



A New Decade, New Trajectory for the Brazilian Economy?

Brazil wrapped up 2019 with GDP growth estimated to be no more than 1.17 percent—hardly cause for excitement after a decade in which Brazil grew 3.6 times slower than the average for emerging and developing nations—but hopes are higher for 2020. The Brazilian government predicts the economy will grow 2.4 percent this year, encouraged by new economic policies, low inflation and higher consumer confidence, and the passage of pension reform in October 2019.

This optimism also stems from the government's ambitious economic agenda for 2020: tax reform, administrative reform to modernize the Brazilian state, and new policies to encourage investment and open trade. Notably, two major, pending initiatives on trade to resolve difficulties within Mercosur and allow the trade bloc to engage in meaningful conversations with the European Union remain uncertain. And the stakes are high. Beyond the obvious economic implications, the political fate of the current administration—whose approval rating has slowly waned—depends heavily on its ability to restore growth and reduce unemployment.

On January 27, 2020 the Brazil Institute hosted a panel featuring experts Mauricio Moura, Christopher Garman, Monica de Bolle, Mauricio Mesquita Moreira, and Amy Erica Smith on the prospects of the Brazilian economy and the political environment in 2020. The discussion covered topics ranging from the public's changing views on President Jair Bolsonaro, the administration's proposed economic reforms and Brazil's structural issues, to free trade, and the economy's effect on politics.

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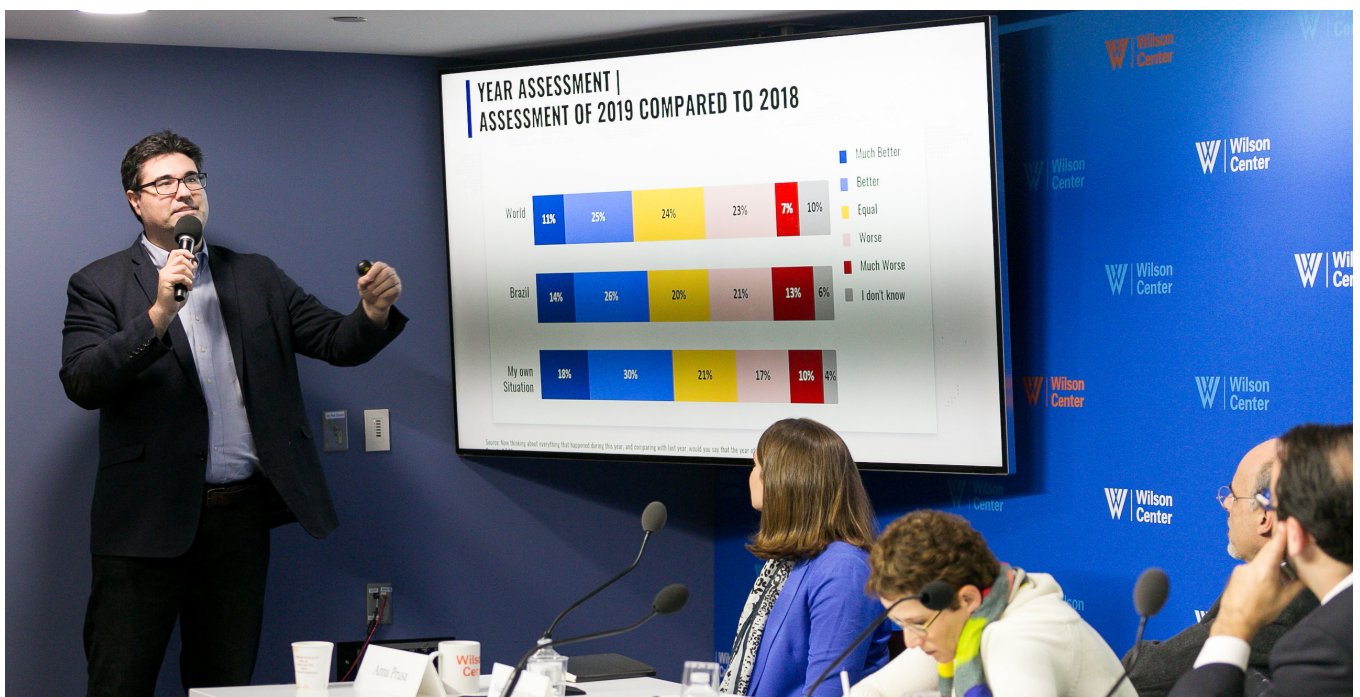
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Paulo Sotero, Director of the Brazil Institute, opened the event, acknowledging that Brazil experienced low economic growth in 2019—just 1.17 percent. Though modest, this growth nonetheless shows evidence of economic improvement, a cause for hope after five years of economic stagnation. The Brazilian government predicts that this upward trajectory will continue into the future: the administration estimates that in the next two years, GDP will increase 2.23 percent and 2.5 percent respectively. Economic reforms spearheaded by Speaker of the House Rodrigo Maia are responsible for much of this optimism, including the promised administrative and tax reforms on this year’s political agenda.

Mauricio Moura, CEO and Founder of IDEIA Big Data, described the Brazilian public’s changing views of the Bolsonaro administration according to polling conducted by his company. Since January 2019, President Bolsonaro’s approval rating has decreased from 50 percent to 34 percent, while the disapproval rating has increased from 22 percent to

30 percent. The data also showed that the largest pool of support comes from middle-income, Protestant men from southern and southeastern regions of the country. Meanwhile, the largest pool of disapproval of Bolsonaro’s government consists of lower-income, Catholic women from the northeastern region. Moura argued that these women, as well as other low-income demographics, feel alienated by Bolsonaro’s government and pessimistic about Brazil’s economic future.

Moura’s 2019 end-of-year survey data further demonstrates the differing opinions on Bolsonaro’s performance during his first year in office. The percentage of people who described the year as difficult was not far from the percentage of people who described the past year as hopeful: 21 percent and 15 percent respectively. In addition, the public rated the economy as Bolsonaro’s best area of performance during his first year in office, while rating the environment, closely followed by education, as his worst areas. Despite





this political polarization, Moura emphasized that optimism prevails. The public expects a reduction in unemployment; improvements in the economy, public security, education, and health; and increased consumption of durable goods this year. In closing, however, Moura argued that local issues will take precedence in municipal elections this October—and cautioned that “fake news” will also impact these elections, as it did in 2018 when Bolsonaro was elected president.

Christopher Garman, Managing Director for the Americas at Eurasia Group, similarly emphasized the political divide in Brazil. He explained that Bolsonaro’s “anti-establishment” rhetoric has weakened the executive branch’s relationship with Congress and as a result, the administration “will never have a working majority in Congress.” Nonetheless, Garman described the country’s political conditions as constructive for the advancement of reforms aimed at increasing GDP. Since the approval of the historic pension bill in October 2019, the Bolsonaro administration has proposed additional reforms. The economic team, headed by Economy Minister Paulo Guedes, has sent three different proposals for constitutional reforms to the Senate: PEC 186/2019, which aims to ensure constitutional limits on spending; PEC 187/2019, which aims to eliminate current public funds; and PEC 188/2019, which aims to transfer revenue to state and municipal governments,

Garman explained. Proposals for administrative, tax, and microeconomic reforms in the lower House, paired with trade opening and privatization agendas show that the administration has a broad and ambitious plan for the economy.

Garman noted that unlike the pension reform, the more recently proposed economic plans have not generated public debate, and are unlikely to hurt the economy if not acted upon. Nevertheless, party leaders are likely to support them in order to increase their own control over resources, a strategy that members of Congress have adopted to ensure reelection. Garman expects that the three proposals (PECs) previously mentioned and the “Mansueto Plan” (PLP 149/2019) will be approved later this year or in 2021. Continuation of these reforms will provide Congress with a clear agenda, as members will be in “cruise control,” he argued. However, popular discontent with economic growth and social unrest could discourage legislators from supporting reforms, complicating the approval process.

Though he emphasized the positive effects of economic reform on the Brazilian economy, Garman also commented on the importance of other factors, such as education and the environment, for economic growth. He cautioned that high rates of deforestation could lead to short term economic repercussions, and as a result, the administration must also address these issues.



Monica de Bolle, Senior Fellow at the Peterson Institute for International Economics and professor at John Hopkins University, emphasized Brazil's structural issues. She argued that the lack of reaction to low interest rates in Brazil was evidence of economic stagnation. In addition, though high taxes and low productivity have afflicted the economy, the country's regressive VAT tax system may also have negative effects, and the lack of mechanisms to address this issue could lead to social unrest. De Bolle then identified the environment and education as critical long-term factors for the economy, since both must be addressed to ensure sustainable economic success.

De Bolle stated that Brazil currently does not have an agenda for climate change, which has likely contributed to secular stagnation—the lack of economic growth. However, in other countries facing similar economic challenges, leaders have begun de-carbonization efforts. Brazil also does not currently have education policies to address its low OECD PISA scores; these test scores reveal that Brazilian high school students do not reach the minimal capacity level in science, math, or reading regardless of socioeconomic status. Experts thus predict a future rise in the low skilled workforce, which will further decrease Brazil's economic productivity, de Bolle warned.

To conclude, she argued that the government must take a more holistic approach to addressing Brazil's economic growth, and seriously consider factors such as education and the environment for long-term economic prosperity.

Mauricio Mesquita Moreira, Principal Economist at the Inter-American Development Bank, focused his comments on free trade and Mercosur. Despite 30 years of efforts to liberalize trade in Brazil, the economy remains closed, as shown by high tariffs and trade-to-GDP ratios. While other Latin American countries that liberalized their economies experienced an additional 1 percent growth in GDP per year for a period of 20 years, protectionist measures in Brazil have led to recession.

To address the issue of free trade, the Bolsonaro government pushed forward on the EU-Mercosur agreement, and renounced Brazil's developing country status in the World Trade Organization (WTO) in 2019. Mesquita considered these to be steps in the right direction, but noted that the EU-Mercosur agreement will take at least a decade to be implemented, and thus is unlikely to happen during Bolsonaro's term. He therefore argued that multilateral agreements must take place in conjunction with unilateral agreements to ensure more immediate actions towards economic liberalization.





Following the debate over Brazil's economic prospects in 2020, Amy Erica Smith, Associate Professor of Political Science at Iowa State University and Fellow at the Wilson Center, asked whether and in what ways the economy matters for politics. Drawing on research from the Getulio Vargas Foundation, Smith explained that Brazilian presidents often take the blame or receive credit—depending on the situation—for aspects of the economy unrelated to their presidential performance. For example, U.S. interest rates and commodity prices are often attributed to presidents, despite their lack of control over these aspects. Therefore, although Congress is driving economic reform in Brazil, Bolsonaro is likely to get credit for their efforts, Smith argued.

She then discussed the societal impacts of economic performance. During times of economic shock in the 1980s, individuals were more likely to convert to Pentecostalism, as these churches appealed to individuals suffering from the “pathogens of poverty;” Smith argued that the rise of Evangelical political leaders today may be due to the “neoliberal shocks” of the 1980s. Smith also presented research from economists at Iowa State University, which suggested that individuals living in unstable economic situations tend to “withdraw from society,” to shy away from participating in politics, instead devoting their time to religion. She concluded in agreement with de Bolle that long-term actors on the Brazilian economy, such as education and the environment, should be examined further.

“What happens in the next six to eight months will be very, very important for Brazil's outlook for the next couple of years, because if you take steps on this agenda, you guarantee the fiscal anchor on the fiscal emergency reform, you guarantee the spending cap is resolved, you anchor lower real interest rates, and you have progress on the micro-economic reform agenda.”

-- Christopher Garman

Q&A Session

Q: Is there currently an increasing trend in individuals converting from Catholicism to Protestantism? Are churches engaging in politics?

Smith explained that participation in secular society may be decreasing, while participation in religious civil society may be increasing as the result of economic shocks. Unpredictable economic events occurring in Brazil are leading people to withdraw from aspects of society that aren't immediately necessary for their short term, such as political participation. However, they participate in the Pentecostal church because it preaches prosperity theology: the belief that their strong faith will lead to material prosperity. She also noted that though individuals may withdraw from political engagement and turn to the church, the church is very much politically involved. In addition, she mentioned the increasing conversion rate from Catholicism to Pentecostalism.

Moura added that fertility rates among Evangelicals are higher than the national average. Recent data shows that Evangelicals have children younger, and that they have more children than the average Brazilian. According to Moura, Brazil will likely be a majority Evangelical country by 2050. As a result, politicians must appeal to this demographic to ensure their political success.

De Bolle further stressed the influence Evangelicals have on politics. Based on her analysis, there is a strong correlation between the share of evangelicals in a given municipality and the share of the second-round vote for Bolsonaro: municipalities with larger shares of Evangelical populations tended to have 60 percent or more support for Bolsonaro.

Q: If Bolsonaro is pushing for privatization programs, why didn't he vote in favor of the privatization of the Banco do Brasil?

Garman explained that though the administration is supporting "a robust agenda for privatization," Bolsonaro has not approved the privatization of Banco do Brasil, Caixa Econômica Federal, or Petrobras. Instead, he has decided to "do corporate overhaul and to sell assets" within the three companies. However, the state utility company, Eletrobras, may receive congressional approval for privatization next year. If Bolsonaro wins reelection, he may then tackle Petrobras.

De Bolle commented that despite Bolsonaro's "economic nationalist rhetoric," he has a liberal economic agenda. However, she warned that historical trends show that many nationalist agendas began as liberal ones, and the current agenda may not be seen through to the end.



Q: How can the risk to democracy in Brazil undermine the economy?

According to Moura, “higher income people are less concerned about democracy.” Wealthier individuals seem to be more concerned about the ousting of the Workers’ Party (PT) than stable education systems. On the other hand, lower income individuals understand the risk associated with the appointments of people that may undermine democracy.

De Bolle noted that in Brazil, unlike in the rest of the world, the middle class tends to align with the government, regardless of its views. The economic and financial elite tend to view the economy as an entity independent from democratic institutions. However, weak institutions have negative short and long-term effects on the economy. If the economy does well in the short run, the weakening of institutions is legitimized, which could lead to long term problems. De Bolle alleged that democratic institutions are being weakened by Bolsonaro, and that society is losing faith in the Supreme Court.

Garman contested that the “independence of the judiciary, the strengthening of Congress over budgetary resources, and the weakening of the executive branch” demonstrate the strengthening of democratic institutions, as an unintended result of polarized politics.

Smith remarked that, while research shows “there isn’t a strong causal linkage between democracy and economics,” she would like to believe that the failure of liberal democracy would ultimately hurt the economy.

Q: How long is Paulo Guedes expected to remain the Minister of Economy?

According to Moura, since his appointment, Guedes has become the second most well-known minister of the Bolsonaro administration. However, this has led to the polarization of public opinion: while the middle class feels that Guedes will positively impact the economy, lower-income individuals feel disconnected from him, and feel that he doesn’t appeal to their needs.

De Bolle predicted that Guedes will retain his position as Minister for the time being.


Garman added that because Guedes has a strong relationship with the president, he is likely to stay in office, though his position can’t be guaranteed.

“The discussion [in European countries] is about decarbonization and how do you make fiscal, monetary, [and] public investment policies. All of these things come together under the agenda of decarbonization. If you want to be a modern economy, if you want to look towards the future, that is where the discussion needs to be, and that is not where the discussion is in Brazil.”

-- Monica de Bolle



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