

# Challenges confronting Brazil

Getulio Vargas Foundation,  
April 4, 2013

Luiz Carlos Bresser-Pereira  
[www.bresserpereira.org.br](http://www.bresserpereira.org.br)

# Just before the 2008 global financial crisis

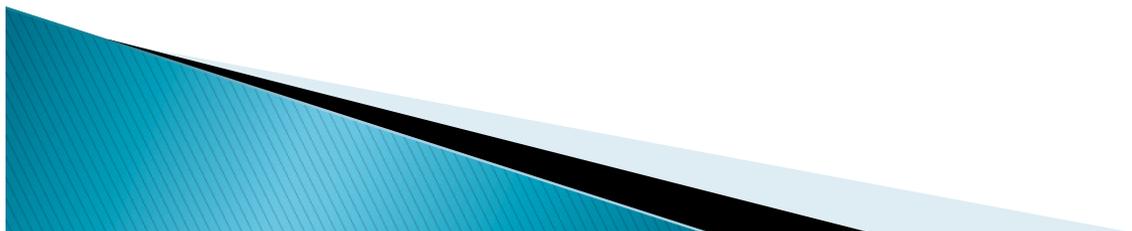
- ▶ Brazil was seen by rich countries as a highly dynamic economy and the “the best o the BRICs”.
- ▶ In the early 2010s, back to 2,5% growth  
Growth numbers in the mid 2000s was back to modest 2,5%

BRICs	GDP Growth
China	10%
India	8
Russia	6
Brazil	4,5

# Why so much enthusiasm, given so modest performance?

Because, among the four countries, Brazil was the one

1. that followed more industriously the economic policies and reforms recommended;
2. that proportionate easy gains in carry-trade operations by appreciating gradually the real since 2003;
3. that offered better conditions to multinationals' investments.



# Why was Brazil's growth satisfactory in mid 2000

- ▶ Because, pushed by China, the price of the commodities increased, and exports were multiplied by more than three

Ano	Exportações (US\$ bi)
2002	60,4
2004	96,6
2006	137
2008	197,9
2010	201,9



# Why has been Brazil's growth so modest since 1994?

(Note that I am using as starting point 1994 because in this year the Real Plan finally controlled high inertial inflation)

Because, by following dutifully Washington's recommendations, Brazil:

1. Kept the interest rates too high,
2. Kept the exchange rate highly overappreciated,

What meant a disincentive to investment.  
and resulted into a small (1.8%)



# Why is the investment rate low?

Not because

- ▶ Domestic savings are small
- ▶ Lack of investments in the infrastructure
- ▶ Lack of good institutions.

But because

- ▶ Although the interest rate fell, it remains too high and
- ▶ the exchange rate continues to be highly overvalued.



# Why does the interest rate continue to be high

- ▶ Because the Brazilians continue to be hostage of inflation.
- ▶ Because the rentier neoliberal coalition gains from high real interest rates.
- ▶ Because this coalition claims that the “natural interest rate” is much higher here than in other countries, and successfully persuades the government and civil society on that freak argument.



# Why is the exchange rate overvalued in Brazil?

Because Brazil does not neutralize the tendency to the overvaluation of the exchange rate. Or, in other words, because:

- ▶ The interest rate is high.
- ▶ Brazil suffers from a non-neutralized Dutch disease.
- ▶ Because Brazil does not control sufficiently capital inflows.
- ▶ Because politicians, households and foreign interests are happy with an overvalued real.



# Politicians are happy with an overvalued currency

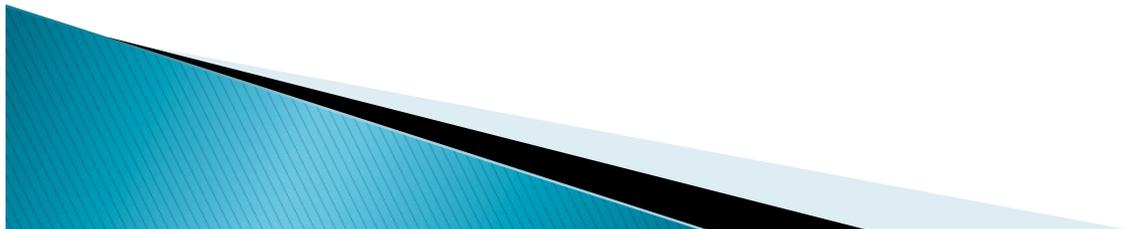
- ▶ Because, when a currency depreciates, wages (and other incomes) will fall in real terms.
- ▶ Because firms and banks indebted in foreign currency will suffer from the depreciation.
- ▶ Because when elections get near, a common strategy is to appreciate the national currency – what will decrease inflation and increase wages, and facilitate politicians' reelection.

I call this “exchange rate populism”.



# Households and firms are happy with an overvalued currency

- ▶ Households, because wages and salaries remain high;
- ▶ Agribusiness, because they know that a tax on exports will be required to neutralize the Dutch disease. (Although what they will pay with the export tax will be returned to them on the form of a depreciated currency).
- ▶ Business firms. Only the ones that are indebted in dollars.
- ▶ Banks. Most of them, because they often have credits with the above firms.



# And the inflation?

- ▶ Inflation is **not** the fundamental problem that the Brazilian faces since 1994.
- ▶ If the indexation of the contracts signed with the government had been forbidden, Brail's inflation would be just a little above the one existing in rich counties.



# My modest predictions

- ▶ The exchange rate will continue in the same level in the two next years.
- ▶ Brazil will continue to grow modestly.
- ▶ But, after the October 2014 presidential election, in which Dilma Rousseff will most likely reelected, either the government will realize that he must depreciate the real, or it will face a new balance of payment crisis.



**Luiz Carlos Bresser–Pereira**  
Professor Emérito da Fundação Getúlio Vargas  
[www.bresserpereira.org.br](http://www.bresserpereira.org.br)

