What can African countries learn from Brazil’s inclusive growth and development?

Policy briefing:

Is there a new Brazilian development model?

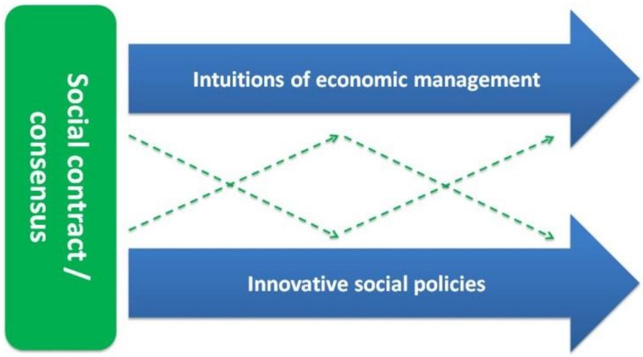
Since the mid-1990s, despite occasional short-lived crises, Brazil appears to have embarked on a new developmental trajectory in which reasonable growth performance has been combined with an increasingly effective assault on poverty and inequality. The pro-poor character of economic growth in Brazil during the contemporary era stands in marked contrast to the experience of previous boom periods.

The International Research Initiative on Brazil and Africa has examined key aspects of Brazil’s development experience since the mid-1990s and concludes that this constitutes a new Brazilian development model. Our ten key findings are:

1. The Brazilian model is a blend of consensus and conjuncture

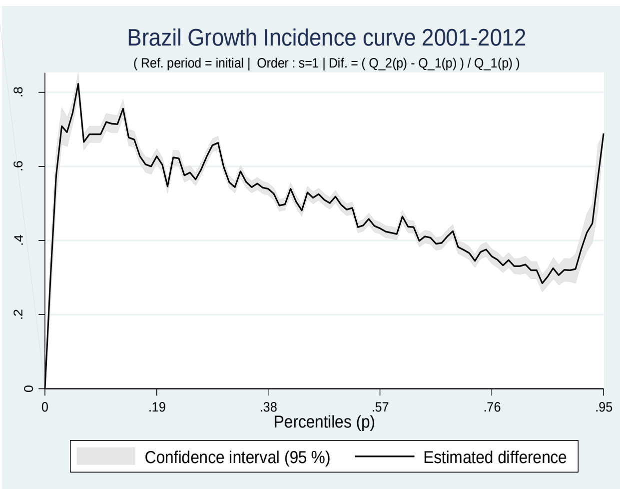
Our assessment is that a unique combination of economic and social policies is primarily responsible for the unexpected success shown by Brazil. There are specific features of the institutions of economic management developed after the stabilization plan of 1994 which together with innovative social policies emerging from municipal activism and a favourable social contract set a new course for Brazil.

The Brazilian development ‘model’ in action:



A renewed consensus or ‘social contract’ is acutely significant in ensuring the conditions for a positive evolution of these institutions. It ensures economic and social policies work together and reinforce each other. This is what we mean by a ‘model’. Of course, not all policies fitted together always. Important areas such as infrastructure lacked effective policies; while others like the effective prosecution of corruption cases were stymied by institutional bottlenecks.

2. Brazil’s development model is based on inclusive growth



The defining feature of Brazil’s recent economic success is not the fact that the economy grew steadily during the first years of the new century. GDP growth rates have averaged 3% since the mid-1990s and Brazil did not achieve Chinese or Indian rates of economic growth. It is the quality of its economic growth that is noteworthy.

The lowest deciles of income grew at Chinese rates, while the wealthiest deciles of income did much less well, growing at Cote d’Ivoire rates. While all sections of society saw their incomes rise, the poorest benefited most. This has been reflected in declining levels of inequality in Brazil. The GINI index fell from 60.13 in 2000 to 54.69 in 2009.

3. Macro stability has underpinned progress

The cornerstone of Brazil's successful economic transition has been a process of cumulative institutional reforms. These have affected the formulation of fiscal and monetary policy in addition to the operation of the financial sector. Taken together these reforms have underpinned the price and financial stability, which have in turn facilitated the pursuit of inclusive growth.

The critical turning point in the transition to inclusive growth came two decades ago with the elaboration and implementation of a complex stabilization plan, the Plano Real (Real Plan) between 1993 and 1994. Introduced to combat hyperinflation, the Real Plan was introduced gradually and cleverly employed a pegged exchange rate. Allied with trade liberalization this maintained an external check on domestic price formation without stifling growth. The formal currency peg was replaced with an inflation targeting framework at end of the 1990s.

4. Fiscal capacity and responsibility has been vital

Accompanying the introduction of a new and pegged currency, the Real policymakers added a firmly orthodox plank to their counter-inflationary strategy by setting targets for the fiscal balance. Their strategy combined more effective constraints on public spending with limited reform of the taxation system. The centrepiece of the reform programme was the formulation of a fiscal targeting framework, an institutional innovation which would go on to prove very effective in ensuring the continuation of price stability, while building credibility among outside investors. The fiscal autonomy of states and municipalities was also reduced, providing an effective constraint on public spending.

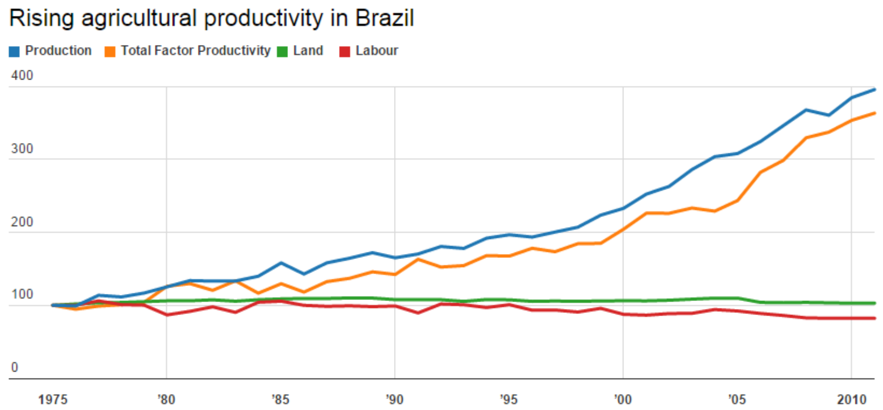
Thanks to the effective reform of its financial system, Brazil has seen a considerable expansion of credit to households, firms and to finance the expansion of housing stock. The expansion of credit has proven an important driver of growth. The national development bank (BNDES) has played an active role, which helped to limit the impact of international financial contagion following the Lehman Brothers collapse.

The tax raising powers of the various levels of government have proven impressive by emerging market economy standards, accounting for over 30% of GDP. As growth accelerated following stabilization it has consequently proven possible for the federal government to combine fiscal rectitude with a rise in spending on social programmes

5. Agriculture has been transformed

One of the key elements of Brazil's economic transformation over the past two decades has been the resurgence of agricultural exports. Agriculture has undergone a dramatic transformation, making Brazil one of the major breadbaskets of the world: in 2010 the country was the world's foremost producer of sugar, coffee, orange juice and poultry, the second main producer of soybeans, the third main producer of corn, and the fourth main producer of pork. Yet any notion that the agricultural sector had the potential to become an export dynamo would have seemed highly improbable during the 1970s and 1980s.

Brazil has made dramatic improvements in agricultural productivity. Whereas the total area of land in agriculture has remained basically the same since the mid-seventies, production has increased by nearly 300%. The surge in agricultural productivity experienced by Brazil has comfortably outstripped that of other countries in the region and has outpaced China and the USA.



While agricultural policy making had a relatively limited impact on performance of the sector, broader institutional changes exercised a much more important role. The renaissance of Brazilian agriculture should not be seen in terms of expansion of factors of production but also in terms of institutional and technological innovations, not all of which could be described as sector-specific.

Brazil did not follow a carefully laid out, predetermined strategy whose aim was to turn the country into the international agricultural giant which it is today. It pragmatically adapted its light touch market-oriented agricultural policies in order to seize opportunities opening up in both domestic and international markets.

6. Brazil shows the 'resource curse' is not inevitable

Brazil was never dependent on a single commodity and diversification under Import Substitution Industrialisation met moderate success in broadening the productive base. Recent export performance shows the effectiveness of exploiting underlying natural comparative advantages in agricultural and minerals as a platform to move up the value chain and develop successful agro-industry

A key driver of the productivity gains experienced by the Brazilian agricultural sector has been a strong record of innovation, one area where the state has played an active and consistent role. EMBRAPA, a federally funded agricultural research agency, has been central to funding research and facilitated research networks linking agricultural producers, research laboratories and private sector suppliers of agricultural seeds, technology and equipment.

The agricultural transformation of Brazil should not simply be understood in terms of a quantitative increase in production and exports; there have also been qualitative improvements which have allowed producers to seek out new - and lucrative - market niches whether domestically or in the global marketplace.

7. Social policy has focused on inclusion & productivism

Social policy has been a core component of the Brazilian development model, making a significant contribution to inclusive growth. Transfers-in-kind, as in education, training and healthcare, and transfers in cash, as in social insurance and social assistance, have been the object of policy activism.

The 1988 Constitution constituted a watershed, enshrining the principle that government has a responsibility to ensure a minimum income security to all citizens independently of their capacity to contribute to social insurance. Two social pension schemes, the Previdencia Social Rural and the Beneficio de Prestação Continuada, were both established in the mid-1990s. Subsequently, the Lula administration implemented Bolsa Família, which provides regular income supplements for households in extreme poverty with conditions ensuring children's school attendance and primary healthcare utilization. Together with rising minimum wages, Brazilian antipoverty transfers have played an important role in reducing poverty and inequality.

The recent increase in social expenditure in Brazil is likely to have a direct effect on growth through their effect on demand. Estimates of the multipliers applying to government expenditure suggest that the focus on disadvantaged groups in the expansion of social policy had measurable effects on economic growth. IPEA has estimated that the GDP multiplier of social expenditure taken as a whole was of the order of 1.37 in the mid-2000s, while the social expenditure multiplier in household income growth rates was higher at 1.85.

8. Rising tax revenues have been redistributed

Brazil has managed a remarkable 7% increase in tax revenue as a percentage of GDP between 1995 and 2010, from 26.9% in 1995 to 34% in 2010. This is intriguing because it is associated with neither a change in the tax code nor a change in tax administration.

We argue that that a combination of baseline conditions, namely strong bureaucratic capacity; and the process of democratisation, partisan competition, fiscally responsible centre-left coalitions, and executive power, created the conditions in which strong preferences for redistribution became embedded in effective redistributive social policy.

Social expenditures have received both an absolute and a relative increase in its share of resources. Until recently, the rise in tax/GDP ratio did not provoke public and political contestation, suggesting an underlying association with the social contract in Brazil. The recent public interest in tax and tax policy perhaps signals new tensions, and boundaries, in the social contract.

9. Labour market intuitions reduced earnings inequality

Not only have average earnings increased in Brazil, but they have increased most for groups of workers who used to earn the least. As the most important component of household income, the inequality in labour incomes reproduces the declining trends in household income. The Gini of labour incomes declined in Brazil from 0.54 to 0.41, a reduction of just below one quarter. Demographic and spatial factors, as well as informality jointly account for the bulk of the reduction in the Gini coefficient of labour incomes in Brazil. The decline in earnings inequality can be attributed to lower gender and race wage gaps, and to lower urban and regional wage premia.

10. There are limitations to the model

In the last few years, a variety of signals suggest the Brazilian model could be running against hard constraints. While the initial impact of the global financial crisis was muted, it arrived later through other channels: the slow-down of growth experienced by the Chinese economy and other emerging economies added to the fall in demand for commodities associated with recession and austerity in high income countries.

There is growing public concern with the incidence of taxation and the destination of government expenditure, which spilled over into opposition to the infrastructure investment associated with the 2014 World Cup. The eruption of popular protests in mid-2013, if nothing else, serves to underline the fact that Brazil's economic and social reforms are still very much a work in progress.

There's a strong case for further fiscal reform in Brazil, an area where the initial impetus of reform in the 1990s has notably slowed. In the field of infrastructure (a central issue in the 2013 demonstrations), sustained failure to finance and effectively regulate has led to significant deficiencies in transport and communications networks. There continues to be a strong public perception of graft and corruption, which generates resistance to sustained infrastructure planning and investment.

While there is a tightening of conditions in the policy environment, in some areas the model appears resilient. It is perhaps too early to assess whether the current conjuncture will lead to significant changes in Brazilian economic and social policy, and its aim to stimulate inclusive growth.

This briefing is based upon an IRIBA working paper 13 'Synthesis paper: Is there a new Brazilian model of development?' by Armando Barrientos and Ed Amann, available at: http://www.brazil4africa.org

IRIBA is a DFID funded research programme, based at the University of Manchester. It brings together an international team of researchers, examining how lessons from Brazil's development experience can be learned and adapted for African countries.

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