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Institutions for Macro Stability in Brazil: Inflation Targets and Fiscal Responsibility

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Abstract
Monetary and fiscal institutions have played a decisive role in the stabilisation of the Brazilian economy since the mid-1990s. Brazil's experience of designing and managing institutions to this end is likely to be of interest to other emerging and low- or middle-income economies. In Brazil institutional reforms were predominantly made in response to a succession of internal and, particularly, external crises. Indeed, perhaps nowhere in the world has inflation received as much attention from economists as in Brazil. The consequent accumulation of theoretical and practical knowledge resulted in a wealth of theories about the nature of Brazilian inflation. As such, the Brazilian experience offers many lessons to be learned, both in the sense of what could be done and what is better avoided.

When it abandoned the exchange rate anchor, Brazil was one of the first emerging economies to adopt a system of inflation targets. In the area of fiscal policy, a succession of institutional changes – from changes in the budget and management of the public debt to the fiscal adjustment of regional governments – culminated in the adoption of the Fiscal Responsibility Law shortly after the introduction of new monetary and exchange policies. However, consolidation of the new currency, the Real, and accelerated growth shortly after the turn of the century, followed by the global financial crisis, meant that the agenda of structural reforms was abandoned. New aspects were introduced to economic policy, such as a strong link between the growth of public debt and credit supply.

Recent stagnation, with repeated years of low growth, inflation pushing at the ceiling of its target, and primary surplus below its target, sets new challenges for the Brazilian economy.

Keywords
fiscal policy, monetary policy, Brazilian economy, institutions, macrostability, macroeconomics, Brazil, inflation, fiscal responsibility

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1. Introduction

Monetary and fiscal institutions have played a prominent role in the macroeconomic stabilisation of the Brazilian Real. The creation of the present currency in 1994 may be considered a watershed moment. Previously Brazil's was an economy marked by hyperinflation, one which had already undergone a moratorium on foreign debt and seizure of internal savings, and which suffered from a distinct lack of fiscal discipline. Following the introduction of the Real, Brazil's economy ultimately settled into controlled inflation and rebalanced foreign and public accounts. Table 1, below, summarises the development of the main macroeconomic variables in the period after stabilisation, during which economic policy has been founded on a tripod comprising systems of inflation targets, a floating exchange rate and responsible fiscal management.

Table 1: selected indicators during the period 1999-2013

Indicator	1999-2002	2003-2006	2007-2010	2011-2013	Average
SELIC (%)[1]	19,688	16,375	11,125	9,723	14,228
IPCA Variation (%)	8,768	6,433	5,145	6,083	6,607
GNP Real Variation (%) [2]	2,150	3,525	4,625	2,000	3,075
Primary Surplus (% GNP)	3,650	4,500	3,250	2,533	3,483
DLSP (%) GNP)[1]	52,475	50,275	41,325	35,167	44,810
Nominal Exchange Rate (R$/US$)[1]	2,398	2,500	1,875	2,083	2,214
Gross Fixed Capital Formation (% GNP)	16,450	15,950	18,550	18,967	17,479
Current account (% GNP)	-3,400	1,275	-1,328	-2,600	-1,513

Source: IPEADATA (primary surplus, DLSP, commercial balance, nominal exchange rate, EMBI Brazil and Exchange Reserves); IBGE (GNP and IPCA); Central Bank of Brazil (SELIC); and IMF (Current Account). Own draft.

(1) End of period DLSP = Public Sector Liquid Debt
(2) New series of Quarterly National Accounts, according to the method used in 2006 by the IBGE.

In light of this, the Brazilian experience is likely to be highly useful for assessing the importance of fiscal and monetary stability for the macroeconomy, in the sense both of understanding the recent history of Brazil's institutional changes, management of public and private finances, and policies for price stability, and of using insights from this to contribute to current discussions around future policy changes.

This paper aims to highlight the origins of the most notable features of current fiscal and monetary institutions in Brazil, and to analyse their impact on the recent development of Brazilian economic policy.[1] The paper mainly follows historical events chronologically. The argument is supported some monetary statistics included in the main text itself, and also by key fiscal statistics[2] set out in an annex at the end of the document.

The following section briefly places Brazilian macroeconomic institutions in historical context. Sections three and four offer more in-depth accounts of, respectively, monetary and fiscal institutions. Section five summarises the economic significance and contributions of, and main challenges facing, Brazil's current macroeconomic institutions.

2. Brief historical contextualisation of Brazil's macroeconomic institutions

Brazil is a huge, diverse, and complex country, and one whose society and economy was for a long time somewhat insulated from the rest of the world. As such, important developments in its fiscal and monetary institutions have tended to occur for internal reasons, and can be traced a long way back into the country's history.

Since independence in 1822 and the subsequent formation in the nineteenth century of first the Empire of Brazil and later the Republic, the political organisation of Brazil has taken the form of a federation in which the governments of the states have played a very important role, such as in the formation of basic infrastructure (they built and controlled the first great ports, railways and banks). Political cycles, alternating between dictatorial and democratic governments, had something of a pendulum effect on the extent of federal power, as Brazil swung between periods of fiscal and financial centralisation and decentralisation. Over the course of time, municipal governments gradually gained more and more influence in the federation,[3] to the point where they now occupy the position previously enjoyed by the state governments, controlling basic social expenditure, such as on education and health, as well as town planning.

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1 This essay focuses on the role of fiscal institutions; for a greater emphasis on the development of fiscal policy and public accounts, see Giambiagi (2009), among other authors.
2 This has attracted interest since the official fiscal indicators in Brazil, considered in the graphs and tables, are verified and published by the Central Bank of Brazil, with historical series available at: http://goo.gl/4MrrPN.
3 For a wide-ranging and updated view of fiscal federalism from different perspectives, see Serra and Afonso (2007a), among others.

The handling of government affairs and accounts also presents an interesting picture. An all-inclusive code of public accountability had already been introduced in 1920. Later, after a parliamentary initiative of 1950 and considerable debate, a basic budget act was published in 1964. This act arguably was revolutionary; expenditure began to be recorded on an accrual basis, a principle only adopted by governments of rich countries decades later. The act sought to integrate plan and budget, and to budget with financial and equity management, through the publication of differentiated and circumstantiated balances.

However, the value of this new and sophisticated budgeting and accounting system was eroded over time by a number of factors. Firstly, it suffered from the open exceptions by the governments of the military dictatorship, which went on to approve the budget proposal in parliament over a period of time, excluded the public debt and many budget expenses, and used state banks – even the central bank – to assume costs and reduce debts. Secondly, hyperinflation diminished the effects of the changes and of the equity positions themselves.

It is important to understand the context of the military government that came to power in Brazil in 1964 and which adopted a series of economic reforms that, in essence, lay the foundations for the institutions that have shaped the Brazilian macroeconomy up to the present day. Indeed, although designed under an exclusive political regime and for an economy largely sealed off from the outside world, it is curious how, almost half a century later, the foundations for Brazil's tax system, banking system and administrative system remain predominantly the same.

A dictatorship can use exceptional means – i.e. means not ordinarily available to democratic regimes – to impose reforms that reflect a technical ideal, even if they fail to meet the expectations of most of the population. Of course, this is not to say that dictatorship is the quickest or most efficient way to modernise institutions; it is merely to record the historical fact that in 1960s Brazil military governments took the opportunity to undertake genuine structural reforms to public finances, creating new and consistent institutions that were reasonably solid and close in form to those recommended by theory based on the experiences of other countries. These changes were motivated by national decisions (at that time, Brazil did not need help from, or monitoring by, multilateral bodies), albeit decisions originating with different people and interests. During the military dictatorship the reforms were, without question, in line with plans and strategies that had been designed in advance and implemented rigorously (even by force).

The 1960s was also a time of major institutional change related to monetary policy, with reforms having already begun in 1964. In that year, the Brazilian economy recorded the highest inflation rates in history, rising 25% in the first quarter alone (in terms of geometric progression an inflation of 144% a year). In this context, the Government Economic Action Plan (PAEG) was launched, with the aim of promoting stabilisation and a return to growth, and eliminating external restrictions on the Brazilian economy.

The fight against inflation had chronological priority over the other objectives of the Plan, not because monetary stability was more important than the objectives of growth and balance of payments, but because it would not be possible for the country to develop while on the brink of hyperinflation. The possibility of economic recovery, then, lay in inflation control, elimination of price distortions accumulated in the past, and in modernising capital markets, leading to increased savings.[4]

Following this logic, maintaining or increasing the Brazilian economy's capacity for savings was associated with the battle against inflation. Inflation had two main causes: (1) government spending, which was higher than the withdrawal of purchasing power of the private sector in the form of taxes on public loans; and (2) the disjuncture between the tendency to consume, resulting from the wage policy, and the tendency to invest, associated with the policy of expanding credit for companies. These inflationary pressures were compounded by monetary expansions.[5]

In light of this diagnosis of the causes of Brazilian inflation, anti-inflationary policy was based on three pillars: (1) containing government deficits of non-priority expenditure and rationalising the tax system; (2) limiting the rise in real wages to increases in productivity and acceleration of development; and (3) controlling credit policy to prevent the excesses of cost-push inflation and, at the same time, being realistic in order to adapt to it.

Another diagnosis of Brazil's economy offered by the PAEG was institutional strangulation, i.e. the presence of an institutional framework unfavourable to economic development, as

4 See Simonsen (1970).
5 For more on this, see Lara-Resende (1989).

revealed by the low real return of long-term financial assets (which discouraged public and private investment financing); the financial system's weakness; disorganised taxation; the propensity to public deficits; and employment legislation that discouraged job creation.

In order to overcome these barriers to development, three areas of institutional disarray – finance, taxation and the external sector – were identified as needing reform as a prerequisite for both stabilisation and economic growth.

In terms of monetary institutions, the financial reform implemented by the PAEG stands out. Its objective was to create mechanisms of long-term financing which avoided the inflationary financing of the public sector, and to allow the private sector to take back industrial investment so as to improve economic growth.

These objectives led to the adoption of important measures such as the creation of index linking, under which public debt was issued in National Treasury Re-adjustable Bonds (ORNT) and private securities came under the capital markets law. This guaranteed a real positive rate of return, protecting savers against inflation and encouraging saving. Compulsory saving mechanisms were also developed, and investment and financial banks, the Central Bank of Brazil (BCB) and the National Monetary Board were all created.

These measures restructured the national financial system and led to a resurgence in the market for public bonds. However, it introduced problems that later would lead to a great impasse in attempts to control the country's inflation, namely the index linking which adapted the economic system to high inflation and led to past inflation being projected into the future.

This had the effect that Brazil's status as an inflationary economy was acknowledged and tacitly accepted, allowing inflation-linking rules to be introduced and leading Brazilians to coexist peacefully with inflation. This index linking permeated all reforms, with the introduction of rules for exchange rate and salary corrections, financial asset protection and tax system adjustment.

As a result, both the structuring of the financial system, with the introduction of index linking and the formation of a market for public bonds, and the strategy of financing via indebtedness adopted by the state resulted in conditions that allowed inflation to take a seemingly automatic trajectory. In other words, that which seemed to give life to the economic system by allowing 'peaceful' co-existence with inflation in fact gave rise to a process that ended up immobilising it.

The formation of a new Brazilian tax system in the mid-sixties also followed historic steps to change the currency and credit. Based on research carried out by a technical commission formed before the 1964 coup, the new military government imposed approval of a new and genuinely revolutionary tax system in 1965. Brazil was a pioneer in introducing value added tax (VAT); indeed, it was the first continent-sized and federally organised country to adopt this tax on a national scale. However, Brazil today finds itself still paying for its original sin, while no other country has ever applied VAT in the same way. Brazilian VAT is determined under a physical credit system (to date Brazil ignores universal financial credit), restricted to the circulation of goods (initially it was not imposed on fuels and electricity) and, most seriously, delegated to state level. (Another form of VAT, limited to industrialised products (IPI) was implemented at the same time at federal level.)

The new system also consolidated income tax following the more modern standards of the rest of the world, and created a system of vertical distribution of tax receipts in favour of regional governments, which was logical and straightforward.

Based on indirect taxes, the system quickly responded well to the so-called economic miracle (based on increased consumption of durables) between the end of the 1960s and the mid-1970s. During this period, crucially, the tax burden grew in phases when the economic cycle was expanding. Federal centralisation was also efficient, at least in trying to direct regional expenditure and encourage investment, particularly in economic infrastructure.

After the mid-1970s oil crisis, the economy and tax burden stagnated and the government tried to compensate for losses by other federal bodies by encouraging borrowing, including from abroad. As fiscal functionality fell, political pressure mounted for gradual decentralisation; state governors became directly elected again, while the President of the Republic continued to be chosen indirectly. In this context, a huge and growing tax system reform movement was less concerned with changing taxes than with decentralising income, whether by increasing those collected directly by regional governments (which interested the governments of the wealthiest regions the most), or by redeeming and raising the percentage of federal funds intended for participation funds (which was favoured by governments of the poorer regions).

A similar process of reform also took place in public administration itself, including self-imposed reforms and bold changes: devolution (with many municipalities, foundations and funds), and decentralisation (with the two aforementioned spheres of regional governments).

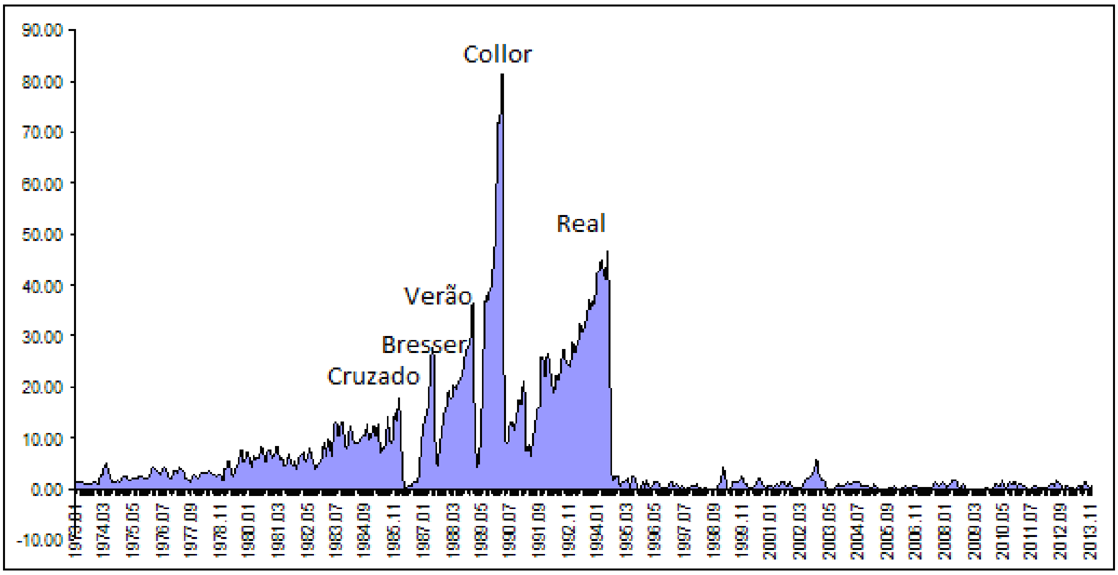
3. Monetary Institutions

3.1 Background to the Real Plan

Although inflation was relatively high in the period before the 1970s, it was largely kept under control thanks to gradualist inflation-control measures such as fiscal austerity, monetary, credit and salary contraction, and realignment of monitored prices.

The oil shocks of the 1970s (1973 and 1979) inaugurated a fresh outbreak of inflation in Brazil (see Figure 1, below), with growing indexing mechanisms allowing the Brazilian population to live with increasingly high rates of inflation. A wide variety of assets were indexed, including savings accounts, public debt, rental contracts and, from 1979, wages contracts as well. This indexing process reduced the uncertainties of agents with regards to the future economic environment, and lessened the pressures on internal interest rates.

Figure 1: Inflation in Brazil - monthly change of IGP-DI - 1974 to 2013



Source: IPGP-FGV (2014)

Inflation began to accelerate more sharply from the beginning of the 1980s. The decade was marked by the threat of an exchange rate crisis due to the second oil shock, the rise in international interest rates and the greater difficulty of obtaining outside resources. Given these conditions, Brazil was forced to seek a consubstantiated external adjustment through a standard internal demand-control policy.

A combination of factors – including internal recession, a drop in real wages, exchange rate devaluation, drops in oil prices and interest rates, and the recovery of the United States economy – helped to meet external accounts targets in 1983.[6] In this respect, the external adjustment of the Brazilian economy between 1981 and 1984 was highly successful in generating large commercial surpluses and rebalancing the balance of payments. However, the internal imbalances and, notably, the high inflation rates were treated with excessive tolerance and/or passive complacency.

In short, the external crisis of the 1980s compromised the standard of financing that had been maintained in the Brazilian economy since the reforms of 1964, and unleashed the process of accelerated inflation. The collapse of external financing made it necessary to establish commercial surpluses, making the need for public sector financing even greater in order to cover external liabilities. At that time, very particular relationships were established between exchange rate, fiscal and monetary policies. This was because the need to finance the balance of payments led to policies of exchange rate devaluations, which in turn extended the financial burdens of liabilities designated in dollars, leading to an escalation of the fiscal crisis. This situation also imposed limits on the control of monetary policy, since without obtaining the resources required in the payment of the external liabilities, the public sector depended on the placement of bonds and the growth of the monetary base. In turn, placing the personal property debt depended on the reliability and liquidity of public bonds, and also on the value of the interest required in appreciation of private capital.[7]

Under these conditions, inflation was taken not only at the value of the public deficit, but also on the conditions of fixed exchange and interest rates, which limited other prices in the economy and imposed an inflation ceiling. That being the case, breaking the link between fiscal, monetary and exchange rate policies depended on abandoning the active exchange

[6] See Carneiro and Modiano (1989).
[7] For a study of this period, see Lopreato (2002).

rate and interest policies, which would only be made possible by means of alternative conditions to enable the financing of the balance of payments and the restructuring of external public liabilities.

In view of these circumstances and the deep economic crisis that the country experienced throughout the period, the 1980s are often considered to be a 'lost decade' for the Brazilian economy. GDP had practically stagnated, even in years of great recession (1981: -4.3%; 1982: 0.8% and 1983: -2.9%). Inflation, even amidst weak economic development, had already accelerated significantly, reaching 100% per year in 1980, accelerating with the maximum exchange rate devaluation in 1983, and reaching 224% per year in 1984 (General Price Index - IGP).

By this point, it had become clear that the Brazilian economy's most salient problem was inflation, and it is in this context that debates about the causes of Brazilian inflation arose.[8] Having witnessed the ineffectiveness of the fiscal and monetary measures adopted to curb inflation – even when restrictive fiscal and monetary policies were implemented, inflation continued to accelerate – the theory that indexing the economy was an essential part of the problem of Brazilian inflation was gaining ground. This inertial inflation was a powerful mechanism for automatic retro-alignment of price increases in the economy, inasmuch as it enabled agents to incorporate past inflation into new contracts. This grew from inflation's inertial nature itself, as, in an indexed economy, the inflationary trend was based on the previous period's inflation, which was made worse by fluctuations from supply or demand shocks that were incorporated into the inflationary trend.[9]

As seen in Figure 1, the second half of the 1980s and the first half of the 1990s were marked by failed attempts to combat inflation: the Cruzado Plan in 1986, Bresser Plan in 1987, Verão Plan in 1989 and Collor Plan in 1990. Indeed, this period was characterised by grand experiments and theories regarding how to control inflation. These, along with their flaws, helped in drafting the Real Plan, a landmark that ended the almost decade-long cycle of failed attempts to combat inflation in Brazil.

[8] The causes of inflation and suggestions for stabilisation policy in Brazil were the subject of an intense debate between Brazilian economists; some major studies published on this topic include: Arida (1982 and 1986); Arida and Lara-Resende (1985a and 1985b); Bresser-Pereira (1981), Bresser-Pereira and Nakano (1984a and 1984b); Lara-Resende (1980 and 1985); Lopes (1976 and 1986); Modiano (1983); Rangel (1974) and Simonsen (1970).

[9] A classic work on this subject is by Lopes (1986).

It is worth noting that the 1980s also represented the decline of a growth model that had been in place in the Brazilian economy for almost 50 years, sometimes called the Import Substitution Model (MSI), based on a commitment to state-led growth.[10] This growth model had led to the "final stage" of industrialisation in Brazil, encompassing all sectors of industry in the country (although there was no internalisation of technical progress or development of an industry able to face international competition).[11]

The crisis of the 1980s, therefore, was not merely economic; it represented, in the form of the state fiscal-financial catastrophe, a crisis for the whole paradigm of development in place before then.

3.2 The Real Plan and its main institutions

It is against this background of a changed model of economic development that a programme of structural reform was adopted in Brazil in the 1990s, comprising government reform, new commercial and financial policy with a clear liberalising inclination, downsizing of the state apparatus, tax reform and a privatisation programme with extensive involvement from the financial system. This amounted to a process of structural change in the Brazilian economy, based on two main aspects in particular: reform of the state, and commercial and financial liberalisation.

With regards to the first aspect, the development model adopted by Brazil in the 1990s comprised major institutional changes amounting to a readjustment of the role of the state in the economy, which became very different from the role of the state during the MSI era. In the new model, the guarantee of government credibility became a requirement of the international market, since in an environment characterised by free movement of capital between countries, fiscal austerity policies become major indications of an economy's payment capacity.

[10] Castro (2011, p. 133) summarises the main features of the Import Substitution Model adopted in Brazil: 1) direct involvement by the state in providing economic infrastructure and in priority sectors; 2) high protection to national industry by means of tariff and non-tariff barriers, and 3) the supply of credit by the state for new investment projects. In addition to this, the author highlights three key roles of the state in this model: that of stimulating industrialisation by means of credit concession, exchange rate policy, tariff and non-tariff measures; that of the employer, aimed at removing the strangulation points of the economy; and that of the manager of scant exchange resources, preventing exchange rate crises resulting from a higher demand for foreign currency.

[11] Castro (1994) argues that, despite some inefficiencies inherent in the state-led industrialisation and development model adopted by Brazil, it had by the beginning of the 1980s created a complete and integrated industrial structure.

Meanwhile, the second aspect of structural change – the sweeping liberalisation that saw the opening up of the economy commercially and financially – served, together with privatisation, to guarantee the Brazilian government a supply of liquidity. This, along with the return of liquidity in the international arena, made abandoning exchange rate devaluation viable as economic policy, and was the essence of the price stabilisation policy in Brazil (as will be discussed later on).

This sets the scene for the Real Plan, a price stabilisation strategy implemented in Brazil in three distinct phases between May 1993 and January 1999. These phases can be summarised as follows: (1) short-term fiscal adjustment; (2) the de-indexing of the economy, and (3) the introduction of an exchange rate anchor.[12]

In the first phase, involving endorsing fiscal adjustment, the objective was to equalize budget imbalances in Brazil in the coming years, and thereby forestall inflationary pressures. The adjustment had three main features: reducing expenditure, increasing revenue, and reducing federal government transfers. The first and second features were included in the Immediate Action Programme (PAI), launched in May 1992, with the aim of reducing public spending, increasing tax-collection, combating tax evasion, redefining relations between Federal, States and the Municipal Governments, and strengthening the process of decentralisation. The third feature was based on the approval in February 1994 of the Emergency Social Fund (FSE), which was to be funded by 15% of all taxes collected in order that the federal government would not need to infringe the spending obligations established by the constitution of 1988. The importance of this fund – the reason for the label 'emergency' – lay in the fact that there were insufficient resources to finance social spending, meaning a risk of inflationary financing.

Authors making the case for fiscal adjustment tended to argue that inflation caused erosion of the budget and masked the public deficit.[13] With revenue indexed but expenditure not indexed there was a corrosion of government expenditure. Along with the management of the National Treasury, which sped up the release of budgetary items and corroded the real value of expenditure, this led to a reverse Tanzi effect in Brazil. This was because the increase in inflation, rather than reducing government income, reduced its real expenditure

[12] See Modenesi (2005).
[13] E.g. Bacha (1994).

and its deficit, meaning that the interruption of the inflationary process would lead to fiscal deterioration and therefore making fiscal adjustment a precondition for price stabilisation.

However, other authors argued that the link between public deficit and inflation could be refuted empirically as the good results of public accounts from 1990 to 1993 (which displayed a primary surplus in every year) did not inhibit inflationary acceleration.[14] Furthermore, the fiscal adjustment proposed by the Real Plan was not effective, with primary results of 0.24% of GNP in 1995; 0.9% in 1996; -0.88 in 1997 and 0.01% in 1998, although the absence of this adjustment did not stop a fall in inflation in this period. The fact that the public deficit was not at the root of the inflationary process does not mean to say, however, that the Brazilian fiscal situation was not problematic, or even that outside investors' lowered expectations was not partly a result of this.[15]

The second stage of the Real Plan sought to eliminate inflationary inertia and align the economy's relative prices. As discussed in the previous section, the indexing system on the one hand eased the effects of inflation on the economy, making it possible for economic agents to coexist for a long time with high inflation rates in Brazil, but on the other hand made it more difficult to stop inflation, because of the great weight of its inertial nature. Stopping inflation therefore turned into combating inertial inflation, which had to be prevented as a precondition for monetary policy to be effective again. A further preoccupation in the second stage of the Plan was the realignment of prices. A wide array of relative prices existed as a result of differences in the periods when they were readjusted. This meant that in the event of a sudden drop in inflation, problems would arise linked to the distribution conflict involved in the transfer of income from agents whose contracts were phased out to agents whose contracts were readjusted. Stopping the process of inflation therefore needed to happen in a neutral way, with alignment of all prices and incomes on the same date and by means of an indexer which would be the same for all.

The Real Value Unit (URV) was set up in March 1994 in order to align relative prices and co-ordinate inflationary expectations. It consisted of an account unit indexed by the average of three inflation indexes: the General Market Price Index (IGP-M) of the Getúlio Vargas Foundation (FGV), the Extensive Consumer Price Index (ICPA) of the Brazilian Geography

[14] Lopreato (2002).
[15] Castro (2011).

and Statistics Institute (IBGE) and the Consumer Price Index (IPC) of the Economic Research Institute Foundation (FIPE). In addition to this, the market – in order to increase its credibility in relation to the URV – went on to have one-to-one parity with the dollar. The URV was launched on 1st March, 1994 against the backdrop of all these factors, and remained in place until 30th June of the same year, when it was jettisoned in order to convert to the new currency – the Real – on 1st July. On that date, as summarised by Modenesi (2005), the redenomination of the monetary stock, the changing of all the currency in circulation in the country and the conversion of contracts still drawn in terms of cruzeiros reais were made at a rate of 1 Real = 2,750.00 Cruzeiros Reais, which was the URV value at 30th June, 1994.

At the same time as the URV was created, the Brazilian Central Bank took action on the exchange market, selling all dollars at the URV/dollar parity of one-to-one, creating an asymmetrical exchange band in Brazil with a ceiling of 1. In order to do this, the Central Bank held US$ 40 billion in international reserves. It is important to stress that the exchange rate was not fixed, but both the National Monetary Council (CMN) and the Central Bank had very strict instructions regarding the need to maintain the exchange rate's upper limit.

The third phase of the Real Plan encompassed the period July 1994 to January 1999. It saw firstly the adoption of a system of monetary targets and later the replacement of this with a system of exchange rate targets.

As the new currency began to circulate, Brazil chose to adopt a system of monetary targets comprising the following measures: (1) adopting targets for the monetary base, which could only be changed by 20% and by the CMN; (2) weighting the monetary base in international reserves; (3) setting up a fixed parity between the Real and the US dollar, and (4) changing the CMN with regards to its composition and the transfer of its authority to issue currency to the national congress.

However, this new policy did not have the expected results. This was because for the system of monetary targets to be successful the currency had to be circulating at a stable speed, but with the inflationary process interrupted the Brazilian currency recovered its traditional functions of value reserve, means of exchange and account unit, which led to an increase in demand for Real stock. This involved severing the relationship between monetary stocks and price levels, creating difficulties for the Central Bank when it came to determining the amount of currency supply compatible with price stability, and caused the system of monetary targets to fail in Brazil.

With the system of monetary targets abandoned, the system of exchange rate targets took its place – a system which could be said to constitute the essence of the process of price stabilisation in Brazil. The use of exchange as an anchor for monetary policy was possible due to the economic liberalisation entailed in the structural reforms of the 1990s and the measures used to overvalue the exchange rate. This set of policies meant that Brazilian imports were relatively cheaper than domestic production, which meant an increase in external competition and collective demand shifting in favour of imported products. This in turn exerted less pressure on internal prices and restricted the domestic production sector's ability to shape prices and co-ordinate inflationary expectations.

The revalued exchange rate policy altered the framework (mentioned above) of relationships between exchange, fiscal and monetary policies in place during the previous period. This policy made it possible to reduce uncertainty over the behaviour of basic prices in the economy, as economic agents could now form expectations based on a predictable exchange rate.

Besides the exchange anchor, monetary and fiscal policies were also used to reduce exchange rate uncertainties. Guarantees had to be offered to attract capital to finance possible balance of payments imbalances, which would in turn ensure that there were no unmet expectations for capital investors which could result in capital flight and problems in the price stability strategy being adopted. As well as high interest rates, the reforms of the 1990s – i.e. privatisation and commercial and financial liberalisation – helped to attract outside capital to Brazil.[16]

Most of this capital was seeking a return from public bonds, with interest rates set to meet foreign economic agents' expectations, and guaranteed by the Brazilian government. This meant that public finance had to accommodate the costs of the exchange and interest policies and prevent situations that could risk capital flight.

With regards to monetary policy, high interest rates throughout the period 1994-8 served as another anchor on prices, and at some points were more important than the exchange

[16] See Lopreato (2002).

anchor itself, which, by virtue of its changed nature by the end of that period, lost its capacity to act as a price anchor.[17]

As such, the system of exchange rate targets was highly successful in reversing the process of severe and chronic inflation that had devastated the Brazilian economy. However, after going through the financial turbulence caused by the Mexican crisis in 1995, the Asian crisis in 1997, and the Russian crisis in 1998, Brazil abandoned its fixed exchange rate system due to speculative attacks that reduced foreign reserves. The system of exchange rate targets was replaced by the system of inflation targets, marking the beginning of a new phase in the stabilisation process in Brazil, and the end of the Real Plan.[18]

To summarise the outcome of this period, then, it is notable that the macroeconomic system at the time, characterised by high interest rates, an overvalued currency and a rising trend in public debt, was efficient in controlling prices, despite the adverse effects on the real economy in terms of reduced economic growth, deficit in the balance of payments and growth of public debt.

To illustrate macroeconomic behaviour during the Real Plan years, Table 2 (below) traces selected indicators for the period 1994-98.

Table 2: Selected indicators in the period 1994-98

Indicator	1994	1995	1996	1997	1998
Growth of GNP (% p.a.)	5.3	4.4	2.2	3.4	0.0
Gross Fixed Capital Formation (% GNP)	20.7	18.3	16.9	17.4	17.0
Inflation (% p.a.)	2,075.827	66,008	15.757	6.926	3.196
Balance in current transaction	-0.308	-2.388	-2.734	-3.477	-3.944
International reserves (US$ millions)	38,806	51,840	60,110	52,173	44,546
Interest rate	__	53.09	27.41	24.78	28.79
Real exchange rate/dollar	0.64	0.92	1.01	1.08	1.16
Primary surplus	5.2	0.2	-0.1	0.9	0.0
Liquid public sector debt (% GNP)	30.0	28.0	30.7	31.8	38.9

Source: IPEADATA (2014), IMF (2014) and BCB (2014)

[17] For more on this, see Castro (2011).
[18] Modenesi (2005).

As these indicators suggest, the Real Plan was a highly successful experiment in stabilisation for the Brazilian economy. In the period following 1994 inflation fell significantly and stayed at this level.

However, this price stability was achieved through relatively high interest rates and an overvalued exchange rate. With regards to the interest rate, while high level rates served to attract outside capital and to finance the balance of payments – helping with the strategy of sustaining high exchange rates – they also increased the proportion of public debt indexed to them, causing this variable's trajectory to increase at the same time. The overvalued exchange rate, meanwhile, brought problems for the balance of payments in current account transactions, as demonstrated by successive growing deficits, which also contributed to the declining trend of foreign reserves from 1996.

One further result of the price stability policy was weak economic growth. During the 1990s, the performance of GDP was somewhat irregular; in the early years of the decade – a period of high inflation – GDP showed negative growth (4.3% in 1990; 1.0% in 1991 and -0.5% in 1992), increasing again with the introduction of the Real Plan and after the currency stabilised. The return of growth, however, was only at decreased rates, reflecting the difficulties of resuming investment on poorly maintained bases. As the next section will mention, it was only from the mid-2000s that GDP grew more significantly.

3.3 The inflation targets system

The Brazilian exchange rate crisis in January 1999 resulted in a major devaluation of the Real against the US dollar, seeing it fall from a rate of 1.20 in December 1998 to 1.98 in January 1999. Initially, the policy adopted by the Brazilian government was to suddenly increase the basic interest rate in an attempt to counter the fall in the exchange rate and avoid a return to inflation.

After the stabilisation of the exchange rate in the middle of 1999, the government announced that it would adopt an inflation target system. Opting for a floating exchange rate system meant that the exchange rate had to be replaced as the anchor of monetary policy and another variable adopted instead to coordinate market expectations and control inflation in this new context.[19]

This period was marked by a three-fold change in the macroeconomic system in force up until then: the monetary system of exchange rate targets was replaced by an inflation target system, the system of semi-fixed exchange rates gave way to a managed floating exchange rate, and the fiscal system began to pursue primary surplus targets. This change became known as the Brazilian macroeconomic tripod. Each aspect is discussed in turn below.

Firstly, the system of inflation targets adopted in 1999 in Brazil can be summarised as follows: (1) inflation targets are represented by annual changes in a general price index; (2) targets and their respective tolerance intervals are fixed by the National Monetary Council (CMN) based on a proposal from the Ministry of Finance; (3) targets and their related tolerance intervals are fixed for two years; (4) the Central Bank of Brazil is responsible for carrying out the policies necessary to meet these targets; (5) a target is considered to have been met when the accumulated variation of inflation, measured by the price index adopted for the January to December period of each calendar year, is within its respective tolerance interval; (6) when a target is not met, the Chairman of the Central Bank must publish, by means of an open letter to the Minister of Finance, a detailed description of the causes of the failure, the steps to ensure that inflation returns to the set levels, and the period in which the steps are expected to produce results; (7) the Central Bank of Brazil must publish, by the last day of each calendar quarter, an inflation report covering the performance of the inflation targets systems, the outcomes of monetary policy decisions taken, and an inflation forecast.[20]

The instrument of monetary policy chosen by the Monetary Policy Committee (Copom) to meet inflation targets was the short-term interest rate known as the SELIC rate. SELIC is the rate used as a benchmark for interest in the Brazilian economy; it sets the boundaries of the reserve exchanges between financial institutions and is considered by the market to be the main indicator of the government's monetary policy. This rate safeguards all the issued bonds of the Central Bank of Brazil, the National Treasury, and various states and

[19] See Barbosa Filho (2006).
[20] That specification of the goals system can be found in Bogdansky et al. (2000).

municipalities, as well as inter-financial deposits held by many banks with a commercial portfolio, commercial banks and savings banks.

Under the system of inflation targets, inflation is fundamentally controlled by fixing the basic interest rate at a level that is compatible with the inflationary target set by the CMN. Copom is made up of the management of the Central Bank and meets every 45 days to set the interest rate it considers appropriate in order to meet the inflation target.

An important feature of the System of Inflation Targets is its high level of transparency; besides the Inflation Reports, the minutes of Copom meetings are also published, as well as press releases and different studies on the management and direction of monetary policy in Brazil. The aim of these mechanisms is to give credibility to the monetary authority's actions and interventions in the country's economy.

When adopting the inflation targets system, the CMN decided to use the Extensive Consumer Price Index (IPCA) calculated by the IBGE as a benchmark for monetary policy. Every month the IPCA selects the prices from a basket of goods and services identified in the Family Budget Research Study (POF), taking as its target population families whose monthly earnings are equivalent to between 1 and 40 minimum wages, living in the urban areas of Belém, Fortaleza, Recife, Salvador, Belo Horizonte, Rio de Janeiro, São Paulo and Porto Alegre, Brasília and Goiânia. It is noteworthy that Brazil uses the "full" index of the IPCA unlike other countries which use either a purged index of prices with a high sensitivity to supply shocks such as in food and energy, or prices fixed by the government.

The second feature of the Brazilian macroeconomic 'tripod' is the shift from a system of semi-fixed exchange rates to a managed floating exchange rate. Although price control was no longer the responsibility of the exchange rate (as with the exchange rate anchor system), figures showed that exchange rate variations brought about by changes in the Brazilian basic interest rate appear to be the main mechanisms for transmitting monetary policy to inflation. It is notable that, by adopting the floating exchange rate, the Central Bank of Brazil regained control of monetary policy and the exchange rate became the variable responsible for absorbing external shocks.

The third aspect concerns fiscal policy. After the signing of two agreements with the International Monetary Fund at the end of the 1990s, Brazil put in place a fiscal system with targets for the primary surplus, with the aim of maintaining public debt stability and giving the government credibility, thus enabling it to reduce the interest rate paid on public borrowing at a later date.

In this arrangement, there were relatively important links between fiscal, monetary and exchange rate policies. Primarily, the monetary market, controlled by the system of inflation targets, influenced the debt market via bonds known as National Treasury Financial Securities (LFT), indexed to the SELIC interest rate (the instrument of monetary policy). This being so, when the SELIC rate was high to counter inflationary problems, it had an impact on the growth in public debt, since a large part of this debt was remunerated based on SELIC.

In addition, the high interest rate amplified the differential between Brazilian and outside foreign rates, and meant that capital seeking higher returns was attracted to the Brazilian economy, which, with a floating exchange rate system, contributed to the appreciation in value of the national currency.

Under this new framework, the other macroeconomic policies were subordinate to price control via monetary policy, responding passively to its decisions.

Moving on to the performance of the Brazilian economy under the inflation target system, it is notable that the Central Bank of Brazil met the inflation targets put forward (except for in 2001, 2002 and 2003), indicating that the system can be considered highly successful in controlling price levels. The fact that the country has experienced a long period of chronic high inflation contributes to this outcome being seen as a major success for the Brazilian economy, although the associated costs of this price stabilisation policy must also be assessed.

The evolution of prices can be seen in Table 3, below, which shows the history of inflation targets in Brazil, showing the exact target, the tolerance interval for inflation fluctuation, and the real rate of inflation as measured by the IPCA.

Table 3: History of Inflation Targets in Brazil (1999-2013)

Year	Regulation	Goal (%)	Band (p.p.)	Lower and Upper Limits (%)	Effective Inflation (IPCA % p.a.)
1999	Decision 2,615	8	2	6-10	8.94
2000	Decision 2,615	6	2	4-8	5.97
2001	Decision 2,615	4	2	2-6	7.67
2002	Decision 2,744	3.5	2	1.5-5.5	12.53
2003[1]	Decision 2,842 Decision 2,972	3.25 4	2 2.5	1.25-5.25 1.5-6.5	9.30
2004[1]	Decision 2,842 Decision 3,108	3.75 5.5	2.5 2,.5	1.25-6.25 3-8	7.60
2005	Decision 3,108	4.5	2,5	2-7	5.69
2006	Decision 3,210	4.5	2	2.5-6.5	3.14
2007	Decision 3,291	4.5	2	2.5-6.5	4.46
2008	Decision 3,378	4.5	2	2.5-6.5	5.90
2009	Decision 3,463	4.5	2	2.5-6.5	4.31
2010	Decision 3,584	4.5	2	2.5-6.5	5.91
2011	Decision 3,748	4.5	2	2.5-6.5	6.50
2012	Decision 3,880	4.5	2	2.5-6.5	5.84
2013	Decision 3,991	4.5	2	2.5-6.5	5.91

Source: Central Bank of Brazil.

(1) The Open Letter of 21/1/2003 set out adjusted goals of 8.5% for 2003 and 5.5% for 2004.

As the table shows, in the period 1999-2013 inflation was outside the set tolerance interval in three years, namely 2001, 2002 and 2003. In those three years, several external and domestic shocks – such as the energy crisis, the effects of the 11th September 2001 terrorist attacks, the Argentinian crisis, and the crisis of confidence in relation to the presidential elections in 2002 – affected the Brazilian economy, with a significant impact on inflation. The mandatory open letters of the Chairman of the BCB during these years point to exchange rate devaluation as the main reason the targets were not met. In 2001, 38% of the increase in the inflation rate was explained by currency devaluation, while in 2002 the exchange rate's contribution to inflation was 46%. The high inflation of 2003 was explained by inflationary inertia, resulting from the pressure on prices occurring in the previous year.

In all the other years the inflation targets were met, and the high interest rates were the instrument used to meet them. Meanwhile currency appreciation was not simply an unwanted by-product of the monetary policy, but rather the essence of that price-control strategy, as became clear in the years when the inflation targets were not met.

Among the consequences of the price control policy for the real economy, it is notable that high interest rates were identified as one of the main reasons for low Brazilian GDP growth when compared to other emerging countries. Real GDP grew by around 3% on average in this period, considerably lower than countries like China and India, which grew at rates of 9.9% and 7.02% a year respectively between 1999 and 2013.

The exchange rate also displayed a rising trend, because (as mentioned above) the high differential between domestic and foreign interest rates contributed to a substantial inflow of foreign capital and a consequent appreciation in Brazil's currency. Despite the benefits of this strategy for price control, this currency appreciation discouraged exports and encouraged imports, causing current account deficits in the balance of payments. This limited growth and made financing the balance of payments dependent upon attracting short-term, speculative capital.

Lastly, in relation to public accounts, despite successive positive primary results, net borrowing grew in the public sector when compared with the period 1994-8, something that is largely the result of expenditure tied to payment of public debt interest. As explained above, this is because the return on LFTs was linked to SELIC at high levels, which resulted in a high financial cost for the Brazilian economy.

In light of the associated costs of the price control policy, in particular the high interest rates put in place by the monetary authority, some authors have put forward theories to explain Brazil's high interest rate. These theories range from the reduced efficiency of Brazilian monetary policy to a pro-conservative consensus in the Brazilian Central Bank, multiple interest rate balances, the fragility of public accounts or jurisdictional uncertainty.[21] Another explanation sometimes offered for high interest rates in Brazil on the market side is the lack of independence of the central bank which, in order to be credible, must offer high rates of return for investors.[22] However, a theoretical weakness of this thesis is that increased

[21] Modenesi and Modenesi (2012).
[22] See Barbosa-Filho (2006).

independence of the Central Bank could risk compromising coordination between fiscal and monetary policies.

In order to alleviate the macroeconomic restrictions imposed on the Brazilian economy by high interest rates, some authors suggest a more flexible system of inflation targets, such as adopting a longer convergence period for the targets (18 to 24 months), using core inflation (instead of the wider index), and including economic growth as one of the explicit goals of monetary policy.[23]

4. Fiscal Institutions

If, at the risk of being simplistic, one were to summarise in one sentence the overall state of fiscal institutions in Brazil, one might say that they reproduce the contradiction which so defines the Brazilian economy and Brazilian society itself.

One the one hand, Brazil boasts instruments and practices which are among the most advanced in the world and are recognised by international bodies. Although some reforms have been abandoned or forgotten in recent years, the country still has a sophisticated and well-organised process of budgeting, taxation, and financial management, including for debt and equity. This sits in the midst of a wide-reaching and rich democracy, with a decentralised federation both *de jure* and *de facto*.[24]

One the other hand, there are delays and setbacks which are increasing. Disregarding the advanced public accounting system, Brazil's main fiscal indicators are still collected from bank statistics, as they have been since the 1980s. Recently, the country resorted to a series of devices which damaged the credibility of both the authorities and of fiscal policy, with the market and ratings agencies setting higher and higher primary surplus and principal targets, in order that the results be presented in a realistic fashion.

It is worth mentioning at this point the level of prominence given to taxation throughout the following analysis. This is not a flaw of analysis; rather, it reflects the perception that the persistent increase in the Brazilian tax burden was the decisive variable in making the fiscal adjustment viable in the country during different economic circumstances. It is rare indeed for a peacetime economy to have succeeded in increasing its levels of taxation to such a

[23] Oreiro et al. (2012).
[24] See Rezende and Afonso (2006) and Serra and Afonso (2007a), among others.

degree. (The graph below shows its post-war development; although taxation barely reached 20% of GDP before the tax reform of the sixties, it was already at 27% of GDP when the Real was introduced in 1995, and reached a record of 37.4% of GDP in 2013.) Decades ago taxation in Brazil was much higher than the average for emerging economies, and several years ago it reached and surpassed the average for advanced economies. The most remarkable thing is that the national tax revenue grew in relation to GDP until the latter slowed down or declined (Figure 2, below, shows this post-Real development).

Figure 2: Overall post-war gross tax burden: 1947-2013 (in % of GDP)

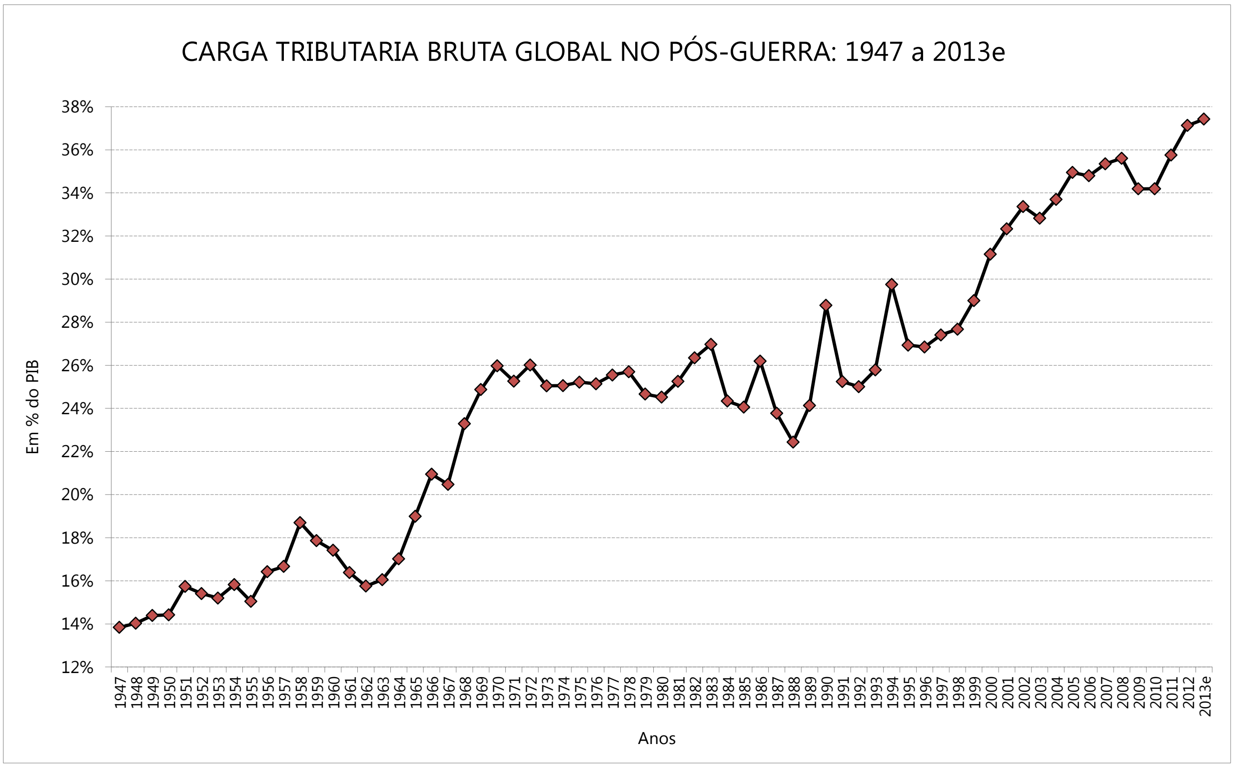
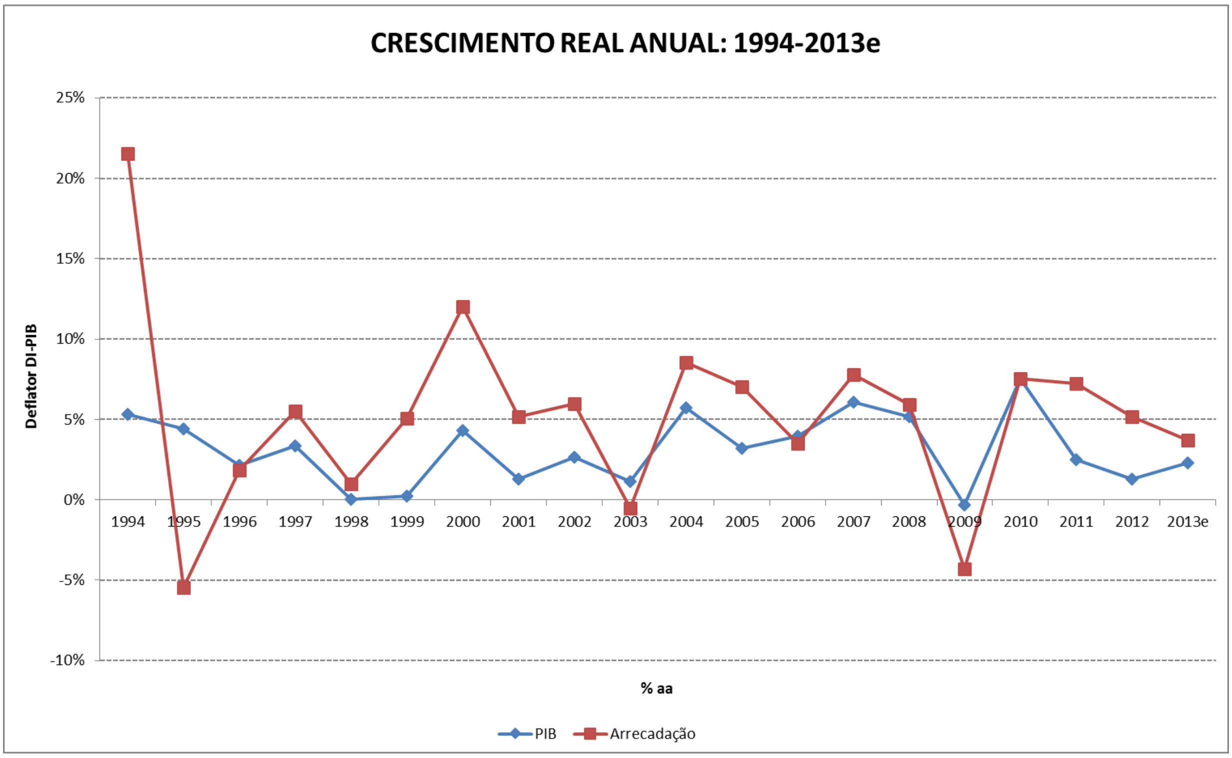


Figure 3: Yearly Real growth, 1994-2013. DI-GNP deflator % per year GDP Tax collection



Successfully increasing the tax burden meant that there was never a need for a plan to improve discipline or control over public spending, much less to reduce it.[25] Reform of public spending is generally a topic simply ignored in official speeches and even in analyses, while changes in social security is a frequent topic for detailed discussion. It was not by chance that the government's primary expenditure alone jumped from 13.7% to 23% of GDP between 1991 and 2013. Even when investors in public debt demanded changes to ensure that the debt service was fulfilled, they almost always wagered or requested an increase in the tax burden rather than a reduction in primary spending.

4.1. Democratic Cycle of Fiscal Reforms

The country's return to democracy in the mid-eighties did not hinder institutional reforms, and even led to a new cycle of them. While these sometimes lacked technical consistency, they had the advantage of being drawn up in a political environment where they were more likely to gain national approval.

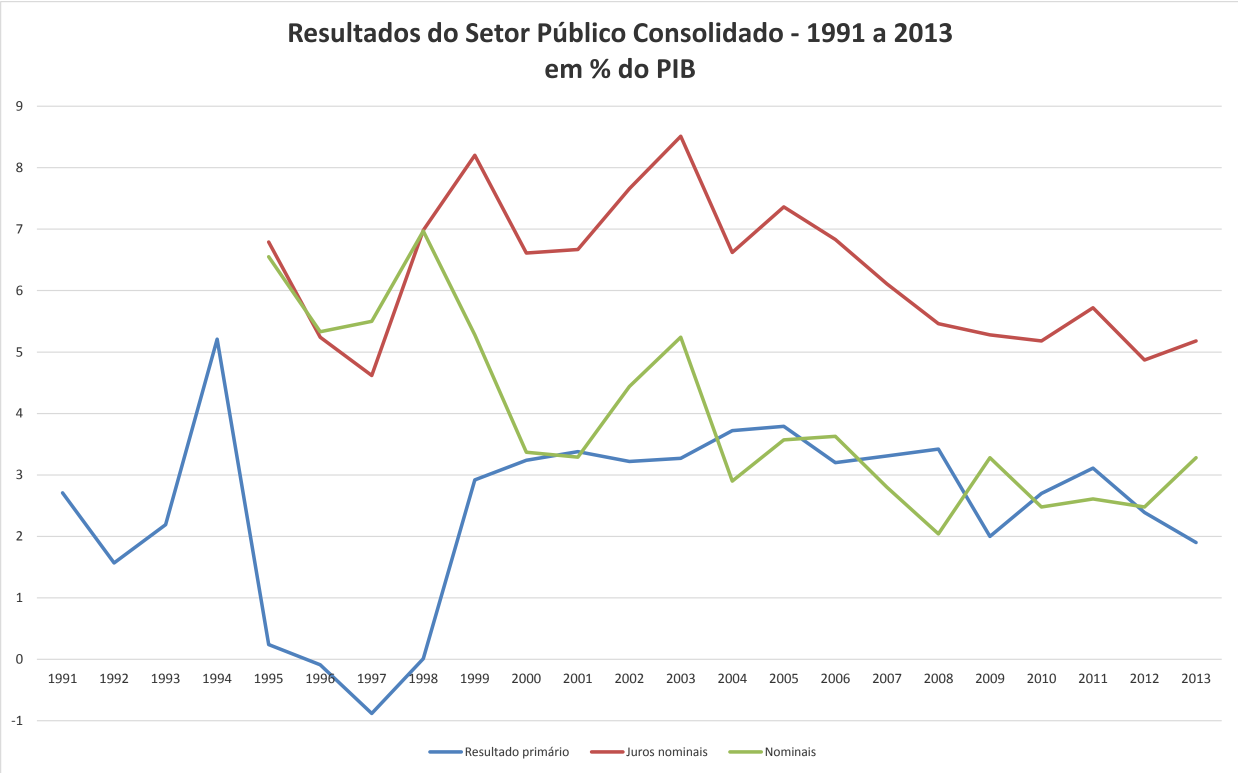
[25] One of the rare recent works to deal solely with public spending and its efficiency is Brunet, Berté and Borges (2012).

One milestone in the political process was the Constitution of October 1988, approved by an assembly made up of members of congress directly elected for this specific duty. During its implementation, the president defined the tax reform proposed at that time as the fiscal arm of re-democratisation, because the emphasis was on weakening the revenue of the central government in exchange for strengthening that of regional governments, particularly those of the less developed regions, to the detriment of the advanced ones – in other words, decentralised (vertical) and regional (horizontal) shares of income. This political logic is still present today in debates on the tax system and possible new reforms.

Even before the new constitution, a huge process of decentralisation of both taxation and finance had already begun; from the start of the eighties, the federal government transferred increasing portions of income tax (IR) and tax on industrialised products (PI) to the participation funds of the regional governments and, in particular, those states regained some autonomy in managing their main tax on the circulation of goods (ICM). The new constitution deepened decentralisation, but did not go as far as setting up a new tax system.

Macroeconomic fiscal management also saw structural change. By the mid-eighties there was a consensus among analysts that lack of fiscal discipline was a striking and permanent feature of the country. The deficit, nominal and also primary, was a constant factor that was difficult to measure correctly, because the Brazilian government has always been heavily de-concentrated and decentralised, and in particular because the monetary authorities and even public banks issued debt and carried out spending in the name of the Treasury – both at a national and state level (they were all owners of commercial and even development banks). Figure 4, below, shows the clear improvement in the trend of large fiscal flows since the nineties, with a growing primary surplus, inverse development of nominal rates and consequent reduction in nominal deficit for the public sector (including all state companies at the turn of the century). The post-Real period is marked by clear fiscal adjustment to the inevitable (historically) gentler deterioration from 2009, along with the inevitable contagion in the face of the global financial crisis.

Figure 4: Results of the Consolidated Public Sector – 1001 to 2013 in % of GDP



(Primary Results | Nominal rates | Nominals)

The regional governments have always played an important role in the fiscal history of the Brazilian federation.[26] Since its creation, they have experienced different cycles of accelerated borrowing, including from abroad, which very often resulted in moratoria and, inevitably, in these debts being assumed by the national government. This does not mean that the federal government had a much better track record in fiscal discipline, as it has never had any limiting conditions imposed on its borrowing capacity, internal or external – not to mention that for decades monetary authorities could issue and place bonds, as well as the fiscal transactions carried out through some official federal banks.

The historical trend towards fiscal indiscipline began to change in the mid-1980s, when a long cycle of in-depth reforms of fiscal institutions began, lasting until the end of the century.[27]

The creation of the Secretary of the National Treasury (STN) under the Ministry of Finance in the mid-eighties can be viewed as the starting point of this shift. Concerned about

[26] See, among others, World Bank (2008).
[27] For an analysis of the long-term development of Brazilian fiscal policy, which also details series of historical statistics, it is essential to see Giambiagi (2008) and Jaloretto (2009).

modernising fiscal management and improving knowledge and, therefore, control of the public accounts, the government decided to withdraw all government functions that were previously exercised by the central bank and state banks, in particular the Bank of Brazil.

The so-called monetary budget was thereby extinct, which, in practice, was the mechanism which allowed those organisations to assume commitments which were not recorded in the budget and which were not even registered in the Union's balances, such as buying regulatory stocks, granting subsidies and financings and – most importantly – issuing and serving the public debt. The most striking feature of that process was the creation of the single National Treasury account – centralising all accounts, making them available and depositing them in the central bank itself – and the transfer of all debt management, which previously was carried out by the central bank, which went on to operate purely for the purposes of complying with monetary policy.[28]

The Constitution that was announced in October 1988 brought with it greater advances towards fiscal stabilisation. Most importantly, it enshrined the country's full re-democratisation. The result, in large part, was that legislative power assumed an important role in the life of the nation. This was particularly so because, during much of the Constitutional Assembly's work, the political system was organised as a parliamentary one, with the presidential system in place only at the last stage of that assembly.

Parliament continued to reproduce and to formalise through legislation the duality which defines the Brazilian fiscal scene. This began in the Constitution itself.

One could argue that the constitution helped reform in that within the tax system, it pushed through substantial decentralisation and created new contributions bands which would later enable the tax burden to increase. In the budget, it modernised the system with three new legal requirements: a multiannual plan, budgetary guidelines and an annual budget. In the area of financial regulations, it made it constitutional to prohibit the central bank from financing governments and opened the way for a national law to later be drawn up on fiscal responsibility, which also applied to regional governments.

[28] For an analysis on the organisation and management of the Brazilian public debt, see Silva, Carvalho and Medeiros (2009).

However, the same constitutional assembly also opted for a number of fiscally detrimental measures. It gave stability to public service companies, including those contracted without an invitation to tender. It offered amnesty to those who had taken out official loans and even tried to peg the real interest, reinventing the crime of usury. It expanded the size of the judiciary, the legislative body, and the federation itself, creating new bodies and states, and in the same vein set up and increased benefits and social services, without a clear source of funding.

Despite the process of reform, the creation of the Real[29] in the middle of 1994 did not bring with it more broad fiscal changes. A few months before the currency change, a plan of action with several fiscal austerity measures had in fact been put together, but was never implemented. Up until then, there was very little political propensity for austerity in the public accounts (not even given the political currents of a more conservative or liberal parliament that in Brazil, unlike richer countries, also argued for more measures to loosen fiscal control).[30]

The Real Plan was accompanied by only two fiscal measures, but they played a secondary role in the stabilisation process.

Firstly, even before the Plan was drawn up, there was a yet more temporary – and low quality, by the lights of taxation theory – tax innovation taken from the macro plan. This was the creation of a tax on financial transactions (known as the cheque tax), which was charged for a year in 1994. Rather than helping to increase federal tax revenue in the year the Real was created, it served as an experiment in tax collection that would be recreated later, on the pretext of being a temporary social contribution to finance the public health system.

Secondly, within the Real Plan itself, the only fiscal innovation was a release of tax revenue; a fifth of the revenue from taxes or contributions would be set aside in a fund, initially called an emergency fund, then a social fund and then a stabilisation fund, to be allocated freely in the budget, regardless of the original obligation. This paved the way for assigning a larger portion of tax revenue to cover interest on debt.

[29] For further details of the idea behind the Real Plan, see Franco (2000).

[30] Thus, for example, in the Constitutional Assembly of 1987/88, the more right-wing members of parliament allied themselves with the more left-wing ones to approve stability for public service companies, even if they were not accepted through invitations to tender; amnesty in official loans, particularly for rural farmers, and also the pegging of real interest at 12% pa and the crime of usury.

Even so, it is strange that the first few years following the creation of the new currency were marked by high and increasing deficit and debt, even given the effects of the very high basic real interest rate. The cheque tax was temporary and taking it out of the budget in practice basically only meant that the contributions collected to finance social security as a whole were also used to finance the payroll of inactive dependents of the Union. In other words, wages, profits and turnover were taxed in order to meet the cost of financing social spending for all, but, following the decoupling of spending obligations, they ended up financing spending on public servants, which should be accounted for by the traditional fiscal budget.[31] But, indirectly, by releasing tax-free resources previously spent on personnel costs, they could attend to the service of the public debt. Through this process, efforts to implement fiscal adjustment were advanced indirectly and even covertly.

With the introduction of the new currency from June 1994, an extremely aggressive monetary policy had to be adopted, applying real interest to the stratospheric rates, in order to compensate for the lack of a previous fiscal adjustment or a significant contribution from the accounts in the immediate post-stabilisation period. Monetary policy exercising a monopoly on macroeconomic policy was not new to Brazil, and caused a repeat of failed, previously attempted plans.

Shortly after the creation of the Real, as mentioned above, economic policy was forced to resort to the exchange anchor in an attempt to control prices and rates. The exchange rate was fixed for some years, even in the face of residual inflation, and when this caused a greater imbalance in external accounts, the system was initially made flexible but without stopping the bleeding.

For some, the predominance of the exchange rate resulted from the weakness of other facets of economic policy, in particular fiscal policy. Apart from the monitoring of general fiscal targets remaining from agreements with the IMF in the early 1980s, there was no organised system for formulating and, in particular, effectively generating primary surpluses that would be sufficient to serve the debt and keep it under control, sustainable both in proportion to gross domestic product (GDP), and below a top-limit ceiling.

[31] For a discussion on social cohesion and security costing, see Serra and Afonso (2007b).

If on the one hand worse fiscal results were recorded in the first years of the Real than those prior to the creation of the currency, with even the public sector recording a primary deficit,[32] on the other hand, some crucial institutional changes were made at the time to improve the long-term state of public finances.

The second half of the 1990s saw a number of legal changes (including through constitutional amendments) which, firstly, did not form part of, or result from, an organised plan (they were individual and mutually exclusive measures) and, secondly, which followed a course parallel to the circumstances at the time (they were not formulated because of a primary deficit). In general, it is inevitable that changes to fiscal instruments end up having practical and political effects but again, this can only be seen in the medium and long term.

Among other changes at the end of the last century, one could mention the privatisation of strategic sectors of the economy, the renegotiation or rolling on of regional governments' debts which were assumed by the National Treasury, tax legislation regulating the state ICMS (the so-called Kandir Act), and the creation of a simplified system for collecting tax from micro and small companies (known as the Simples Act), and, lastly, the issuing of an act which set up a new, responsible fiscal system.

It is worth stressing that these institutional changes were irrelevant when it came to getting fiscal results. To the contrary, in some cases they even made the accounts worse in the short term: the Kandir Act provided compensation transfers from central government to regional government; the Simples Act increased the waiver, in particular for social security; privatization and renegotiation brought to light some debts of state companies, banks and regional governments contracted in the past, which were not known or fully accounted for (known as skeletons) – and which, paradoxically, when they were regularised, worsened recent results.

In any case, whether they were harmless or had a negative impact in the short term, these changes were crucial in creating a better future for public finances, and for the economy itself.[33]

[32] For a critical analysis of the development of the public accounts in the immediate post-Real period, see Giambiagi and Ronci (2004), Giambiagi (2008), Jaloretto (2009) and, for more recent years, Almeida (2013).
[33] For a general and theoretical approach on Brazilian public finances from different perspectives, see Além and Giambiagi (2001) and Oliveira (2009).

The new government which took office in 1995 sent to Congress a set of constitutional amendments, ranging from reforms of the tax system, welfare system and administration, to reforms in the economic and productive system, which sought to break up monopolies (such as in oil and gas) and make way for concessions and greater private involvement in companies or sectors previously dominated or controlled by the state (such as mining, energy generation and distribution, infrastructure, transport services, and oil drilling).

By the end of the decade Congress had voted for tax reform,[34] approved reforms restricting social security, and accepted administrative reforms, but these things were largely ignored within government, except for, eventually, one detail: the constitutional amendment required the Executive to send a plan for regulating the article dealing with the general provision of public finances, which later became known as the Fiscal Responsibility Law – the LRF.[35]

The process of privatisation was much more successful. Initially, in the legislative field, it required a good deal of political effort to approve amendments to the Constitution that mitigated or reversed the state-forming or nationalising slant that had dominated the Constitutional Assembly a few years prior. In the early nineties, as we have already seen, the government had already promoted a major and rapid liberalisation of the economy and had begun to sell off some state companies, such as the iron and steel sector. However, it was after the legal reforms that it really became possible to break the state monopoly in sectors such as oil, energy, telecommunications, mining and transport, and an extensive and rapid process of selling off state companies took place. This was in addition to the proposal to increase concessions for private participation in areas where it previously had little involvement, such as roads, ports, and oil and gas extraction.

The banking system was also restructured; federal banks were cleaned up and reinforced, and almost all state banks were privatised. Sanitation companies, energy distributors and transport companies, including subways, passed into private management, with governments often motivated or forced to carry out this privatisation in exchange for the federalisation of their debts.

[34] On polemics and failures of recurrent tax reform plans, see Varsano (2003) and Mendes (2013).

[35] Therefore, the LRF was administered nationally and at the initiative of parliament, and not at the instigation of the International Monetary Fund, as the political opposition alleged at the time. Rather, the Fund itself came to issue an unfavourable analysis of the draft plan (or on condition that other reforms were carried out beforehand).

Even having gained initially with tax decentralisation, states could not service the accelerated indebtedness of the past decades. In the case of credit, much was contracted from abroad, and in the case of bonds – together with federal state banks – by means of papers passed through private banks to state banks and then on to the central bank. The federal government assumed these debts (in some cases, it was even necessary to do so in order to clean up its own banks) but in exchange it demanded a payment on sight of the balance to be renegotiated in exchange for offering lower, subsidised interest rates in the new debt. Most state governments only succeeded in making such a payment, and this more favourable rolling of debt, viable in exchange for a commitment to privatise state energy, transport and communications companies, and thus be able to forestall the sale of part of the control to a federal bank (the BNDES). Few paid attention to this connection between privatisation and renegotiation in which this second and somewhat unorthodox fiscal measure was used as a means of engendering economic reform.

Specifically regarding the renegotiation of debts, the federal government took over the debt of 24 states for a total of US$ 82 billion (equivalent to 10.5% of GDP), under what were initially fairly favourable conditions: at least 30 years for payment (if there was some remaining, a further 15 years); fixed interest rates of between 6% and 7.5%, plus inflation adjustment (IGP); monthly instalments that should not exceed 11% or 15% of net revenue. By the terms of these agreements, the states could not issue new bonds until their total debt was compatible with their annual revenue. If they did not fulfil their commitments, the federal government was authorised to block transfers from the Participation Fund and the regional governments also lost the special benefits of the agreement. Despite these governments always paying all the monthly instalments on time, the Treasury credit balance resulting from the main line of refinancing was 10.3% of GDP at the end of 2013, falling only 3.2 points of product in thirteen years, because the interest rate and indexing had been separated from the new economic conditions. It is hardly surprising that governors and mayors sought a renegotiation of these conditions as a matter of urgency. The federal government reached the point where it sent a draft plan to Congress at the end of 2012 to reduce the conditions.[36]

[36] For a more recent assessment of the renegotiation of regional public debts in Brazil, see Manoel, Garson and Mora (2012) and Pellegrini (2012).

On the tax front, the draft constitutional reform focused on indirect taxes, with the aim of creating two general value added taxes, one with federal jurisdiction (lower) and another with state jurisdiction (the ICMS merged with the municipal ISS). In this case, the so-called destination principle was adopted in interstate transactions – utilising an innovative system of crossing both taxes so that the central government could both charge the state of origin and transfer the revenue to the state of consumption (known as the *barquinho*, or 'small boat', model).[37] Although members of parliament have defended this comprehensive reform, the federal government itself withdrew support for the proposal at the end of the decade through fear of not being able to further the heavy increase in the tax burden needed to achieve fiscal stabilisation as agreed with the IMF.

While the constitutional structure of taxes did not change, major changes were made to infra-constitutional legislation, but again, without the formation of an articulated plan.

A general, no-frills law on the circulation of state tax (ICMS) known as the Kandir Act[38] was approved in 1996. Once again, the initiative came from a congressman (who later became Planning Minister and negotiated approval of the bill). In the face of heavy damage to imports inflicted by currency appreciation, the federal government supported measures aimed at alleviating those effects. The main change introduced by the Kandir Act was to grant general exemption for exports, both manufactured goods and primary products (only accepted by states in exchange for the federal government committing to give compensation to those who had lost the most). This was a major innovation because, since the creation of the Republic in the 19th century, state governments had always taxed exports abroad heavily. It was, however, suggested that long-chain industrialised product exports continued to be taxed indirectly, as the state treasuries generally try not to return accumulated credit balances, a recurrent problem for those making large investments in production.

Another legal change in the immediate post-Real period involved the creation of a simplified taxation system, known as *Simples,* for micro and small businesses. Although this initially only applied in federal jurisdiction (including social security), a decade later it was expanded to include state (the ICMS) and municipal taxes (the ISS), and became known as

[37] For details of that process, see Varsano (2014).
[38] Supplementary Act no. 87, of 13/9/1996: complete text available at: http://bit.ly/lmUS3do.

SuperSimples. A unique and simple refinement was made by applying an aliquot (which varies according to activity – not all are included – and size) on gross turnover, and payment in a single collection bill (with the bank network responsible for redistributing the revenue to different bodies as stipulated in the law). The initiative was led by the federal government, who recognised the enormous bureaucratic complexity of the Brazilian system and were offering a simpler alternative for over 95% of taxpayers, albeit at the cost of a considerable waiver. It is curious that at the time of the system's creation and expansion it was not seen as the crucial means for formalising employment and enterprises which it increasingly became, accounting for an overwhelming proportion of new taxpayers who registered with the general social security scheme, not to mention making a significant contribution to the current, all-time low employment rate.

Despite all these institutional reform measures, towards the end of the last decade of the twentieth century, a new and more serious international crisis took place – with the difference that Brazil was now at its epicentre.

The government's reaction was to radically change economic policy, albeit due to a lack of options. Earlier, we saw how the Brazilian economic policy 'tripod' developed without prior planning, nor were the different elements adopted at the same time. First it opted for the inflation targets system. In creating this system, Brazil was the first emerging economy to have this instrument accepted in the aid programme of the International Monetary Fund (IMF), which previously had stuck to monitoring the imbalance of balances, and preferred countries to adopt a currency stabilisation fund (currency board).

Fiscal adjustment came next, and was carried out on two fronts. Firstly, an ambitious programme of fiscal adjustment was designed, under pressure from the IMF, which combined a major increase in taxes with general cuts to expenditure (although this drastically reduced investments). The results were published and strictly monitored in order to meet the targets of increasing primary surplus and stabilising the public sector's net debt. On the second front, the federal government sought to adopt measures to avoid fiscal imbalances recurring, and to avoid having to end every year lowering fiscal packages, with an increase in taxes and cuts to spending. Although it did not make much progress with taxation and social security reforms, the government prioritised the publication of a new general code for public finances which was supported by Congress; indeed, it was Congress that took the initiative to ask the Executive to send a bill to regulate this code which, despite being stipulated in the 1988 Constitution, had never been debated.

In less than a year, a bill to create a responsible fiscal system passed through Congress and was approved by a quorum sufficient to change even the Constitution.[39] The act is very broad (it has over 100 articles)[40] and, as a supplementary act which sets general, constitutional regulations, applies to all administrative bodies in the three spheres of government.

The Brazilian act – the first of its type to be adopted by an emerging economy – includes both principles (such as the balance of the budget in the long term) and specific limits, as well as an emphasis on transparency. It only specifies one restriction, to comply with an express constitutional decision, which applies to spending on the salary payroll: the maximum should be 50% of current revenue for central government and 60% for other governments, with sub-restrictions for powers and bodies, as well as a prudential limit (which, if exceeded, prohibits wage increases and hiring). Another oft-cited limit for public debt is regulated by the LRF, which covers on what basis it will be applied, how, and how it will be adjusted. The public debt ceiling itself was fixed at a later date by the Senate, initiated by the President, but without the powers of veto.

Now the targets for fiscal results, and their component parts (revenue and expenditure, as well as debt and equity), are fixed annually in an act drawn up by each government (the Budgetary Directives Act – LDO) which also contains an estimate for the next two years. Throughout the year, periodic checks are made to see whether the revenue effectively being collected matches the one initially drafted, and if there is a mismatch a budget sequestration (linear or differentiated, if regulated in the LDO) is automatically put into effect. It is noteworthy that there are no national or aggregate goals, as each government sets and pursues its own targets.

The LRF itself includes some get-out clauses, such as exemption from complying with limits in the event of disaster, low growth or recession, drastic changes of economic policy or if there is a request from the Senate Executive. But, being a supplementary act (it requires a special quorum and cannot be changed by presidential act), is also applies to regional

[39] The history of the preparation and voting of the LRF has been set out in detail by Afonso (2010).
[40] Supplementary Act no. 101 of 4/5/2000; complete text available at: http://bit.ly/l3pznnq.

governments and, traditionally, is very stable (it cannot be amended by an exclusive act of the Federal Executive). Furthermore, one pillar of the LRF was to forbid the central government taking on debts from other governments or loaning to then directly – a classic problem in a country which has already experienced successive internal and external moratoria of regional governments which have ended up being assumed by the central government.

The LRF was also accompanied by another act which criminalised breach of the most basic rules, stipulating both loss of political mandates and even prison. Since it was so all-encompassing and multifaceted, mixing a code of conduct with rules, the Brazilian LRF won worldwide recognition as a highly modernising piece of legislation.[41]

In this general overview of events, the introduction of the LRF can be seen as the act which consolidated or concluded the process of institutional changes. In the midst of this, the budgetary process was reformulated, revenue, accounting and finance administration was modernized, most public companies and banks were privatised, and regional debts were renegotiated by the central government, among other things. If after the LRF few advances were made in changes to fiscal legislation, the same is not true for the field of management, where efforts continued to be made to modernise fiscal administration in its very diverse activities. This is the case, for example, for the national government and most of the regional governments adopting an integrated system of budget management, accounting, finance and equity (known as SIAFI), and also the use of electronic fiscal notes in taxation (the issue involves an on-line record in treasury checks), reducing costs for taxpayers and making the work of tax-collection organisations easier and more efficient.

Brazilian fiscal management is particular to a democracy and a relatively autonomous federation. Each unit of government, national or regional, prepares, estimates and approves its own budget and, at the end of the financial year, its statement of accounts. Each government has the authority to legislate, charge and collect its taxes, and also to regularly receive and dispose of revenue distribution guaranteed constitutionally. Each government can freely hire officials and determine their wages, buy goods and services, and also contract labour, and, lastly, each government can decide freely to contract debts. In this

[41] For a comparative analysis of the Brazilian experience in world context, see Ter-Minassian (2010) and World Bank (2008).

context, the fiscal system does not follow a basic direction formulated from the centre; goals are set and pursued freely, without standardisation. It is up to the federal government to try to exercise some control by means of discretionary recourses, namely voluntary transfers and loans, in collaboration with state banks or multilateral organisations, with National Treasury guarantee. In practice, since most regional governments still owe a lot to the Treasury itself on account of the different financing schemes implemented before the LRF was brought out, the key variable in national fiscal management is the service of renegotiated debt. In this case, defaulting is invalid (the Treasury can block and withdraw cash directly from the individual coffers of a debtor government which does not pay on time), and the volume of payments is so high that it ensures, in and of itself, that the regional governments will make a substantial primary surplus (the regional governments paid the Union the equivalent of 0.78% of GDP in return for these operations in 2013). In practice, the regional primary surplus only gets worse if the central government grants these governments the ability to contract new credit operations. Another aspect of this situation is the growing criticism, particularly from political scientists, that the country paradoxically is experiencing a new wave of political centralisation, as regional governments' room for manoeuvre in fiscal terms is very limited.[42]

4.2 Riding the Wave of Growth

As such, while the last decade and a half has not seen any changes which could be labelled structural reforms, it did display the best performances yet in traditional fiscal indicators. In particular, the targets for generating a significant primary surplus in the public sector and reducing net borrowing were successively met.[43] A good example is in the development of public sector debt shown in the graph below: in the most widely-used measure in the country, net borrowing went down by 48% to less than 34% of GDP between the end of 2000 and 2013. (By the gross methodology, closer to the one used by other countries, the latest position is much higher, at 67% of GDP.)

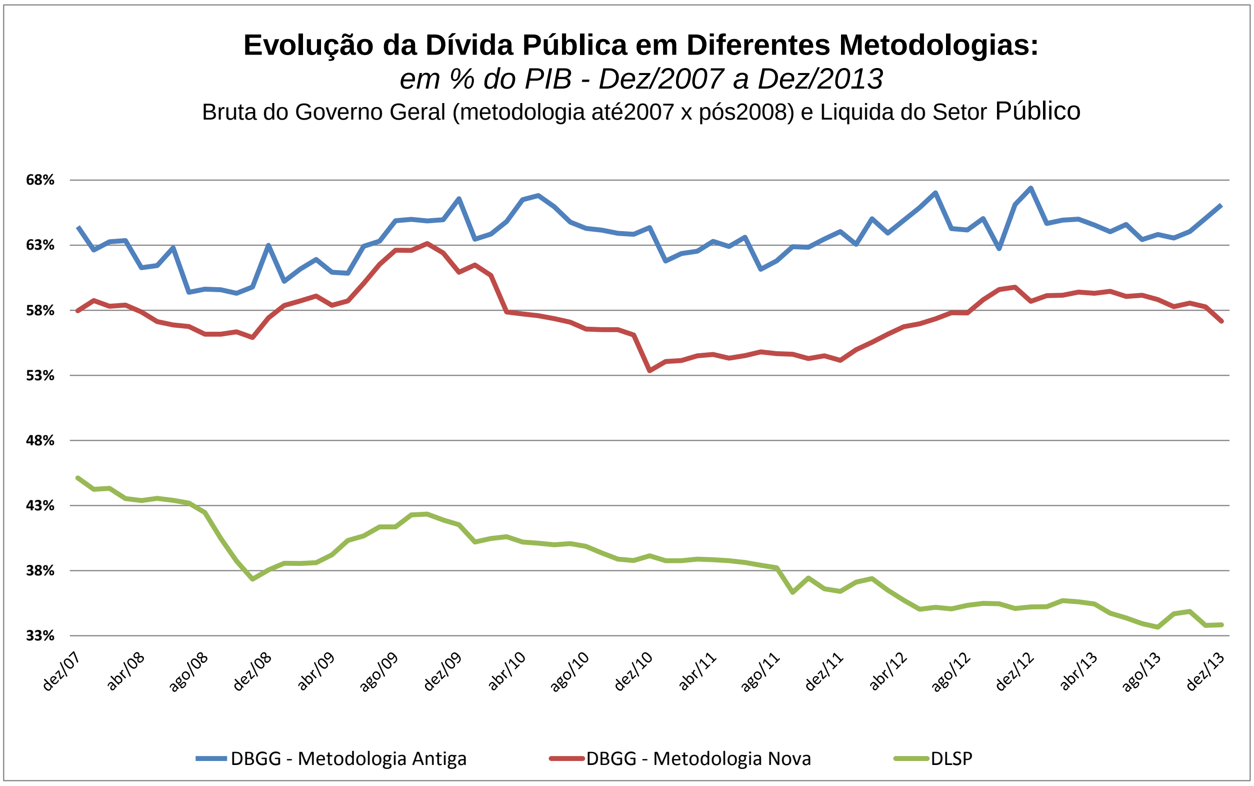
[42] A good example is Ismael (2013).

[43] For a wide-ranging assessment of the Brazilian economy from international organisations, see OECD (2001) or IMF (2013), among other authors.

Figure 5: Development of the public debt, traced by different methodologies

in % of GDP - Dec/2007 to Dec/2013

Gross of the General Government (methodology up to 2007 x after 2008) and Net of the Public Sector



(DBGG - Old Method | DBGG - New Method | DLSP)

The spectacularly favourable external setting, with the best commodities price boom of the post-World War period, created conditions in which Brazil displayed the best growth rates of recent decades, albeit driven mostly by consumption and by expanding internal credit.

In some ways, we can recognise that this more favourable economic setting was an important factor in the government's lack of interest in maintaining the momentum of legislative changes, despite enjoying a substantial parliamentary majority and widespread popular support; it simply did not seem necessary.

The good performance of fiscal indicators, however, was accompanied by changes in the profile of the main variables. Despite no longer having to respond to external or fiscal crises, as in the recent past, the overall tax burden remains high and is increasing, which has in addition allowed public spending to grow and to therefore create the highest primary surplus in the last two decades. It was not by chance that public debt, conventionally measured by the concept of borrowing and which counts the central bank, atypically, as part of the public sector, fell to the point where it set off the accumulation of foreign reserves from the middle of the last decade. Since Brazil collects indicators for the whole public sector and includes the central bank, the reserves are deducted from the liabilities and thus foreign debt becomes negative, with a strong correlation between net borrowing and the exchange rate: paradoxically, incidents of maxi-depreciation reduce public debt drastically, while incidents of appreciation cause it to rise. It is an unusual situation and radically different from that of other countries.

Social policy has become active, and has gained central importance in the fiscal setting, which in the past was limited to a concern for generating sufficient economy to meet debt commitments, particularly foreign debt. In the nineties, the priority was for universal public services, with decentralisation of primary education and the healthcare system – indeed, the main result for both of these services was municipalisation. Already in the past decade, the focus has shifted to benefits, both social security (benefitted by real increases in the minimum wage, which pays more than half of the pensioners in the general scheme), and welfare benefits (timely, incipient income transfer programmes were consolidated in the family allowance).[44]

With the necessary costing increased for management of these policies, social spending has more than doubled in two decades and today reaches levels much more comparable to the European welfare state than to emerging Asian or Latin American countries. Currently, calculating all the costs and the three spheres of government, it is close to 25% of GDP. It is interesting that in order to finance such high social spending, an excessively high tax burden has become both inevitable and necessary.

Brazil takes advantage of its tax potential in a way that few other countries, including wealthy ones, do, because it uses and abuses the application of indirect taxes. With an economic organisation marked by a business concentration that is high and still rising, and with recourse to uncommon tax practices such as large-scale tax substitution, assumed profits, applying excessively high aliquots of value added taxes on strategic inputs (such as fuel, energy and communications) and even some years ago taxation on current bank movement, Brazil is very successful at generating an indirect, overall tax burden. This tax-collection success is also the result of long and sizable investments in the modernisation of

[44] See Serra and Afonso (2007b).

tax administration, which today has recourse to technological resources on a par with those of the most advanced economies and with relatively reduced costs. For instance, 100% of income tax declarations, even of individuals, are filled out electronically and submitted online.

On the other hand, advances in how tax collection is carried out have a rather damaging counterpart, namely a heavy reliance on regressive taxes in a society already marked by deep concentration of income and wealth before tax and which, after tax, becomes even more unequal. The collection impetus is not replicated in direct taxes, as is clearly shown by the fact that tax collection on urban real estate property (IPTU) is less than a third of tax on car ownership (IPVA), while no tax at all is collected on undeveloped land (ITV). Even in the case of income tax (IR) it is difficult to reach the very rich and even many middle-class professionals, as they do not receive income as individuals (and are not, therefore, subject to the progressive table) but rather as individual firms (subject to a much lower burden and with an equal aliquot, regardless of income), a phenomenon prevalent in the Brazilian private sector more generally which is likely to intensify more than in other economies (and which is the result of applying an excessively high tax burden on work and in general). Despite these different examples, fiscal fairness is a subject ignored and even avoided in national debate, both political and even academic – strangely, it arouses more interest abroad, as Brazil is notorious for being one of the most unequal countries in the world.[45]

One can say that in the context of accelerated economic growth both fiscal and macroeconomic policy produced their best results in decades, and it was no surprise that the reform agenda lost priority, and later was even rejected. There was consensus, including in the financial market, that fiscal austerity was one of the three pillars of Brazilian economic policy introduced at the end of the last century (alongside the inflation targets system and a floating exchange rate) in response to the major crisis the country was at the centre of. Successive governments, despite changing hands, have kept this in place.

[45] For recent and comprehensive calculations on fairness, both in tax collection and in the fulfilment of social public spending, see Rezende, Afonso, Gaiger and Ferreira (2013).

4.3. The Small Wave and Stagnation

The state had a specific response to the global financial crisis and, as in the rest of the world, this put fiscal policy on the agenda of national debate.[46]

The first and most important feature of its response was what it did not do: Brazil did not instigate, or even propose, any structural reform. This ran contrary to past Brazilian experience, in which any crisis was used as an opportunity to introduce structural reform.

Another striking feature was giving priority to revenue (reducing the tax burden) over expenditure (public investment remained among the lowest of any country in the world) – a truly liberal response, though the government did not see it as such. Even when the worst of the crisis was over, the federal government continued to grant and diversify tax burden reductions, to the point of a proposal to change the base of the salary payroll to gross turnover in the case of contributions to social security, for a selected group of sectors.

But where Brazil introduced a global innovation was in terms of linking public revenue to credit,[47] on account of successive loans granted by the National Treasury to the banks it controls (in particular, the BNDES), and to the bond issue account; it jumped from 8.5% to 15.3% of GDP between the end of 2007 and 2013. In the beginning, at the height of the financial crisis, the state banks played a crucial role in restructuring equity and recovering credit, including for family consumption. But that earlier success was not recreated when later the rate of national investment was raised, as many more borrowers took advantage of cheap, long-term state credit to shift funding for existing projects rather than apply for new ones, and the banks were used to implement strategies to convert public debt into primary revenue (a growing proportion of the credits granted by the National Treasury came back at the cost of selling shares and other receivables, and also resulted in dividends and taxes).

As in the rest of the world the government contracted debts in the post-crisis period, but unlike other countries, it did so in an attempt to extend the supply of credit – initially to promote a major restructuring of equity (which liberated the central bank from carrying out that traditional function) and then to generate revenue and artificial results for the National

[46] Barbosa Filho (2010) is one of the rarest and most academic books showing the view of the Brazilian economic authorities in relation to the crisis, the so-called countercyclical response and even the assumed creation of a new inclusive model of economic and social development.
[47] This topic is discussed in detail in Afonso (2011).

Treasury itself. It is not surprising in this context that, despite the fact that the public banks had strongly increased their share in the economy's credit, the national investment rate fell from 19.1% to 18.4% of GDP between 2008 and 2013.

Currently, fiscal policy is marked by growing controversy, from market analysts to those of multilateral organisations and rating agencies, who blame the use of atypical fiscal manoeuvres for hiding fiscal deterioration, while the government claims it has enforced the law and followed past processes which are recognised internationally.[48] Behind the debate was the overwhelming use of net theory by governments and analysts to measure the public debt, and more and more attention is being paid to gross theory, the one most used abroad.[49] Regardless of which side is right, fiscal conventions that have reigned in the country for decades have undeniably been shaken.

The big question today is whether conventions have merely been shaken, and it would be possible to regain credibility without structural changes, or whether confidence has been lost and a new round of reform would be necessary to restore it.

5. Macro institutions in Brazil: economic significance, contributions and main challenges

This analysis has sought to demonstrate the relevance of institutions, and also of monetary and fiscal policy, to the economic and social stabilisation and development of the Brazilian economy following the creation of the Real.

Despite the relative success achieved, it is important to bear in mind that the processes involved – from the formulation of the monetary and fiscal instruments mentioned, to their implementation and consolidation – did not result from prior appropriate strategic planning. The institutional reforms were, in general, carried out in response to a succession of internal and, principally, external crises. The need to face both economic and structural crises allowed different governments to approve important legislative changes in the National Congress, as well as amendments to the Constitution enacted shortly before in October 1988. The cycles of institutional reforms of monetary and public finance did not, therefore, result from an organised plan, country, or even government, but were imposed by dint of circumstances.

[48] Afonso and Barros (2013) describe and comment on the different so-called atypical fiscal measures which central government has turned to recently to meet primary surplus targets.
[49] On this debate on the debt, see Gobetti and Schettini (2010).

Perhaps nowhere in the world has inflation received as much attention from economists as in Brazil. The theoretical and practical accumulation of knowledge – the result of living with inflation for a long time – resulted in innumerable theories regarding the nature of Brazilian inflation. The ability of inflation to resist the most diverse strategies deigned to combat it led to a cease in hostilities and the seeking instead of a peaceful coexistence with inflation.

Inflation only gained the notoriety it presently holds in Brazil from the way it affected people who lived through the day-to-day reality of Brazil from the mid-1980s to the mid-1990s. This was enough time to leave ingrained in the public psyche the trials and tribulations connected to the battle against inflation, from the freezing of prices to the contraction of credit by confiscating people's savings.

Price and contract indexing, which at first alleviated the effects of inflation on the economy and made it possible for economic agents to coexist for a long time with fairly high inflation levels, also had major consequences for the perpetuation of inflation in Brazil; inflation became extremely hard to stop due to the great weight of its inertial component. During this period, exchange rate devaluations were used to finance the balance of payments, and as a result of this the government had its financial liability taxes denominated in enlarged dollars, and the securities debt placement depended on higher and higher interest. This situation created very specific divisions between fiscal, monetary and exchange policies.

The Real Plan was a milestone in that, in the middle of 1994, it disrupted a long process of chronic high inflation whose origins stretched back to the 1960s. It is worth highlighting in that plan the system of exchange rate targets, which, along with the behaviour of fiscal policy and high interest rates, was the institution responsible for price stability in Brazil, despite the costs it brought to the real economy. The policy of appreciated exchange which could now be adopted due to the increase in international liquidity, changed the nature of the relationships between the exchange, fiscal and monetary policies of the previous period. This policy made it possible to reduce uncertainties about the behaviour of basic prices in the economy, with monetary and fiscal policies used to reduce uncertainties related to the exchange rate.

In 1999, as the anchor of monetary policy was abandoned, the system of inflation targets stepped in. From then on, the macroeconomic tripod became key, combining the system of a floating exchange rate, primary surplus targets, and an inflation target system. In this new arrangement, fiscal and exchange policies were subject to the policy of price stabilisation, the latter being controlled by monetary policy.

In the fiscal field, while Brazil stood out even on the international stage by modernising its institutions by the end of the last century, it is worth remembering that this was more the result of a response to crisis than organised planning. Circumstances called for fiscal reform, from privatisation and control of regional finances to the system of fiscal responsibility. Lastly, governments had to react to a series of macroeconomic crises, from the old outbreaks of hyperinflation through successive external crises, to the adoption and consolidation of different stabilisation plans. In response to each crisis, some institutional change was advanced, culminating in a picture of relative fiscal stability that was more notable after the turn of the century (and that gained even international recognition).

For no other reason than a drive for modernisation, fiscal institutions were abandoned in the first decade of this century, when crises gave way to the longest and most profound period of economic calm witnessed in Brazil, and in Latin America itself, since the Second World War. From the boom in commodities to the rise in family consumption, accelerated growth enabled good fiscal results with no institutional change.

But the great global financial crisis of 2008-2009 was bound to change all that, and Brazil confronted it in a peculiar way: with state action, as in the rest of the world, but without a resultant rise in public investments. Instead, it continued to supply credit to the rest of the economy through state-owned banks, at the expense of government borrowing.

The Brazilian historical tradition of facing a crisis with reforms was broken – and note that this was considered the greatest crisis of world capitalism since 1929. This does not mean that the government did not set in motion fiscal policy, first to get out of the global crisis, then to accelerate growth which continued to stagnate and was well behind the average for emerging countries. Current expenditure, in particular social security and welfare benefits, continued to increase, ahead of the economy and tax collection.[50] Fiscal benefits were rapidly multiplied, from tax waiver to credit subsidies.[51] Fiscal results declined, and the federal government, rather than reduce the fiscal goal, decided on strategies to create a

[50] The recent growth in the primary expenditure of central government, in particular led by more social security and welfare benefits, is highlighted by Almeida (2013). The pressure for expenditure in the regional spheres has already been discussed by Sturzenegger and Werneck (2006).
[51] See Afonso and Diniz (2014).

primary surplus artificially. Controversy aside, the country has undeniably opted to patch up the reform of its tax system, and even the fiscal system more broadly.[52]

The thrust of the government's argument was to deny the crisis, to claim that managing is better than legislating, and to therefore refuse to draw up draft reforms, much less attempt to have them approved in Congress – despite the fact that it enjoys a considerable and growing parliamentary majority, and even widespread popular support in opinion polls.

The agenda of institutional reforms was left to one side. Firstly, in the middle of the last decade, growth of domestic consumption driven by credit and the world economic boom was taken advantage of, which succeeded in getting the best rates of economic growth in a generation, with inflation reduced and still decreasing. This scenario, in its own right, did away with efforts to promote institutional reforms. Secondly, even the drastic changes at the macro level which began in mid-2008 with the global financial crisis did not lead the government to propose structural changes – precisely because the official argument denied that the crisis would reach the Brazilian economy.

It was at the turn of the last decade that the strategy of fiscal and monetary policy changed significantly, and became openly countercyclical, in the government's view, or flexible, in the view of the market. A central aspect of that strategy began by reducing the link between fiscal and credit instruments, since the wager was on rapid public indebtedness providing the public banks with funding and continuity in credit expansion. The resulting scenario, however, was marked by production stagnating and an increase in inflation. Even so, there is no debate or proposal on the horizon to review, much less restructure, monetary, tax and fiscal institutions. The official argument is that economic policy follows the same tripod designed at the end of last century, with a floating exchange rate, inflation targets and fiscal austerity.

Currently, inflation – or the constant threat that inflation will return to previously seen levels – is the reason for a large part of the Brazilian government's economic policy, which is something that receives no further consideration or explanation. Policy starts from the assumption that inflation negatively affects everyone, and, because of this, must be fought, even to the detriment of other economic variables such as increasing production and

[52] See debate in Rezende, Oliveira and Araújo (2007).

employment. Despite the price stabilisation achieved in the mid-1990s, inflation has not fallen from its position of priority in the sphere of economic policies.

In this context, any prospective future, including in the short term, looks rather gloomy.[53] Public debt and the tax burden have already reached levels higher than those of other emerging countries. Investments form an ever-smaller proportion of the budget, while in contrast, the overwhelming majority of expenditure is committed, either contractually or politically (from wages and pensions to income transfers, whether profits or interest). How can a tax burden that is already considered high, both historically and comparatively, be raised further? How can you reduce spending which has already been cut when, politically, society puts pressure on you – sometimes by taking to the streets – to increase the availability, and improve the quality, of public services?

Possibly the greatest challenge for the Brazilian economy today is to re-start precisely that process of institutional reform, last carried out at the end of the previous century, which today serves as a benchmark for other emerging economies. There is no longer any doubt that sustained economic growth led by the growth of consumption has its limits, and the most it has achieved today is preventing a full-blown recession. A combination of the increasing inflationary pressure – even after the rise in basic Real-dominated interest rates – and the economy's worst external results in the post-war period, up to the significant reduction of the public sector's primary surplus, meant that the Brazilian macroeconomic tripod lost either its sustenance or its sustainability.

The consensus that new institutional arrangements are necessary is growing, gradually. To start with, there is an increasingly pressing matter to deal with – a prerequisite, even – before reviewing individual policies, which relates to the fragile co-ordination of the macroeconomy: there seems to be a lack of any organised set-up to improve interaction between the different economic authorities. Practice has been marked by somewhat autonomous management by the party responsible for each segment of economic policy (such as monetary policy, tax collection, management of expenditure and debt), without any formal process for integrating activities. Exercises in macroeconomic consistency disappeared, not only from official research studies, but also from the national academic

[53] For a detailed prospective exercise, see Giambiagi (2009) and Velloso, Mendes and Caetano (2009), among others. For a discussion on alternative strategies, see Afonso and Mussi (2009).

arena. As a result, it is not uncommon that fiscal policy sometimes displays one trend (expansionist) while monetary policy goes in exactly the opposite direction (contractionist). In a government in which there is no lack of professional bodies for various fields of activity, it is strange that there is no official body tasked with bringing together, integrating and co-ordinating the authorities and the policies involved in the Brazilian macroeconomy.

The more troubled the outlook for a vigorous fiscal agreement, the greater the possibility – or even the need – for agendas of reform of the fiscal institutions in Brazil to be taken up once again. There is no lack of opportunities, from the taxation system or budget system to the fiscal responsibility law itself, which has not yet been fully regulated. But the first change should be in the strategy of the federal government which, since the rise of the Workers' Party, has opted for a minimalist approach, fearing the reaction of parliament, despite the fact it has always enjoyed a broad and growing majority.

Paradoxically, Brazil's past experience, which could ultimately serve as a lesson for other emerging countries, must now become a point of reference for the country itself – a country which faces the enormous challenge of building a new macroeconomy fit for its future.

For the outside world, the great question is: amidst this remarkable duality, will Brazil become a model in public finances, in monetary policy and even in federalism for other economies, in particular emerging or developing economies? Every case is different, but it is hoped that some lessons from Brazil's experience may be considered by other countries, not only in relation to what course of action to take, but in particular, what to avoid.

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Statistical Annexes

Resultado primário do setor público consolidado: em % do PIB - 1991/2014

Composição	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**
Governo Central	0,98	1,10	0,81	3,25	0,47	0,34	-0,25	0,51	2,13	1,73
Estados/Municíp.	1,40	0,06	0,62	0,77	-0,16	-0,50	-0,68	-0,17	0,20	0,51
Estados	n.d.	n.d.	n.d.	n.d.	n.d.	n.d.	n.d.	-0,38	0,14	0,39
Municíp.	n.d.	n.d.	n.d.	n.d.	n.d.	n.d.	n.d.	0,21	0,06	0,12
Empresas estatais	0,33	0,41	0,76	1,19	-0,06	0,07	0,05	-0,33	0,59	1,00
Federais	n.d.	n.d.	n.d.	1,63	0,38	0,26	0,24	-0,22	0,60	0,87
Total	**2,71**	**1,57**	**2,19**	**5,21**	**0,25**	**-0,09**	**-0,88**	**0,01**	**2,92**	**3,24**

Composição	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Governo Central	1,69	2,16	2,28	2,70	2,60	2,17	2,23	2,35	1,31	2,09
Estados/Municíp.	0,80	0,72	0,81	0,90	0,99	0,83	1,13	1,01	0,65	0,55
Estados	0,55	0,58	0,70	0,83	0,80	0,69	0,98	0,86	0,55	0,45
Municíp.	0,25	0,14	0,11	0,07	0,19	0,14	0,15	0,15	0,10	0,10
Empresas estatais (/	0,89	0,34	0,18	0,12	0,20	0,20	-0,05	0,06	0,04	0,06
Federais	0,61	0,10	-0,05	0,00	0,05	-0,04	-0,06	-0,01	-0,05	-0,02
Total	**3,38**	**3,22**	**3,27**	**3,72**	**3,79**	**3,20**	**3,31**	**3,42**	**2,00**	**2,70**

Composição	**2011**	**2012**	**2013**
Governo Central	2,25	1,96	1,57
Estados/Municíp.	0,80	0,49	0,34
Estados	0,72	0,43	0,27
Municíp.	0,08	0,06	0,07
Empresas estatais (/	0,06	-0,06	-0,01
Federais	0,01	-0,02	-0,01
Total	**3,11**	**2,39**	**1,90**

n.d. Não disponível.

/a A partir de 2002 (inclusive), exclui resultados da Petrobras.

Fonte primária: Banco Central e SEST (estatais em 1994 por resíduo),

Elaborado por Fabio Giambiagi.

Primary result of consolidated public sector: in % of GDP – 1991/2014

Composition	**1991 …**
Central Government	
States/Municip.	
States	
Municip.	
State companies	
Federal	
Total	

Composition	**2001 …**
Central Government	
States/Municip.	
States	
Municip.	
State companies	
Federal	
Total	

Composition	**2011 …**
Central Government	
States/Municip.	
States	
Municip.	
State companies	
Federal	
Total	

n.d. = Not available

/a From 2002 (inclusive), excludes results of Petrobras.
Primary source: Central Bank and SEST (state in 1994 per residue).
Prepared by Fabio Giambiagi

Evolução da dívida líquida do setor público por principais componentes: em % do PIB - 1991/2013

Composição	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Dívida interna	**13,5**	**18,4**	**18,8**	**21,5**	**23,0**	**27,1**	**27,8**	**33,1**	**35,1**	**36,5**
Governo Central	**-2,1**	**0,8**	**1,9**	**6,7**	**9,0**	**13,3**	**15,5**	**19,4**	**20,0**	**21,6**
Base monetária	1,5	1,4	1,0	3,6	2,8	2,2	3,3	3,9	4,2	3,9
Dívida mobiliária/b	5,4	9,1	9,9	11,7	14,3	19,7	26,1	32,2	35,3	38,9
Renegociação E&M							-5,0	-8,7	-11,3	-12,5
FAT	-0,9	-1,3	-1,5	-2,0	-2,3	-2,3	-2,4	-3,3	-3,6	-4,1
Créditos Tesouro a inst.fin.of.										-0,4
Oper. compromissadas	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,5
Demais dívidas	-8,1	-8,4	-7,5	-6,6	-5,8	-6,3	-6,5	-4,7	-4,6	-4,7
Estados/Municípios	**5,9**	**8,1**	**8,3**	**9,6**	**9,5**	**10,2**	**11,5**	**12,6**	**14,0**	**14,1**
Renegociação E&M							5,0	8,7	11,3	12,5
Outras	5,9	8,1	8,3	9,6	9,5	10,2	6,5	3,9	2,7	1,6
Empresas estatais (A)	**9,7**	**9,5**	**8,6**	**5,2**	**4,5**	**3,6**	**0,8**	**1,1**	**1,1**	**0,8**
Dívida externa	**23,3**	**18,7**	**14,4**	**8,5**	**5,0**	**3,6**	**4,0**	**5,8**	**9,4**	**9,0**
Total	**36,8**	**37,1**	**33,2**	**30,0**	**28,0**	**30,7**	**31,8**	**38,9**	**44,5**	**45,5**

Composição	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Dívida interna	**42,4**	**44,7**	**43,7**	**42,7**	**45,2**	**48,4**	**53,0**	**49,5**	**51,1**	**48,6**
Governo Central	**23,6**	**24,6**	**24,7**	**24,6**	**28,7**	**33,0**	**38,7**	**35,9**	**38,5**	**36,7**
Base monetária	4,1	5,0	4,3	4,6	4,7	5,1	5,5	4,9	5,1	5,5
Dívida mobiliária	46,4	40,6	43,1	40,3	44,6	45,2	45,1	41,1	42,7	42,2
Renegociação E&M	-13,4	-14,7	-14,3	-14,3	-13,5	-13,0	-12,4	-12,2	-11,3	-10,8
FAT	-4,7	-5,1	-5,2	-5,3	-5,4	-5,5	-5,2	-5,1	-4,9	-4,5
Créditos Tesouro a inst.fin.of.	-0,3	-0,8	-0,8	-0,9	-0,8	-0,5	-0,5	-1,4	-4,5	-6,8
Oper. compromissadas	-0,7	5,2	3,9	3,0	1,7	3,3	7,0	10,7	14,1	7,7
Demais dívidas	-7,8	-5,6	-6,3	-2,8	-2,6	-1,6	-0,8	-2,1	-2,7	3,4
Estados/Municípios	**16,7**	**18,4**	**17,5**	**17,1**	**15,6**	**14,7**	**13,6**	**13,0**	**12,0**	**11,4**
Renegociação E&M	13,4	14,7	14,3	14,3	13,5	13,0	12,4	12,2	11,3	10,8
Outras	3,3	3,7	3,2	2,8	2,1	1,7	1,2	0,8	0,7	0,6
Empresas estatais	2,1	1,7	1,5	1,0	0,9	0,7	0,7	0,6	0,6	0,5
Dívida externa	**9,6**	**15,7**	**11,1**	**7,9**	**3,2**	**-1,1**	**-7,5**	**-11,0**	**-9,0**	**-9,5**
Total	**52,0**	**60,4**	**54,8**	**50,6**	**48,4**	**47,3**	**45,5**	**38,5**	**42,1**	**39,1**

Composição	2011	2012	2013
Dívida interna	**49,4**	**49,4**	**48,7**
Governo Central	38,2	38,0	37,5
Base monetária	5,2	5,3	5,2
Dívida mobiliária	42,7	43,4	42,0
Renegociação E&M	-10,4	-10,4	-10,0
FAT	-4,5	-4,6	-4,3
Créditos Tesouro a inst.fin.of.	-7,7	-9,3	-9,7
Oper. compromissadas	8,3	11,9	11,0
Demais dívidas	4,6	1,7	3,3
Estados/Municípios	**10,7**	**10,9**	**10,7**
Renegociação E&M	10,4	10,4	10,0
Outras	0,3	0,5	0,7
Empresas estatais	**0,5**	**0,5**	**0,5**
Dívida externa	**-13,0**	**-14,1**	**-14,9**
Total	**36,4**	**35,3**	**33,8**

/a A partir de 2001 (inclusive), exclui resultados da Petrobras e compara a dívida pública com o PIB a preços correntes.

/b Em 1991, inclui NCZ$ bloqueados.

Fonte primária: Banco Central.

Elaborado por Fabio Giambiagi

Development of public sector net borrowing per main component parts: in % of GDP – 1991/2013

Composition	**1991 …**
Internal debt	
Central Government	
Monetary base	
Securities debt/b	
E&M renegotiation	
FAT (WPF)	
Treasury Credits to off. fin. inst.	
Committed oper.	
Other debts	
States/Municipalities	
E&M renegotiation	
Others	
State companies(A)	
External debt	
Total	

Composition	**2001 …**
Internal debt	
Central Government	
Monetary base	
Securities debt/b	
E&M renegotiation	
FAT (WPF)	
Treasury Credits to off. fin. inst.	
Committed oper.	
Other debts	
States/Municipalities	
E&M renegotiation	
Others	
State companies(A)	
External debt	
Total	

Composition	**2011 …**
Internal debt	
Central Government	
Monetary base	
Securities debt/b	
E&M renegotiation	
FAT (WPF)	
Treasury Credits to off. fin. inst.	
Committed oper.	
Other debts	
States/Municipalities	
E&M renegotiation	
Others	
State companies(A)	
External debt	
Total	

/a From 2001 (inclusive), excludes results of Petrobras and compares the public debt with GNP at current prices.
/b In 1991, includes blocked NCZ$.

Primary source: Central Bank.
Prepared by Fabio Giambiagi

Resultado fiscal do setor público consolidado (% PIB)

Composição	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Resultado primário	2,71	1,57	2,19	5,21	0,24	-0,09	-0,88	0,01	2,92	3,24
Juros reais	2,88	3,45	2,98	3,96	4,81	3,07	3,11	6,60	3,94	4,33
Juros nominais	n.c.	n.c.	n.c.	n.c.	6,79	5,24	4,62	6,98	8,20	6,61
Atualização monetária	n.c.	n.c.	n.c.	n.c.	1,98	2,17	1,51	0,38	4,26	2,28
NFSP /b										
Operacionais	0,17	1,88	0,79	-1,25	4,57	3,16	3,99	6,59	1,02	1,09
Nominais	n.c.	n.c.	n.c.	n.c.	6,55	5,33	5,50	6,97	5,28	3,37

Composição	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Resultado primário	3,38	3,22	3,27	3,72	3,79	3,20	3,31	3,42	2,00	2,70
Juros reais	4,36	1,04	6,44	2,86	6,85	5,34	2,70	1,91	5,60	0,74
Juros nominais	6,67	7,66	8,51	6,62	7,36	6,83	6,11	5,46	5,28	5,18
Atualiz.monetária	2,31	6,62	2,07	3,76	0,51	1,49	3,41	3,55	-0,32	4,44
NFSP /b										
Operacionais	0,98	-2,18	3,17	-0,86	3,06	2,14	-0,61	-1,51	3,60	-1,96
Nominais	3,29	4,44	5,24	2,90	3,57	3,63	2,80	2,04	3,28	2,48

Composição	2011	2012	2013
Resultado primário	3,11	2,39	1,90
Juros reais	3,78	1,39	2,74
Juros nominais	5,72	4,87	5,18
Atualiz.monetária	1,94	3,48	2,44
NFSP /b			
Operacionais	0,67	-1,00	0,84
Nominais	2,61	2,48	3,28

n.c. Não considerado.

OBS: Os juros nominais anteriores a 1995 não foram considerados porque na época de alta inflação não tinham maior significado econômico.

/a A partir de 2002 (inclusive), exclui resultados da Petrobras. /b (-) = Superávit fiscal.

Fonte: Banco Central.

Elaborado por Fabio Giambiagi

Fiscal result of consolidated public sector (% GNP)

Composition	**1991 …**
Primary result	
Real interest	
Nominal interest	
Monetary adjustment	
NFSP /b	
Operational	
Nominal	

Composition	**2001 …**
Primary result	
Real interest	
Nominal interest	
Monetary adjustment	
NFSP /b	
Operational	
Nominal	

Composition	**2011 …**
Primary result	
Real interest	
Nominal interest	
Monetary adjustment	
NFSP /b	
Operational	
Nominal	

n.c. Not considered
NOTE: Nominal interest before 1995 was not considered because at the time of high inflation it had no more economic significance.
/a From 2002 (inclusive), excludes results of Petrobras. /b = Fiscal surplus.
Source: Central Bank.
Prepared by Fabio Giambiagi

Resultado fiscal – Médias por período: em % PIB - 1985/2013

Períodos Anos	Superávit Primário				Juros nominais	Juros reais	Atualização monetária	Necessidade de Financiamento Deficit	
	GC	EM	EE (A)	**Total**				**Nominais**	Operacionais
1985/89	-0,4	0,1	1,0	**0,7**	n.c.	5,8	n.c.	**n.c.**	5,1
1990/94	1,6	0,6	0,6	**2,8**	n.c.	2,8	n.c.	**n.c.**	0,0
1995/98	0,3	-0,4	-0,1	**-0,2**	5,9	4,4	1,5	**6,1**	4,6
1999/02	1,9	0,6	0,7	**3,2**	7,3	3,4	3,9	**4,1**	0,2
2003/06	2,4	0,9	0,2	**3,5**	7,3	5,4	1,9	**3,8**	1,9
2007/10	2,0	0,8	0,1	**2,9**	5,5	2,7	2,8	**2,6**	-0,2
2011/13	2,0	0,5	0,0	**2,4**	5,2	2,7	2,5	2,6	0,7
2011	2,2	0,8	0,1	**3,1**	5,7	3,8	1,9	**2,6**	0,7
2012	2,0	0,5	-0,1	**2,4**	4,9	1,4	3,5	**2,5**	-1,0
2013	1,6	0,3	0,0	**1,9**	5,2	2,7	2,5	3,3	0,8

(A) A partir de 2002 (inclusive), exclui resultados da Petrobras.
n.c. Não considerado. GC: Governo central; EM: Estados e Municípios; EE: Empresas estatais.
Fonte primária: Banco Central.
Elaborado por Fabio Giambiagi

Fiscal result – Averages per period: in % GDP – 1985/2013

Periods Years	Primary Surplus				Nominal interest	Real interest	Monetary adjustment	Need for Financing Deficit	
	GC	EM	EE(A)	Total				Nominal	Operational

(A) From 2002 (inclusive), excludes results of Petrobras.
n.c. Not considered. GC: Central Government. EM: States and Municipalities. EE: State companies.
Primary source: Central Bank
Prepared by Fabio Giambiagi

Comparação entre itens selecionados de gasto social no Governo Central: 1991 e 2013 (% PIB)

Composição	1991	2013	Diferença
INSS	3,4	7,4	4,0
Inativos Governo Central	0,9	1,7	0,8
Saúde /a	1,4	1,6	0,2
Educação /a	0,1	0,7	0,6
FAT /a	0,6	0,9	0,3
LOAS	0,0	0,7	0,7
Desenvolvimento Social	0,0	0,6	0,6
Soma (A)	6,4	13,6	7,2
Transfer. Estados/Municípios (B)	2,7	3,9	1,2
(A) + (B)	9,1	17,5	8,4

/a Na primeira coluna, dados de 1994 extraídos de Além e Giambiagi (1999) e das Tabelas 5 e 10.
Inclui investimento em saúde, educação e reforma agrária.
Fontes: Tabelas 5, 10 e 12. No caso dos gastos com saúde, educação e reforma agrária, inclui investimentos.
Elaborado por Fabio Giambiagi.

Comparison between selected items of social expenditure in Central Government: 1991 and 2013 (% GDP)

Composition	1991	2013	Difference
INSS			
Central Government – unemployed			
Health /a			
Education /a			
FAT (WPF) /a			
LOAS (SWCA)			
Social Development			
Sum (A)			
Transf. States/Municipalities (B)			

/s In column one, 1994 figures taken from Além and Giambiagi (1999) and from Tables 5 and 10.
Includes investment in health, education and agricultural reform.
Sources: Tables 5, 10 and 12. In the case of expenditure with health, education and agricultural reform, includes investments.
Prepared by Fabio Giambiagi

Resultado primário do Governo Central (% PIB)

Composição	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Receita total	**14,56**	**15,22**	**17,30**	**18,92**	**16,77**	**16,14**	**16,93**	**18,74**	**19,66**	**19,93**
Tesouro/BC	9,97	10,59	11,83	13,91	12,15	11,33	12,22	14,01	15,05	15,21
INSS	4,59	4,63	5,47	5,01	4,62	4,81	4,71	4,73	4,61	4,72
Despesa primária	**13,71**	**14,24**	**15,88**	**16,50**	**16,17**	**15,95**	**16,75**	**18,06**	**17,91**	**18,33**
Transferênc.E&M	2,65	2,67	2,87	2,55	2,60	2,53	2,66	2,91	3,28	3,42
Pessoal	3,80	3,93	4,52	5,14	5,13	4,84	4,27	4,56	4,47	4,57
Ativos	2,66	2,63	2,53	2,82	2,63	2,52	2,25	2,31	2,22	2,39
Inativos	0,91	1,06	1,72	1,99	2,14	2,07	1,82	2,04	2,05	1,97
Transfer.	0,23	0,24	0,27	0,33	0,36	0,25	0,20	0,21	0,20	0,21
Benefícios INSS	3,36	4,25	4,94	4,85	4,62	4,89	5,01	5,45	5,50	5,58
Outras despesas	3,90	3,39	3,55	3,96	3,82	3,69	4,81	5,14	4,66	4,76
Discrep.estatística	0,13	0,12	-0,54	0,83	-0,13	0,15	-0,43	-0,17	0,38	0,13
Superávit primário	**0,98**	**1,10**	**0,88**	**3,25**	**0,47**	**0,34**	**-0,25**	**0,51**	**2,13**	**1,73**
INSS	1,23	0,38	0,53	0,16	0,00	-0,08	-0,30	-0,72	-0,89	-0,86
Tesouro/BC	-0,25	0,72	0,35	3,09	0,47	0,42	0,05	1,23	3,02	2,59

Composição	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Receita total	**20,77**	**21,66**	**20,98**	**21,61**	**22,74**	**22,94**	**23,25**	**23,63**	**22,82**	**22,41**
Tesouro/BC	15,97	16,85	16,23	16,78	17,69	17,73	17,97	18,24	17,20	16,79
INSS	4,80	4,81	4,75	4,83	5,05	5,21	5,28	5,39	5,62	5,62
Despesa primária	**19,30**	**19,76**	**18,68**	**19,08**	**20,29**	**20,88**	**21,08**	**20,81**	**21,60**	**21,17**
Transferênc.E&M	3,53	3,80	3,54	3,48	3,91	3,92	3,97	4,39	3,94	3,73
Pessoal	4,80	4,81	4,46	4,31	4,29	4,45	4,37	4,32	4,68	4,42
Ativos	2,48	2,50	2,32	2,32	2,31	2,40	2,35	2,37	2,59	2,44
Inativos	2,11	2,08	2,11	1,97	1,98	1,86	1,82	1,76	1,89	1,80
Transfer.	0,21	0,23	0,03	0,02	0,00	0,19	0,20	0,19	0,20	0,18
Benefícios INSS	5,78	5,96	6,30	6,48	6,80	6,99	6,96	6,58	6,94	6,76
Outras despesas	5,19	5,19	4,38	4,81	5,29	5,52	5,78	5,52	6,04	6,26
Fdo.Soberano do Brasil								-0,47	0,00	0,00
Capitalização Petrobras										0,85
Ajuste metodológico/a	0,00	0,00	0,00	0,14	0,11	0,11	0,07	0,04	0,04	0,03
Discrep.estatística	0,22	0,26	-0,02	0,03	0,04	0,00	-0,01	-0,04	0,05	-0,03
Superávit primário	**1,69**	**2,16**	**2,28**	**2,70**	**2,60**	**2,17**	**2,23**	**2,35**	**1,31**	**2,09**
INSS	-0,98	-1,15	-1,55	-1,65	-1,75	-1,78	-1,68	-1,19	-1,32	-1,14
Tesouro/BC	2,67	3,31	3,83	4,35	4,35	3,95	3,91	3,54	2,63	3,23

Composição	2011	2012	2013
Receita total	**23,91**	**24,18**	**24,57**
Tesouro/BC	17,97	17,90	18,18
INSS	5,94	6,28	6,39
Despesa primária	**21,64**	**22,46**	**22,97**
Transferênc.E&M	4,16	4,13	3,95
Pessoal	4,33	4,24	4,22
Ativos	2,38	2,32	
Inativos	1,77	1,73	
Transfer.	0,18	0,19	
Benefícios INSS	6,79	7,21	7,43
Outras despesas	6,36	6,88	7,37
Fdo.Soberano do Brasil	0,00	0,28	0,00
Ajuste metodológico/a	0,03	0,03	0,02
Discrep.estatística	-0,05	-0,07	-0,05
Superávit primário	**2,25**	**1,96**	**1,57**
INSS	-0,85	-0,93	-1,04
Tesouro/BC	3,10	2,89	2,61

/a Recursos referentes à amortização de contratos de Itaipu com o Tesouro Nacional. n.d.: Não disponível.

Fontes: Até 1996, SPE. A partir de 1997, STN. Dados de despesa de pessoal calculados com base na participação de ativos e inativos nas despesas apuradas pelo Ministério de Administração. A partir de 1995, cálculos do Ministério de Planejamento.

Elaborado por Fabio Giambiagi

Primary result of Central Government (% GDP)

Composition	**1991 …**
Total revenue	
Treasury/CB	
INSS	
Primary expenditure	
Transfer E&M	
Personnel	
Employed	
Unemployed	
Transfer	
INSS benefits	
Other expenditure	
Statistical discrep.	
Primary surplus	
INSS	
Treasury/CB	

Composition	**2001 …**
Total revenue	
Treasury/CB	
INSS	
Primary expenditure	
Transfer E&M	
Personnel	
Employed	
Unemployed	
Transfer	
INSS benefits	
Other expenditure	
Statistical discrep,	
Primary surplus	
INSS	
Treasury/CB	

Composition	**2011 …**
Total revenue	
Treasury/CB	
INSS	
Primary expenditure	
Transfer E&M	
Personnel	
Employed	
Unemployed	
Transfer	
INSS benefits	
Other expenditure	

Statistical discrep.

Primary surplus
INSS
Treasury/CB

/a Resources referring to amortization of Itaipu contracts with National Treasury.
n.d: not available.
Sources: Up to 1996, SPE. From 1997, STN. Figures of personnel expenditure calculated on basis of share of employed and unemployed in the expenditure checked by the Home Office. From 1995, calculations of the Ministry of Planning.
Prepared by Fabio Giambiagi

EVOLUÇÃO DA CARGA TRIBUTÁRIA GLOBAL - 1947/2013p

(Em % do PIB)

ANO	CARGA	ANO	CARGA	ANO	CARGA	ANO	CARGA	ANO	CARGA
1947	13,84	**1962**	15,76	**1977**	25,55	**1992**	25,01	**2007**	35,35
1948	14,03	**1963**	16,05	**1978**	25,70	**1993**	25,78	**2008**	35,60
1949	14,39	**1964**	17,02	**1979**	24,66	**1994**	29,75	**2009**	34,18
1950	14,42	**1965**	18,99	**1980**	24,52	**1995**	26,93	**2010**	34,19
1951	15,74	**1966**	20,95	**1981**	25,25	**1996**	26,85	**2011**	35,75
1952	15,41	**1967**	20,47	**1982**	26,34	**1997**	27,41	**2012**	37,13
1953	15,20	**1968**	23,29	**1983**	26,97	**1998**	27,67	**2013/p**	37,65
1954	15,82	**1969**	24,87	**1984**	24,34	**1999**	29,00	**2014**	
1955	15,05	**1970**	25,98	**1985**	24,06	**2000**	31,15	**2015**	
1956	16,42	**1971**	25,26	**1986**	26,19	**2001**	32,33	**2016**	
1957	16,66	**1972**	26,01	**1987**	23,77	**2002**	33,37	**2017**	
1958	18,70	**1973**	25,05	**1988**	22,43	**2003**	32,82	**2018**	
1959	17,86	**1974**	25,05	**1989**	24,13	**2004**	33,69	**2019**	
1960	17,41	**1975**	25,22	**1990**	28,78	**2005**	34,95	**2020**	
1961	16,38	**1976**	25,14	**1991**	25,24	**2006**	34,79	**2021**	

Fonte primária: IBGE, FGV, Min.Fazenda, FGTS, CONFAZ.
(p) Projeção Preliminar

DEVELOPMENT OF OVERAL TAX BURDEN – 1947/2013p

(In % of GNP)

YEAR	CHARGE	YEAR	CHARGE	YEAR	CHARGE	YEAR	CHARGE	YEAR	CHARGE

Primary source: IBGE, FGV, Exchequer, FGTS, CONFAZ.
(p) Preliminary Projection

EVOLUÇÃO DA DIVISÃO FEDERATIVA DA RECEITA TRIBUTÁRIA POR NÍVEL DE GOVERNO - 1960/2012
(conceito contas nacionais)

Conceito	Central	Estadual	Local	Total	Central	Estadual	Local	Total
	Carga - % do PIB				Composição - % do Total			
ARRECADAÇÃO DIRETA								
1960	11,14	5,45	0,82	**17,41**	64,0	31,3	4,7	100,0
1970	17,33	7,95	0,70	**25,98**	66,7	30,6	2,7	100,0
1980	18,31	5,31	0,90	**24,52**	74,7	21,6	3,7	100,0
1985	17,50	5,98	0,58	**24,06**	72,7	24,9	2,4	100,0
1988	16,08	5,74	0,61	**22,43**	71,7	25,6	2,7	100,0
2000	20,77	8,61	1,77	**31,15**	66,7	27,6	5,7	100,0
2012	25,21	9,58	2,33	**37,13**	67,9	25,8	6,3	100,0
RECEITA DISPONÍVEL								
1960	10,37	5,94	1,11	**17,41**	59,5	34,1	6,4	100,0
1970	15,79	7,59	2,60	**25,98**	60,8	29,2	10,0	100,0
1980	16,71	5,70	2,10	**24,52**	68,2	23,3	8,6	100,0
1988	13,48	5,97	2,98	**22,43**	60,1	26,6	13,3	100,0
2000	17,38	8,19	5,58	**31,15**	55,8	26,3	17,9	100,0
2012	21,14	9,12	6,87	**37,13**	56,9	24,6	18,5	100,0

Fonte: Elaboração própria, a partir de STN, SRF, IBGE, Ministério da Previdência, CEF, Confaz e Balanços Municipais.
Metodologia das contas nacionais inclui impostos, taxas e contribuições, inclusive CPMF, FGTS e royalties, bem assim dívida ativa.
Receita Disponível = arrecadação própria mais e/ou menos repartição constitucional de receitas.

DEVELOPMENT OF FEDERAL DIVISION OF TAX REVENUE PER LEVEL OF GOVERNMENT – 1960/2012
(national accounts item)

Item	Central	State	Local	Total	Central	State	Local	Total
	Charge - % of GDP				Charge - % of GDP			
DIRECT COLLECTION								
AVAILABLE REVENUE								

Source: Own preparation, from STN, SRF, IBGE, Ministry of Social Security, CEF, Confaz and Municipal Balances.
Method of national accounts includes taxes, duties and contributions, including CPMF, FGTS and royalties, as well as active debt.
Available Revenue = own collection more and/or less constitutional division of revenue.

EVOLUÇÃO DA DÍVIDA PÚBLICA E DE CRÉDITOS DO SISTEMA FINANCEIRO: em % DO PIB - 2000/2014

Variáveis	Dez/00	Dez/05	Dez/07	Dez/10	Dez/13	Dez/13-07
DÍVIDA PÚBLICA E DEDUÇÕES						
Deduções Crédito Total Govern., inclusive pra Bancos	8,5%	9,8%	8,5%	14,0%	16,3%	7,8%
Dívida Mobiliária em Mercado	33,7%	44,3%	45,1%	42,2%	41,8%	-3,2%
Dívida Líquida do Setor Público (DLSP)	47,7%	48,2%	45,1%	39,1%	33,8%	-11,3%
Dívida Pública Mobiliária Federal em poder do público (DPMFI)	43,3%	45,6%	46,0%	42,5%	42,2%	-3,8%
Dívida Bruta do Governo Geral (DBGG-metodologia pós 2008)	52,2%	56,4%	58,0%	53,4%	57,2%	-0,8%
Dívida Bruta do Governo Geral (DBGG-metodologia até 2007)	63,2%	67,7%	64,4%	64,4%	66,1%	1,7%
OPERAÇÕES DE CRÉDITO						
Recursos Discricionários	11,5%	9,5%	10,3%	15,6%	25,1%	14,8%
Instituições Financeiras Públicas	12,0%	10,4%	12,0%	18,9%	28,9%	17,0%
Total do Sistema Financeiro Nacional	27,4%	28,3%	35,2%	45,2%	56,5%	21,3%

Elaboração própria. Fonte primária: BACEN (notas da política fiscal e de crédito, bem assim séries históricas).
Deduções de Créditos Governamentias compreendem valores abatidos na apuração da DLSP: recursos do FAT na rede bancária; créditos concedidos para instituições financeiras oficiais (instrumentos híbridos e ao BNDES), aplicações de fundos e programas financeiros, e créditos junto às estatais.
DPMFI em poder público calculada pelo BACEN na nota do mercado aberto .

DEVELOPMENT OF PUBLIC DEBT AND FINANCIAL SYSTEM CREDITS: in % of GDP – 2000/2014

Variables Dec/00 Dec/05 Dec/07 Dec/10 Dec/13 Dec/13-07

PUBLIC DEBT AND DEDUCTIONS
Gov. Total Credit Deductions, incl. for Banks
Securities Debt on Market
Liquid Debt of Public Sector (DLSP)
Federal Securities Public Debt in public control (DPMFI)
General Gov. Gross Debt (DBGG – method post-2008)
General Gov. Gross Debt (DBGG – method up to 2007)

CREDIT OPERATIONS
Discretionary Resources
Public Financial Institutions
Total of National Financial System

Own preparation. Primary source: BACEN (notes of fiscal and credit policy, as well as historical series).
Deductions of Governmental Credits include decreased values in the DLSP calculation: FAT (WPF) resources in the banking system; credits granted for official financial institutions (hybrid instruments and to BNDES), application of funds and financial programmes, and credits with state ones.
DPMFI in public control calculated by the BACEN in the open market note.