonaro and his continued success in the elections and polls are somehow a surprise, highlighting the fact that official polling has placed Bolsonaro as the frontrunner since the beginning. Yet despite his consistent lead, the vast majority of media coverage played up the idea that Bolsonaro would lose the second round to almost any other candidate.

Bolsonaro looks extremely likely to win, particularly as many supporters of candidates defeated in the first round have transferred their votes to him rather than to his opponent, Fernando Haddad. This trend runs counter to long-held political tendencies in Brazil, such as the Northeast’s traditional support for the Worker’s Party (PT) candidate—this year Fernando Haddad—grounded in the region’s disproportionate reliance on the cash-transfer program Bolsa Familia, which the PT consolidated and expanded under former president Lula. Haddad won more of the Northeast’s votes than any other candidate in the first round, but he received a smaller share than various opinion surveys predicted while Bolsonaro over-performed in the region.

Brazilians are looking to overhaul the political system, and are sending a message to the political establishment with their votes. Rodrigues noted that unemployment is at 12 percent and youth unemployment is even higher at 25 percent: it’s not a coincidence that many of the Bolsonaro camp’s most dedicated activists are young people.

Rodrigues concluded his remarks by predicting that Bolsonaro will win the election, Brazil will face challenging times lacking a defined economic plan and direction, and Bolsonaro will operate with significant congressional support at least throughout the first half of 2019.

Monica de Bolle, Director of the Latin America Program at Johns Hopkins School of Advanced International Studies, analyzed the current state of the Brazilian economy and offered predictions for economic policy, assuming a Bolsonaro victory.

She began by explaining the reduced political influence of Bolsa Familia, which Rodrigues had referenced. De Bolle observed that Rousseff's removal of price controls in 2015, as the country faced a major recession, caused immediate inflation but was not accompanied by a proportional increase in the Bolsa Familia stipend—even though the cost of increasing the stipend to bring beneficiaries above the poverty line would cost the government just R\$25 to R\$27 billion, a tiny fraction of the current federal budget. With recipients collecting less in real terms, Bolsa Familia lost political significance. Yet de Bolle said she was astounded that none of the presidential candidates in the first round capitalized on the political opportunity this divergence created. She argued that if a candidate such as *Ciro Gomes*, *Geraldo Alckmin*, or *Marina Silva*, all champions of social programs, had capitalized on this issue and supported an increase for Bolsa Familia, then the first-round election result might have been very different.

Turning to Bolsonaro's strong chances of winning the second round, she stated that gaining an understanding of Bolsonaro will take significant time. It is clear that the conservative leader is a "typical populist." De Bolle observed that the term "populist" is increasingly thrown about, yet the meaning of the word seems to change depending on who is using it. Nonetheless, populists always respond to complex problems with simple "magic formula" solutions that resonate with the public. Bolsonaro is the first Latin American populist in recent history to center his rhetoric not on income distribution, but instead on issues of public security: a serious and relevant concern of most Brazilians given rampant crime and violence in cities. The urban middle class in particular has readily consumed his simple proposals to confront the problem—such as arming the population and expanding the authority of police to arrest and kill suspects at their personal discretion—and therefore stands behind Bolsonaro and in staunch opposition to a return to PT rule.

Another common characteristic of populists, de Bolle explained, is that they never make unpopular economic reforms, no matter how necessary. Brazil faces pressing fiscal problems, including high deficits in the social security system, low growth, and high real interest rates.



Antonio Britto

According to estimates from the International Monetary Fund, Brazil's debt-to-GDP ratio has risen to roughly 85 percent and could easily rise to 100 percent in the next two years given the current economic trajectory. To reverse this trend, the new government will need to immediately introduce reforms, cut discretionary spending, and raise tax revenue.

However, Bolsonaro has only offered details on individual income tax reform: he plans to exempt the lowest tax bracket and implement a flat income tax of 20 percent on the rest of the population. De Bolle predicted that such a policy would reduce tax revenues, and noted that it is also “massively” regressive: it is likely to disproportionately burden the working and middle classes while simultaneously benefiting the rich. However, it is also a policy that would prove popular among those that would benefit from it, and would allow Bolsonaro to temporarily avoid more difficult but fundamental reform.

In regards to the highly controversial pension reform, de Bolle emphasized that Bolsonaro previously opposed reform as a federal deputy, and on the campaign trail he has been inconsistent on the issue. He has also criticized the Temer administration’s attempt at pension reform, which is currently stuck in Congress after running into opposition. De Bolle argued that although Temer’s reform proposal is imperfect, it has already passed many of the time-consuming hurdles in the law-making process and could provide a useful template for a new administration. However, Bolsonaro has suggested starting anew, a process that—even with wide support in the legislature—will take many months, especially with a freshly elected Chamber of Deputies and Senate. Additionally, if Bolsonaro is truly a populist, he will likely shy away from unpopular policies, including those most needed in the pension system. De Bolle thus expects that Bolsonaro’s pension reform—assuming there is one—will be considerably less effective than the bill currently before the National Congress.

De Bolle also warned that financial markets have misjudged Bolsonaro as a pro-market politician who will successfully prioritize economic liberalization and finally pass pension and privatization reforms. As with pension reform, the conservative politician voted against privatization as a federal deputy and has now implied that many of the state-owned companies that investors hoped would be privatized—as stated by Bolsonaro’s economic advisor Paulo Guedes—will remain under state control. Bolsonaro in fact echoed language used by the leftist Rousseff administration in referring to Petrobras, Eletrobras, Banco do Brasil, Caixa Econômica, and other state-owned companies as “strategic companies.”

This divergence between Bolsonaro and his economic advisor is important to watch, de Bolle noted. Bolsonaro has not only contradicted Guedes, a market darling whose presence in the Bolsonaro campaign has been

viewed as a promise of economic liberalization, but has censored Guedes during the campaign to avoid publicly broadcasting their conflict.

Moreover, connections to powerful special interests will force Bolsonaro to avoid advancing other important but unpopular reforms. For example, it will be difficult for Bolsonaro to tackle the financial distortions created by Banco do Brasil’s direct credit lines for agribusiness: the beneficiaries (large landowners and agriculture co-operations) form major conservative block in Congress that is expected to support Bolsonaro’s agenda. Similarly, reducing local content requirements (as many foreign investors desire) would upset domestic industrial interests, who are largely backing Bolsonaro. As a result, de Bolle predicted that Brazil will continue to be a state-led economy and will experience major economic turbulence, unless there is rapid implementation of needed reforms in the near future.

Antonio Britto, Board Member of the Brazil Institute Advisory Council, argued at the outset that it is wrong to view Brazilian politics through the lens of ideology. He contended that the political left and political right are always a minority in Brazil, with the majority of voters in the middle. Bolsonaro, therefore, does not represent the victory of the right over the left; he represents the victory of what Britto called the “party of those against” the status quo—the anti-establishment voters who say they reject traditional parties, technocrats, academics, journalists, and others who seem to have failed Brazil in its current crisis.

Drawing a comparison to former President Fernando Collor, Britto suggested that both Collor and Bolsonaro have risen to power on the backs of this spirit of contempt for the political system. He reasoned that history has circled back to the beginning of the Collor phenomenon in 1989, with Bolsonaro riding a similar political wave and Brazil still experiencing inflation, high levels of violence, and rampant corruption. In this sense, both individuals represent the vote “against.” This history also suggests that Bolsonaro is likely to be contained by Brazil’s political system and democratic institutions. It is “going to be a mess,” Britto conceded, “[but] a democratic mess.” The question of Brazil’s future under a Bolsonaro presidency is not one of left or right, democracy or dictatorship, but rather of Bolsonaro’s likely attempt to solve Brazil’s complex, longstanding problems in a simplistic solutions.

For Britto, the most worrisome player in Brazilian politics may not be the future president, but instead Congress. At present, Congress—with a few exceptions, including the PT—is not organized by parties or ideology; it is organized by special interest groups. It is abnormally conservative, which represents a setback for the progressive social agenda of recent years that brought significant gains for under-represented social groups and strengthened environmental protections, among other policy shifts. Major reforms will be difficult accomplished and likely ineffective, since Bolsonaro and many candidates elected to legislative positions from his Social Liberal Party (PSL) are, ironically, connected to entrenched traditional interest groups despite their political rise as populists. Britto reaffirmed de Bolle's point that due to their populist nature, these politicians will also shy away from meaningful yet controversial reforms and opt instead for simplistic solutions.

With this dynamic in mind, Britto offered a few predictions for a potential Bolsonaro presidency:

First, Bolsonaro represents no real threat to Brazilian democracy; and second, Bolsonaro is not expected to pass any strong reforms beyond some basic economic policy changes in the beginning of his term. Bolsonaro will, however, cause conflict between what the country urgently needs and what he proposes (and Congress endorses). A key problem is that Bolsonaro, in Britto's words, "doesn't know what's going on" and has a limited understanding of the Brazilian economy, as he stated more than once early in the campaign.

Importantly, Britto is not concerned with what will happen in January, when the new president takes office. He is concerned with what will happen after a six-month "honeymoon period," when internal conflicts already brewing—between Bolsonaro and Guedes and the various groups that supported his candidacy—escalate. He urged academics and the press to keep this six-month period in mind. In closing, Britto insisted that a Bolsonaro government will not result in tragedy, only disorder.

Q&A Session

Q: If Bolsonaro gets elected—not because of Bolsa Família, but largely because of the middle class—why can't he take on the civil servant pension system? He would solve a huge problem if he could solve this one issue.

Rodrigues noted that the campaign rhetoric used by candidates and the policies implemented once they are in office often differ. We should expect that many of the policies that candidate Bolsonaro has promoted will change if he enters office. According to Rodrigues, Bolsonaro has been extremely careful not to say anything that might hurt his popularity; however, if Bolsonaro takes office he will no longer be constricted in the same way, and so his actions would likely contradict some of his campaign promises. Furthermore, Rodrigues added that he believes Bolsonaro, if elected, will attempt to begin working on pension reform even before he is sworn into office on January 1, 2019. Rodrigues cited the high renewal rates in Congress as a factor that would help Bolsonaro in passing pension reform before he is inaugurated and the new congressional members take over. Rodrigues argued that it would be unwise of Bolsonaro to ignore this unique opportunity to pass this controversial, yet necessary, pension reform.

Britto defended his belief that some type of pension and fiscal reform will be passed either within the next two months of Temer's administration or the first six months of Bolsonaro's administration, assuming he is elected. However, Britto expressed concern that, due to Bolsonaro's populism, any reform that is passed will be insufficient for Brazil's needs as there are Brazilian peculiarities that must be understood prior to crafting a successful pension reform bill. Britto reiterated that some reforms will be passed through Congress, but there is no guarantee that they will be successful, especially in the long run.

Q: Do you think that Television Globo will play an important role in influencing the results of the second round elections?

Rodrigues pointed out that Globo is one of the largest television networks in all of Latin America. Nonetheless, he does not believe that Globo has enough influence in Brazil to change the results of the elections. The only thing that could change the election's dynamics at this point would be some unforeseen event or news.

Sotero pointed out that Alckmin invested a lot of his resources and strategies in television ads, which was in keeping with the traditional model of campaigning, but proved unsuccessful.

De Bolle argued that many Brazilians no longer trust traditional media, which has been undermined by the use of social media (including WhatsApp), as well as Bolsonaro himself, who challenges their reporting as “fake news.”

Q: How long will markets need to establish a consolidated view of the new administration?

De Bolle explained that the markets are extremely fickle, making it difficult to predict a timeline for how they will react to the election results. Investors are currently bullish on the elections because they believe that the new reforms expected to be passed in the first six months will be advantageous to investors’ interests. However, de Bolle predicted that after the initial honeymoon period, investors will likely realize the reforms were unsustainable or ineffective. The large banks in Brazil believe that any type of reform would bolster Brazil’s economy, so markets might ride this euphoric Bolsonaro wave for some time, but the wave will eventually crash—it is just a matter of time.

Q: Is there a need to reform the political electoral system in Brazil?

Rodrigues clarified that Brazil is currently undergoing political reform, but that it will be a long process due to Brazil’s democratic political system. Autocratic countries can make large changes overnight, but Brazil will need ten to twelve years. He explained that the military regime in Brazil originally set up a two-party system that lasted about two decades. In the 1980s, when democracy was reinstated, the multiparty system returned and several incentives were created to encourage the creation of new political parties. However, the current Constitution only envisioned six to seven fully operational political parties and this year the number of political parties in Congress hit 25 parties. It will take time to address Brazil’s political party system challenges.

Q: Can we expect to see a Bolsonaro administration take a much more active role in the Venezuela crisis?

Rodrigues recounted a conversation with Eduardo Bolsonaro, Jair Bolsonaro’s son and an elected congressman from São Paulo, who said that they are considering breaking relations with Venezuela. Rodrigues reminded the audience that this might simply be “campaign talk” and Bolsonaro’s actual policy towards



Venezuela could shift if elected. However, Rodrigues expects Bolsonaro's administration to take a hard line on Venezuela.

Britto agreed that Brazil will likely take a more aggressive public position vis-à-vis the Maduro regime in the first few months of Bolsonaro's administration. However, Britto noted that this can only go so far, as Brazilian public opinion will likely be against sending military forces into Venezuela's crisis. This opinion is also shared by the Brazilian armed forces.

Q: Is there any correlation between the decline in Bolsa Familia payments and the increase of violence in regions that heavily depend upon Bolsa Familia?

De Bolle explained that there is not a direct correlation between the decline in Bolsa Familia payments and the increase in violence. Instead, the spike in violence seems to be a result of fiscal problems at the state and municipal levels of government. Many states, especially those in the northeastern region of Brazil, have high levels of debt, do not produce enough revenue, and therefore rely heavily on federal transfers. However, due to fiscal issues at the federal level, states have not been regularly receiving these transfers.

Q: Brazil in the early 2000s, after the election of Lula, saw an increase in foreign investment. Might there be a similar occurrence if Bolsonaro is elected?

De Bolle clarified that, unlike Bolsonaro, Lula was not a populist—he was a pragmatist. De Bolle argued that if there was one thing Lula understood very well, it was

that inflation was not only very harmful to Brazil as a whole, but it was especially harmful to his principal voter base: the poor and working class. She maintained that Lula had a level of pragmatism and a political savviness that Bolsonaro does not even come close to having, which brings into question his ability to manage the economy successfully in the long run.

Q: Do you get a sense that Bolsonaro knows what he doesn't know?


A: De Bolle: No.

Q: What are Bolsonaro's views on a commercial agenda and direct investments?

A: De Bolle affirmed that Bolsonaro does not have a well-defined commercial agenda and noted that Bolsonaro has publicly expressed his disdain for China, Brazil's largest trading partner. Bolsonaro has hinted at wanting to open up the Brazilian economy, although she predicts that this posture most likely means that Bolsonaro wants to increase exports, but not necessarily imports. She argued that Bolsonaro will be in favor of investments as long as it does not require Brazil to increase imports. However, de Bolle explained that this is actually conflicting since the composition of imports in Brazil, mostly capital goods, is what leads to investments; hence there would be very little investment growth without reducing the current barriers to imports.



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