OECD Economic Surveys

Brazil

December 2020

OVERVIEW

Executive summary
The COVID-19 outbreak has plunged the economy into a deep recession

COVID-19 caused severe human suffering and triggered a deep recession. Rekindling economic activity past the trough intensifies the urgency of addressing underlying policy challenges.

Economic policies reacted in a timely and decisive manner to the COVID-19 crisis, supporting millions of Brazilians. But the pandemic will nonetheless cause GDP to drop by 5% (Table 1).

Table 1. The economy is in a deep recession

<table>
<thead>
<tr>
<th></th>
<th>2020</th>
<th>2021</th>
<th>2022</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross domestic product</td>
<td>-5.0</td>
<td>2.6</td>
<td>2.2</td>
</tr>
<tr>
<td>Private consumption</td>
<td>-6.2</td>
<td>2.7</td>
<td>2.2</td>
</tr>
<tr>
<td>Government consumption</td>
<td>-4.8</td>
<td>0.5</td>
<td>0.0</td>
</tr>
<tr>
<td>Gross fixed capital formation</td>
<td>-5.1</td>
<td>4.4</td>
<td>5.6</td>
</tr>
<tr>
<td>Exports</td>
<td>-2.0</td>
<td>-0.6</td>
<td>4.0</td>
</tr>
<tr>
<td>Imports</td>
<td>-14.3</td>
<td>-4.4</td>
<td>4.6</td>
</tr>
<tr>
<td>Unemployment rate</td>
<td>13.6</td>
<td>16.0</td>
<td>15.0</td>
</tr>
<tr>
<td>Consumer price index</td>
<td>3.1</td>
<td>3.6</td>
<td>3.2</td>
</tr>
<tr>
<td>Consumer price index (Dec-Dec)</td>
<td>3.8</td>
<td>2.9</td>
<td>3.4</td>
</tr>
<tr>
<td>Headline fiscal balance</td>
<td>-15.6</td>
<td>-7.2</td>
<td>-6.3</td>
</tr>
<tr>
<td>Primary fiscal balance</td>
<td>-10.7</td>
<td>-2.8</td>
<td>-2.3</td>
</tr>
<tr>
<td>Public debt (gross, % of GDP)</td>
<td>91.4</td>
<td>94.3</td>
<td>96.6</td>
</tr>
<tr>
<td>Current account (% of GDP)</td>
<td>-0.3</td>
<td>-0.5</td>
<td>-0.9</td>
</tr>
</tbody>
</table>

Source: OECD projections.

A strong recovery from the recession will require long-lasting improvements in economic policies. A rising labour force and strong commodity prices will no longer underpin growth and public revenues. Instead, the boost to growth from demographics since the year 2000 will be fully reversed over the next 25 years (Figure 1). Productivity, which ultimately drives prosperity, will need to become the engine of growth, following decades of virtual stagnation. Without deep structural reforms to boost productivity, the recovery will be protracted and disappointing. Inflation risks have been contained for some time, but formalising the de-facto independence of the Central Bank could lock in this progress.

Financial intermediation is still limited with total credit around 50% of GDP, but the structure of financial markets is improving visibly. Directed lending operations, long at par with free credit, are receding, following a reduction of interest rate subsidies. This is allowing private banks and corporate bond markets to raise their participation in financial markets. Lending spreads are still high and point to scope for stronger competition in the financial sector, but an ambitious policy agenda aiming at reducing financing costs has been put in place.

Deforestation is a major source of greenhouse gas emissions and has recently rebounded. Current laws and protections have proven capable to reduce deforestation in the past and should be preserved. But they will only be effective when coupled with stronger enforcement efforts to combat illegal deforestation, which will require additional resources.

Raising spending efficiency is needed to address fiscal challenges

Improving fiscal outcomes remains one of Brazil’s principal challenges given a high debt burden, to which the pandemic has added 15 percentage points of GDP (Figure 2). Fiscal adjustment must resume after the crisis, but can be achieved by improving spending efficiency with no need for higher tax rates or new taxes and without detriment to growth or inclusiveness.
Plenty of scope exists for reviewing tax expenditures, including ineffective subsidies to specific activities and special tax regimes, while a public employment reform could generate savings and improve public administration at the same time. Many current expenditures have increased due to revenue earmarking, mandatory spending floors or indexation mechanisms, shifting spending away from where it is most needed, including investment. Reforming mandatory spending items and indexation rules is inevitable to deliver the needed fiscal adjustment and to avoid breaking fiscal rules, which would trigger confidence losses and could derail the recovery.

Figure 2. Gross public debt has shot up

![Graph showing gross public debt](image)

Source: OECD projections, BCB, National Treasury.

StatLink [https://doi.org/10.1787/888934196157](https://doi.org/10.1787/888934196157)

Raising the efficiency of public spending will not be possible without building on remarkable past progress in the fight against corruption and economic crimes. Strong and autonomous enforcement bodies can ensure this, provided that the law provides a credible threat of prosecution.

Large inequalities along several dimensions affect well-being. The richest 10% of the population earn more than four times as much as the bottom 40%. Inequality and poverty have fallen over the past two decades due to strong growth, improvements in education and social transfers. Social benefits amount to over 15% of GDP and are characterised by poor targeting, with almost half of transfers reaching the highest income quintile (Figure 3).

Reviewing current indexation arrangements could free resources for more efficient transfers and generate significant poverty reductions at a low fiscal cost.

Figure 3. Social transfers are not well targeted

Distribution of social transfer spending by quintile of the income distribution (1=lowest income quintile)

![Graph showing social transfer distribution](image)

Source: SEAE

StatLink [https://doi.org/10.1787/888934196176](https://doi.org/10.1787/888934196176)

Well-targeted conditional cash transfers could be expanded and converted into a true social safety net by accelerating benefit concessions in the case of dismissal and withdrawing them more gradually to strengthen job search incentives. This would support informal workers, which account for one third of employment and are not covered by unemployment schemes, and could revert the recent rise of poverty rates and inequality (Figure 4).

Figure 4. Poverty and inequality have edged up

![Graph showing poverty and inequality](image)

Source: IBGE.

StatLink [https://doi.org/10.1787/888934196195](https://doi.org/10.1787/888934196195)
Reviving productivity is the key for a strong recovery of incomes

Realising Brazil’s potential and improving well-being and living standards will only be possible through ambitious structural reforms that boost productivity.

With large parts of the economy shielded from competition, firms face limited incentives to become more productive. Reallocation mechanisms like entry and exit appear weaker than elsewhere, leaving many jobs trapped in firms and activities with little potential for improving productivity and wages. Domestic regulatory burdens and market entry barriers are among the world’s highest (Figure 5).

Figure 5. Product market regulation hampers competition

![PMR indicator graph](https://doi.org/10.1787/888934196214)

Source: OECD PMR Indicators Database.

External competition is hampered by high trade barriers that have cut off Brazil from the opportunities of international trade (Figure 6). Trade barriers are even higher for capital goods and intermediate inputs, elevating domestic production costs.

Figure 6. Average tariff rates are high

![Tariff rates graph](https://doi.org/10.1787/888934196233)

Source: Wits.

Well-designed training policies are key

Deeper integration into the global economy and rising domestic competition would boost productivity, including by facilitating the movement of jobs towards more productive firms and activities. But these structural changes create challenges for workers. Well-designed training and education policies can go a long way to help workers master the transition.

Opportunities for skill upgrading will facilitate the move into new and better-paying jobs and strengthen productivity at the same time.

Scaling up training policies can be a highly effective way to mitigate local employment effects in trade-exposed regions if course content is aligned with skill demands in local labour markets. Strengthening incentives for training institutions to raise employability of participants can help to achieve a better alignment with market demand. Facilitating a better adoption of vocational content in secondary education could also help to prepare youths effectively for a changing economic environment. Together with an expansion of early-childhood education, this could reduce early drop-out rates and foster inclusiveness.
### MAIN FINDINGS

<table>
<thead>
<tr>
<th>Improving macroeconomic policies, governance and social protection</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>COVID19 has caused a strong recession. Inflation and inflation expectations are below target and monetary policy has been relaxed.</strong></td>
</tr>
<tr>
<td><strong>The Central Bank has conducted monetary policy in an independent way but formalising this independence would strengthen monetary policy effectiveness.</strong></td>
</tr>
<tr>
<td><strong>Fiscal outcomes require significant improvements as the pandemic has added to high public debt.</strong></td>
</tr>
<tr>
<td><strong>Better spending would allow savings without jeopardising policy objectives.</strong></td>
</tr>
<tr>
<td><strong>Mandatory spending items have reduced the room for fiscal policy as over 90% of the budget is now determined by law.</strong></td>
</tr>
<tr>
<td><strong>Despite large social transfers, there is no universal social safety net to protect dismissed workers against income losses. Recent emergency benefits improved this temporarily.</strong></td>
</tr>
<tr>
<td><strong>Lengthy appeal procedures lead to court congestion and long delays between sentences and their execution. In penal cases, wealthy defendants can avoid serving prison sentences over many years.</strong></td>
</tr>
<tr>
<td><strong>Whistle-blowing procedures are presently hampered by concurrent competences and parallel systems for similar offences, which make it difficult to protect whistle-blowers effectively.</strong></td>
</tr>
</tbody>
</table>

### KEY RECOMMENDATIONS

| Keep interest rates low until inflationary pressures become clearly visible. |
| Apply fixed-term appointments for the Central Bank governor and directors and limit earlier dismissal to severe misconduct. Safeguard the budget autonomy of the Central Bank. |
| Ensure fiscal sustainability by adhering to current fiscal rules, including the expenditure ceiling. |
| Strengthen spending efficiency by reviewing civil servant pay structures, ineffective subsidies, special tax regimes and tax expenditures. |
| Reduce budget rigidity by reviewing revenue earmarking, mandatory spending floors and indexation mechanisms. |
| Increase benefits and accelerate benefit concessions in the Bolsa Família programme, while withdrawing benefits only gradually. |
| Consider creating the legal basis for executing sentences as of the second instance of appeal, or limit the number of appeals, including to the Supreme Court. |
| Implement a dedicated whistle-blower protection law. |

### Making growth greener and more sustainable

| Brazil has a strong legal framework to protect forests. Deforestation declined up to 2014 but has risen since, particularly in recent years. Enforcement action has declined significantly, reflecting budget and staff cuts. |
| Political discussions have sent mixed signals about the commitment to the existing environmental protection framework. |
| Build on past success in fighting illegal deforestation by strengthening enforcement efforts to combat illegal deforestation and ensuring adequate staffing and budget of environmental enforcement agencies. |
| Avoid a weakening of the current legal protection framework, including protected areas, the forest code, and focus on the sustainable use of the Amazon’s economic potential. |

### Raising productivity

| Administrative barriers and product market regulation restrict market entry and hamper competition. |
| High trade barriers deprive the economy from the benefits of international competition. |
| Taxes are high and compliance costs generated by a fragmented system of indirect taxes are large. High tax litigation adds to court congestion. |
| Judicial uncertainty entails costs for private enterprises. Courts are required to align their decisions with precedence rulings by superior courts, but there is no enforcement mechanism. |
| Further simplify license requirements for starting a company and apply silence-is-consent rules and one-stop shops wherever possible. |
| Reduce tariff and non-tariff barriers, starting with capital goods and intermediate inputs. |
| Consolidate consumption taxes into one value added tax. |
| Ensure the alignment of court decisions with precedence rulings of superior courts by linking judges’ promotions and salaries to compliance with the rules. |

### Improving skills, education and professional training

| High secondary drop-out rates reflect a lack of basic social and cognitive skills. Female labour force participation is hampered by lack of childcare facilities, particularly in low-income areas. |
| Structural reforms like stronger competition and global integration will reallocate jobs across firms and sectors. |
| Scale up resources for professional training courses, but ensure their alignment with local labour market needs. |
The COVID-19 pandemic has caused severe human suffering and triggered a deep recession in Brazil. Economic policies reacted in a timely and decisive manner to the crisis, supporting millions of Brazilians. But a strong and inclusive recovery from the recession will require long-lasting improvements in economic policies. Challenges include improving fiscal outcomes, fighting corruption, strengthening social protection, raising productivity and improving education and training policies.
The COVID-19 outbreak caused severe human suffering in Brazil, with around 6.5 million infections and 175,000 deaths attributed to the disease by early December 2020. The pandemic also reversed a gradual recovery from the last downturn and plunged the economy into another, even deeper recession (Figure 1.1). Domestic consumption and investment declined as millions lost their livelihoods. Economic policies responded in a timely and decisive manner by providing income support for millions of Brazilians, financing short-time work, facilitating a credit expansion, postponing taxes and anticipating benefit disbursements (Box 1.1).

Figure 1.1. After a weak recovery, the economy has plunged into another recession

The pandemic has significantly affected well-being and prosperity. The current need to rekindle economic activity only intensifies the urgency of tackling long-standing structural policy challenges. In the past, these have been partly concealed by favourable demographics and high commodity prices, which allowed a simultaneous expansion of private and public consumption even as productivity growth, the ultimate engine of growth, was virtually stagnant. But demographics reached a turning point in 2019 (Figure 1.2). Over the next 25 years, rapid population ageing will reverse the entire boost to growth from demographics since the year 2000 (IBGE, 2018[1]). Among OECD countries, only Korea and Costa Rica will age more rapidly. On current policies, this will slow down the economy’s growth potential substantially, to around 1.5% per annum, and calls for a substantial overhaul of the growth model of the past.

Figure 1.2. Demographics will no longer support economic growth
Box 1.1. Policy responses to the COVID-19 pandemic

Economic policy responses included new spending measures exceeding 8% of GDP in 2020, for which the expenditure rule has been temporarily suspended. The central government will provide financial assistance to states and municipalities, which are responsible for most health expenditures. Monetary support and regulatory measures have supported additional credit extension to help firms through the trough. Main measures include:

- **Income support measures for low-income workers**: A new temporary emergency benefit of BRL 600 per month over five months, was paid to over 67 million informal, self-employed or unemployed workers earning up to half the minimum wage during April – August 2020. It will be continued until December 2020 at half its previous level. The amount doubled for single parents and, as a side effect, it has led to significant progress in expanding access to basic banking services. Conditional cash transfer programmes have received resources to enrol 1.2 million additional beneficiaries. A short-time work scheme with public income support from unemployment insurance compensated income losses of formal workers and alleviated wage costs for employers in exchange for job guarantees.

- **Support to businesses**: Policy support for SMEs included a low-interest credit line to cover wages for employees earning up to two-times the minimum wage, with the credit risk borne by the federal government and a government fund to provide guarantee for SME loans that could potentially reach 3.2 million firms. Additional new corporate credit lines were created by the national development bank. Tax liabilities and other charges on firms were postponed, with a particular focus on SMEs. Temporary exemptions from certain labour regulations, the possibility to advance annual leave and other measures create further flexibility in working hours for firms.

- **Credit and liquidity measures**: Monetary policy support has reduced interest rates by a joint 250 basis points, combined with prudential and regulatory measures that allow additional credit extension of up to 18.5% of GDP.

Weak growth prospects are not the only challenge: Despite impressive social progress over many years, well-being indicators show a mixed picture. The OECD Better Life index shows strong performance in civic engagement, and average performance in community and life satisfaction (Figure 1.3). In the areas of income and wealth, safety, education housing and health, however, Brazil’s performance is among the lowest in the sample and is likely to deteriorate further with the current deep recession.

Figure 1.3. Well-being indicators

Note: The numbers indicate Brazil’s ranking among the 38 countries comprised in the index.
Source: OECD Better Life Index.

StatLink [https://doi.org/10.1787/888934196290](https://doi.org/10.1787/888934196290)
Large inequalities are one factor affecting well-being and they have been rising again after years of decline. The bottom 40% of income earners receive 10% of disposable incomes, while the top 10% pocket more than four times as much. Female workers earn 20% less than men, compared to 13% for the OECD average. Women are more likely to be in informal employment and poverty is four times the national average among informal workers. White Brazilians earn two thirds more than other ethnic groups, while the latter are 60% more likely to lack access to basic sanitation and more than twice as likely to be illiterate.

**Figure 1.4. Women are facing sizeable wage gaps**


Regional disparities are another crucial challenge. Average incomes in the north-eastern state of Maranhão are less than half of the national average, and the opposite holds for poverty (Figure 1.5). Labour market informality and illiteracy are three to four times more common in the poorer north-eastern states than in the relatively affluent southeast.

**Figure 1.5. Prosperity gaps across regions are large**

In addition, improving well-being will require addressing challenges in economic governance and institutions. Corrupt practices exposed in recent years have wasted public resources and exacerbated income inequalities. Finally, protecting Brazil’s unique natural resources such as the Amazon rainforest will benefit generations of Brazilians, and has a social value far exceeding the short-term private benefits from deforestation.

The strength of the recovery will hinge on economic reforms

Ambitious structural reforms that raise productivity would help to boost growth and to realise Brazil’s potential. Without support from demographics, further progress in material living standards will hinge crucially on productivity growth, which must become the basis for more and better remunerated jobs for all Brazilians, as discussed in Chapter 2 (OECD, 2018[2]; Dutz, 2018[3]). Following decades of slow reform momentum, many of Brazil’s institutional and policy settings were made for a world that is very different from the challenges of today.

Brazil can build on impressive reform progress made in recent years (Box 1.2). A successful pension reform has been key to improve both the financial sustainability and the redistributive character of Brazil’s large pension system (Box 1.3). A reduction of credit subsidies has opened space for more competition and innovation in financial markets. The federal government contribution to basic education FUNDEB, which has been instrumental for the increase in school enrolment over the years, has been made permanent and more than doubled in volume, and it has incorporated monetary incentives for local governments to raise the quality of education. Congress is discussing tax, administrative and civil service reforms, a new insolvency law, a new framework for fiscal relations with states and municipalities, including clearer rules for sharing oil revenues, and measures to enhance budget flexibility. Moreover, recent corruption convictions reflect stronger institutions, including a judiciary that has not shied away from pursuing and sentencing senior leaders.

Box 1.2. Recent and ongoing reform initiatives since 2017

- A pension reform has improved the sustainability and the redistributive character of Brazil’s pension system.
- A draft for an administrative reform affecting civil servants, fiscal relations with states and municipalities and budget flexibility has been submitted to Congress.
- A draft law with refinements to the expenditure rule is being discussed by Congress.
- A new independent fiscal council produces high-quality monthly reports.
- A draft for a first phase of a tax reform has been submitted to Congress.
- Directed lending rates have been aligned with market rates. As a result, interest subsidies and directed lending volumes have declined.
- A new and comprehensive credit registry has been created.
- Regulatory changes are fostering competition in financial markets, including by facilitating the emergence of FinTech companies and open banking.
- A new legal framework for investments in sanitation was approved in 2020.
- Competition in the oil and gas sector has been strengthened.
- Trade agreements with the European Union and EFTA have been concluded successfully. Brazil has started the adherence process to the government procurement agreement of the WTO. Foreign exchange regulations are being aligned with OECD best practices.
- A 2020 law reduces the bureaucracy and eases regulations for opening a business and obtaining licenses.
- A 2017 labour market reform has increased the scope for firm-level agreements to take prevalence over the law, which provides a legal basis for long-standing practice and reduces legal uncertainties, while preserving essential employee rights as non-negotiable. The reform has also strengthened incentives for formal hiring.
- Recipients of conditional cash transfers were granted a 13th monthly payment.
- Labour tax wedges were cut for low-income earners aged below 29 and above 55.
- A 2017 upper secondary education reform has introduced a nationwide common core curriculum from early childhood to secondary school while making curriculums outside the common core more flexible, reducing the mandatory subjects and allowing a better tailoring of curriculums to different student needs. The reform also mandates longer school hours and can help to reduce early school drop-out.

Finding the necessary political consensus for further reforms will not be easy. Many reforms will require changes to many detailed provisions contained in Brazil’s 1988 constitution with supermajorities. Today’s fragmented political landscape and the more limited fiscal room adds to these difficulties, as in the past consensus was often achieved on the back of significant inefficiencies in government spending. But in the current context, a failure to reform will hold back economic progress and difficult political choices will have to be made either way, of which inaction may often be the least attractive one. At the same time, there have been significant initiatives in both the executive and more recently also in the legislative branch to garner consensus around a constructive reform agenda.

The payoff of reform progress would be substantial and rapid enough to be politically appealing, according to estimates based on the OECD long-term growth model (Guillemette and Turner, 2018[4]). An ambitious package that would improve domestic regulation and competition, reduce barriers to foreign trade and improve institutions and economic governance, would generate an average annual growth dividend of 0.9 percentage points over 15 years (Figure 1.6). This would accelerate the recovery and approximately double the currently projected potential per capita growth by 2035. Over time, the growth benefits would continue to rise until reaching 2 percentage points of GDP by 2060. Stronger growth implies that per capita GDP could be 13% higher after 15 years (Table 1.1).

Figure 1.6. An ambitious structural reform package can lift growth

Effects on the growth of GDP per capita

<table>
<thead>
<tr>
<th>% pt.</th>
<th>Employment rate</th>
<th>Capital per worker</th>
<th>Labour efficiency</th>
<th>Potential output per capita</th>
</tr>
</thead>
<tbody>
<tr>
<td>2020</td>
<td>0</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2025</td>
<td>0.2</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2030</td>
<td>0.4</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2035</td>
<td>0.6</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2040</td>
<td>0.8</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2050</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2060</td>
<td>1.2</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2070</td>
<td>1.4</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2080</td>
<td>1.6</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: OECD calculations.

[StatLink](https://doi.org/10.1787/888934196347)
Table 1.1. Expected gains from structural reform are substantial

Estimated impact of selected reforms on real GDP after 15 years

<table>
<thead>
<tr>
<th>Reform</th>
<th>Impact on real GDP</th>
<th>Impact on real GDP per capita</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scenario A: Reduce barriers to entrepreneurship and competition (e.g. by cutting administrative burdens and streamlining licensing requirements)</td>
<td>5.3%</td>
<td>4.9%</td>
</tr>
<tr>
<td>Scenario B: Stronger global integration (e.g. by reducing tariffs and opening the capital account)</td>
<td>8.0%</td>
<td>7.4%</td>
</tr>
<tr>
<td>Scenario C: Improve institutions, economic governance and reduce corruption</td>
<td>6.3%</td>
<td>5.9%</td>
</tr>
<tr>
<td>Ambitious reform scenario: all of the above together</td>
<td>14.1%</td>
<td>13.2%</td>
</tr>
<tr>
<td>Implied average annual growth increase (of ambitious reform scenario):</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>0.9 % points</td>
<td>0.9 % points</td>
</tr>
</tbody>
</table>

Note: These estimates were obtained on the basis of the OECD Long term growth model (Guillemette and Turner, 2018[4]). Scenario A assumes aligning product market regulations as captured by the OECD PMR indicator with the current OECD average by 2060. Scenario B assumes a reduction in average tariffs by around 7 percentage points by 2025, when they would reach the level prevalent today in the five OECD economies with the lowest tariffs. In addition, the capital account is assumed to open gradually to reach Chile’s current level by 2025. Scenario C assumes that institutional quality, as captured by the rule of law index (Kaufmann, Kraay and Mastruzzi, 2010[5]), converges to the current OECD median value by 2060. The individual reform effects do not sum up to the effect of the ambitious reform scenario due to non-linear effects in the model. Source: OECD calculations.

The sequencing of reforms may also play a major role for their success. Reforms often trigger a reallocation of production factors to more productive firms and sectors, as one of the key channels through which productivity and growth are boosted. This can entail significant adjustment costs, particularly if distortions in product and factor markets hamper the ability of factors to move (OECD, 2012[6]; Autor, Dorn and Hanson, 2013[7]). Policies that enhance flexibility and facilitate the reallocation of labour and capital across firms, sectors and regions can significantly reduce these adjustment costs (OECD, 2005[8]; OECD, 2012[6]). The credit, labour market and regulatory reforms that Brazil has undertaken in recent years, for example, will be helpful in this context. At the same time, the sequencing of reforms crucially depends on the domestic political context and the momentum for reform (VanGrasstek, 2011[9]; OECD, 2005[8]).

Against this background, the main messages of the Survey are:

- Ensuring fiscal sustainability after the COVID-19 crisis will require improving the effectiveness of public spending, including better economic governance and more effective public transfers.
- Raising productivity to boost growth after the crisis and over the longer run will require structural reforms. Key areas are competition, regulatory burdens, trade barriers, the simplification of taxes and judicial efficiency.
- Preparing workers for job reallocations due to structural changes – including those the COVID-19 crisis is likely to bring about – will require improvements in skill and education policies.
Box 1.3. Brazil’s 2019 pension reform

In November 2019, Brazil approved a pension reform containing a wide range of parametric changes. These included the introduction of a general minimum age of 62 years for women and 65 for men, while previously retirements based on years of contribution led to effective retirement ages of 53 years for women and 56 for men. Contribution rates were made progressive, leading to visibly higher contributions for high-wage earners and to lower rates for minimum wage earners. Survivor pensions will no longer be 100% of the deceased spouse’s pension, but vary according to the number of dependants. Limits on the accumulation of benefits were also introduced.

The reform improves the distributional footprint of the pension system. By establishing a binding retirement age, it ended the current practice where low-income earners with part of their working life in informal employment retire later than others who retire on the basis of years of formal contributions. Moreover, the reform reduces inequalities between the private sector regime and the public sector regime, as the latter was significantly more generous before. The overall expected savings of 10% of GDP over 10 years are sizeable. The pension reform, which had been recommended in the 2015 and 2018 OECD Economic Surveys of Brazil, is an important achievement.

COVID-19 has plunged the economy back into a long and deep recession

Brazil saw a decade of strong growth at the outset of the new millennium, buoyed by rising commodity prices and favourable demographic developments. Growth then declined drastically as of 2012. The need for structural reforms to boost stagnant productivity became increasingly visible and fiscal accounts were on an unsustainable track. Confidence suffered from a lack of political resolve to address these issues, eventually leading into a deep recession in 2015/16. Public debt rose by 20 percentage points within only three years, while inflation climbed into double digits. As of 2017/2018, slowly improving fiscal prospects, lower inflation and lower interest rates had begun to lift confidence.

The short-term prospects will depend on the health situation

Brazil recorded the first COVID-19 case in late February of 2020. Deaths increased rapidly and Brazil had become one of the global hotspots of the pandemic by June. While the city of São Paulo was the initial epicentre of the outbreak, the virus spread rapidly around the country. The health system soon faced serious shortages, especially in the public sector, on which two thirds of Brazilians depend. Many fatalities occurred among those waiting for admission into an intensive-care unit. Following a decline of as of end-July 2020, new cases and deaths have been rising again as of early November.

Growth turned negative in the first quarter of 2020, as local governments started to impose lockdown measures from mid-March to contain the spread of the virus and avoid even worse human hardship. Distancing measures have been in place in all of Brazil’s 27 federative units, land borders were closed and entry by air from many countries was restricted for months. Growth then plunged further in the second quarter and indicators of confidence, demand and activity fell sharply, but many of them have also shown a strong recovery since (Figure 1.7). GDP expanded again in the third quarter, returning to a level 4% below that of end-2019. For the year 2020, OECD projections expect GDP to decline by 5%, followed by a recovery in 2021 (Table 1.2). GDP will have recovered its pre-pandemic level by early 2022.
Job losses, lower hours worked and significantly reduced earning possibilities for self-employed workers are weighing strongly on private consumption. Unemployment, which never fully recovered from the 2015 recession, is now rising again. Its recent rise, however, reveals only a part of the actual employment losses as many survey respondents did not even pretend to look for a job during the pandemic, and were hence recorded as outside the labour force.

With inflation right at target before the COVID-19 shock started to weigh on demand, financial conditions had eased significantly. Rate cuts of 250 basis points until August 2020, combined with regulatory measures that would allow additional credit extension of up to 18.5% of GDP, will provide favourable conditions for private investment once confidence in the recovery strengthens and credit demand picks up. Fiscal policy, on the other hand, will have to unwind much of the appropriate emergency support even before demand firms, to ensure debt sustainability.

Exports declined in the third quarter of 2020 but are projected to benefit from recovering global demand as of 2021, especially from Brazil’s two major export destinations China and the United States (Figure 1.8). Manufacturing exports are limited by weak prospects in neighbouring Argentina, the major destination for

Source: Central Bank, CEIC, IBGE.

StatLink [https://doi.org/10.1787/888934196366](https://doi.org/10.1787/888934196366)
such exports. Import demand will pick up in line with domestic demand. A slightly widening but moderate current account deficit will continue to be covered by foreign direct investment inflows.

Table 1.2. Macroeconomic indicators and projections

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
<th>2021</th>
<th>2022</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Gross domestic product (GDP)</strong></td>
<td>1.7</td>
<td>1.4</td>
<td>-5.0</td>
<td>2.6</td>
<td>2.2</td>
</tr>
<tr>
<td>Private consumption</td>
<td>2.4</td>
<td>2.2</td>
<td>-6.2</td>
<td>2.7</td>
<td>2.2</td>
</tr>
<tr>
<td>Government consumption</td>
<td>0.8</td>
<td>-0.4</td>
<td>-4.8</td>
<td>0.5</td>
<td>0.0</td>
</tr>
<tr>
<td>Gross fixed capital formation</td>
<td>5.3</td>
<td>3.4</td>
<td>-5.1</td>
<td>4.4</td>
<td>5.6</td>
</tr>
<tr>
<td>Final domestic demand</td>
<td>2.5</td>
<td>1.9</td>
<td>-5.7</td>
<td>2.5</td>
<td>2.3</td>
</tr>
<tr>
<td>Stockbuilding¹</td>
<td>-0.5</td>
<td>0.0</td>
<td>-1.2</td>
<td>-0.4</td>
<td>0.0</td>
</tr>
<tr>
<td>Total domestic demand</td>
<td>2.1</td>
<td>1.9</td>
<td>-6.9</td>
<td>2.1</td>
<td>2.3</td>
</tr>
<tr>
<td>Exports of goods and services</td>
<td>3.3</td>
<td>-2.3</td>
<td>-2.0</td>
<td>-0.6</td>
<td>4.0</td>
</tr>
<tr>
<td>Imports of goods and services</td>
<td>7.0</td>
<td>1.1</td>
<td>-14.3</td>
<td>-4.4</td>
<td>4.6</td>
</tr>
<tr>
<td>Net exports¹</td>
<td>-0.4</td>
<td>-0.5</td>
<td>1.8</td>
<td>0.5</td>
<td>0.0</td>
</tr>
</tbody>
</table>

**Other indicator**

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
<th>2021</th>
<th>2022</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment rate (% of labour force)</td>
<td>12.3</td>
<td>11.9</td>
<td>13.6</td>
<td>16.0</td>
<td>15.0</td>
</tr>
<tr>
<td>Consumer price index (annual growth rate)</td>
<td>3.7</td>
<td>3.7</td>
<td>3.1</td>
<td>3.6</td>
<td>3.2</td>
</tr>
<tr>
<td>Consumer price index (year-over-year growth in December)</td>
<td>3.8</td>
<td>4.3</td>
<td>3.8</td>
<td>2.9</td>
<td>3.4</td>
</tr>
<tr>
<td>Core consumer price index (annual growth rate)</td>
<td>3.3</td>
<td>3.5</td>
<td>2.5</td>
<td>2.2</td>
<td>3.3</td>
</tr>
<tr>
<td>Current account balance (% of GDP)</td>
<td>-2.2</td>
<td>-2.7</td>
<td>-0.3</td>
<td>-0.5</td>
<td>-0.9</td>
</tr>
<tr>
<td>General government headline balance (% of GDP)</td>
<td>-7.0</td>
<td>-5.8</td>
<td>-15.6</td>
<td>-7.2</td>
<td>-6.3</td>
</tr>
<tr>
<td>General government primary balance (% of GDP)</td>
<td>-1.6</td>
<td>-0.9</td>
<td>-10.7</td>
<td>-2.8</td>
<td>-2.3</td>
</tr>
<tr>
<td>General government gross debt (% of GDP)</td>
<td>76.5</td>
<td>75.8</td>
<td>91.4</td>
<td>94.3</td>
<td>96.6</td>
</tr>
</tbody>
</table>

1. Contribution to changes in real GDP.
Source: OECD projections, OECD Economic Outlook Database, Central Bank.

Figure 1.8. Brazil’s main export markets and products

Source: UN Comtrade database.

StatLink 2 https://doi.org/10.1787/888934196385
Risks are centred around the implementation of reforms and fiscal sustainability

Current projections assume a continuation of progress in structural reforms to improve growth and fiscal performance. Fiscal sustainability hinges on keeping the pandemic-related fiscal measures temporary and on resuming the fiscal adjustment in train before the pandemic. A failure to reduce government spending obligations and budget rigidities would imply breaking the expenditure rule, one of the driving factors behind growing confidence and declining interest rates in the run-up to the pandemic. The situation has now been aggravated as the pandemic response has added some 15 percentage points of GDP to public debt. Without strong action, financing costs could rise substantially, jeopardising fiscal sustainability and depressing investment, and Brazil could experience a protracted recession like the “lost decade” of the 1980s.

The political economy of getting these reforms done is not trivial. A fragmented and polarised political landscape casts a shadow over the executive’s ability to build political consensus for key reforms, and implementation risks loom large. Some of the necessary reforms will question long-standing privileges. For example, producers in activities currently shielded from competition have incentives to defend their rents, while user benefits are dispersed. Moreover, some of the benefits from reform may not materialise immediately, unlike some of the costs. Resistance to change may cause setbacks, like the transport strike triggered by rising diesel prices that dented economic activity visibly in 2018. At the same time, if a consensus can be reached, reforms also portend a significant upside, given the significant potential to improve the business climate and the quality of public expenditure.

Social discontent has flared up in several South American neighbours and could also affect Brazil, possibly compounded by deteriorating social conditions as a result of the pandemic. Frustrated aspirations of a rising but still vulnerable middle class have been a common theme across the continent, one that also resonates in Brazil. The 2015/16 recession had already reverted progress with social mobility, deceiving those who thought they would be next in line to improve their lives. Brazil scored 27th out of 30 countries compared in a 2018 OECD comparison of social mobility (Figure 1.9). The resulting frustration was compounded by corruption scandals that have eroded faith in public institutions.

**Figure 1.9. Intergenerational mobility is low**

Expected number of generations it would take the offspring from a low-income family to reach the mean income

Note: These estimates are simulation-based and intended to be illustrative. They are based on earnings persistence (elasticities) between fathers and sons and the current level of household incomes of the bottom decile and the mean, assuming constant elasticities. Low-income family is defined as the first income decile, i.e. the bottom 10% of the population.

Source: OECD Income Distribution Database, (OECD, 2018)
**External vulnerabilities seem contained**

Economy-wide external debt has declined below 2018 levels and is lower than in most emerging market economies, relative to currency reserves (Figure 1.10). Corporate external debt of around 26% of GDP is exposed to exchange rate risks. To what extent these are hedged is hard to ascertain. For the public sector, external debt is not a vulnerability as only 4% of public debt is denominated in foreign currency.

Figure 1.10. External debt is stable and currency reserves are substantial

![Graph showing external debt and currency reserves](https://doi.org/10.1787/888934196423)

1. The external debt definition used here includes intercompany lending and domestic fixed income securities held by non-residents.

The economy has significant cushions against external financial risks. Currency reserves of 19.7% of GDP make the public sector a net creditor in foreign currency and a dollar swap line with the US Federal Reserve could provide additional dollar liquidity. The strong FDI component of capital inflows makes them less likely to reverse quickly, although Brazil experienced strong portfolio outflows in 2020 (Figure 1.11).

Figure 1.11. Foreign direct investment inflows exceed the current account deficit

![Graph showing current and financial accounts](https://doi.org/10.1787/888934196442)

1. Moving average, excluding reserves.

Source: BCB, CEIC.
The flexible exchange rate acts as a shock absorber and has served Brazil well. Bouts of exchange rate volatility have been managed well by the Central Bank using direct market interventions and swap contracts to smooth excess movements, but without impeding necessary adjustments. A recent depreciation is partly related to a flight for safety in the context of the pandemic, declining domestic interest rates and an expanding domestic capital market, which have led some corporate debtors to substitute external debt for domestic financing.

**Financial soundness indicators are solid but the pandemic entails unprecedented risks**

Brazil’s relatively small financial sector had a remarkably smooth ride through the deep 2015/16 recession and financial stability indicators were showing cyclical improvements in the run-up to the COVID-19 pandemic. Bank capitalisation has trended upward and significantly exceeds regulatory requirements, despite some recent declines in the context of easier capital regulations, aimed at encouraging banks to lend (Figure 1.12). Non-performing loans have also been on a declining trend, but could increase as an increasing number of businesses and households will struggle to service their debts. This will put significant strain on the banking system and it is conceivable that the effect of the COVID-19 shock exceeds what is simulated in standard stress test scenarios. The last IMF Financial Stability Assessment of 2018 suggests that banks are broadly resilient to macro-financial shocks (IMF, 2018[11]). Stress test carried out by the Central Bank also point to an ability to withstand substantial shocks to growth or risk premiums (BCB, 2019[12]). High margins point to scope for strengthening competition among financial institutions, as currently pursued by the Central Bank.

**Figure 1.12. Financial stability indicators have deteriorated at the margin during the pandemic**

Source: CEIC, BCB.

StatLink [https://doi.org/10.1787/888934196461](https://doi.org/10.1787/888934196461)
Household credit stands at 30% of GDP after surpassing corporate credit in late 2016. This is mid-range among emerging economies and less than half the OECD average (Figure 1.13). Debt service relative to household incomes has remained fairly stable at around 20%. Corporate bank loans have edged up since March, possibly reflecting the uptake of emergency lending programmes for firms. Overall corporate debt amounting to 57% of GDP is low in international comparison and includes debt securities and financing from abroad, to which large corporates have increasingly resorted over the last years (IMF, 2019[13]; BCB, 2020[14]). As corporate bond issuance picked up, domestic investment funds have shifted their portfolio towards corporate securities, without detriment to their liquidity level, which is close to record highs (BCB, 2019[12]).

Figure 1.13. Household and corporate debt levels remain moderate

1. Data in panel B and D refer to the 4th quarter of 2019.
2. Unweighted average of 32 OECD countries with available data.
Source: CEIC, BCB, BIS Total credit database.

StatLink 2 https://doi.org/10.1787/888934196480
Table 1.3. Events that could lead to major changes in the outlook

<table>
<thead>
<tr>
<th>Uncertainty</th>
<th>Possible outcome</th>
</tr>
</thead>
<tbody>
<tr>
<td>Failure to implement structural reforms</td>
<td>Without structural reforms, the recovery would be much more protracted as current projections are predicated on improvements in productivity and investment. Without reforms to mandatory spending rules, fiscal outcomes will deteriorate further, which could affect investment flows, raise interest rates, and potentially trigger a fiscal crisis.</td>
</tr>
<tr>
<td>A flight to safer assets in global capital markets</td>
<td>If capital flows to emerging markets were to dry up or decline substantially, Brazil could find it more difficult to tap into external financing sources. This could trigger higher interest rates and lower growth.</td>
</tr>
<tr>
<td>A resurgence of COVID-19 cases, triggering more stringent social distancing measures</td>
<td>New lockdowns would depress economic activity and could significantly delay the recovery. A potentially costly fiscal response would have negative implications for fiscal accounts.</td>
</tr>
<tr>
<td>Slower growth in China and the United States due to trade tensions</td>
<td>Rising trade tensions could lead to a slowdown of demand from Brazil’s main trading partners and lower commodity prices would reduce exports and growth. Commodity sectors account for 60% of Brazil’s exports, but only for 5% of GDP.</td>
</tr>
<tr>
<td>A more protracted or deteriorating recession in Argentina</td>
<td>Argentina is the main export destination for Brazil’s manufacturing exports which could decline further if Argentina’s economy fails to recover.</td>
</tr>
</tbody>
</table>

Inflation is below target and interest rates have reached a long-time low

Inflation has been on a declining trend since 2016 and the recession has pushed it further down. While headline inflation has risen since September driven by food prices, this increase is likely to be temporary and inflation remains close to the current inflation target of 4%, which is set to decline to 3.75% in 2021 and 3.5% in 2022 (Figure 1.14). Core inflation has remained lower at 2.6%. Markets expect inflation to remain around 3.5% in 2021 and 2022 (BCB, 2020[15]).

Figure 1.14. Inflation has come down

Below-target inflation has opened up space for significant monetary easing. The benchmark policy rate Selic has fallen by 425 basis points since mid-2019, including 250 basis points of rate cuts since the outbreak of the pandemic. Real interest rates have fallen to almost zero, down from over 9% in late 2016 (Figure 1.15). With plenty of idle capacity and no inflationary pressures in sight, maintaining the current accommodating monetary policy stance well into 2021 appears appropriate to support the recovery, especially in light of the limited fiscal space that will require a gradual withdrawal of fiscal support. This assumes, however, that fiscal policy sticks to current plans. Significant fiscal slippage would likely affect inflation expectations and call for less monetary accommodation.
The contained inflationary pressures and expectations of the last years are partly related to significant economic slack, but they also reflect a prudent and predictable conduct of monetary policy. In 2012-13, the Central Bank cut rates despite inflation being above target, but had soon to retreat as inflation rose (Figure 1.16). The resulting loss of credibility gave rise to several years of high inflation despite an economy in recession. The current situation attests to a significant improvement in the credibility of the Central Bank since then, which is a substantial achievement. The recent easing round only started with inflation declining firmly and expectations very close to the target. The effectiveness of monetary policy has also been enhanced by subjecting directed credit to market rates as of 2017. Together with improving fiscal prospects, this has reduced the neutral rate, defined as the interest rate that allows the economy to grow without causing excessive inflation and it is helping to transform financial markets towards more competition, less directed credit and lower lending spreads (see chapter 2). In the past, large directed credit volumes were decoupled from the policy rate.

Figure 1.15. Monetary authorities have responded by cutting rates

![Figure 1.15](https://doi.org/10.1787/888934196518)

1. TJLP until 12/2017, TLP as of 1/2018
Source: CEIC, BCB.

Figure 1.16. Monetary policy decisions have closely followed inflation dynamics

![Figure 1.16](https://doi.org/10.1787/888934196537)

Note: Inflation expectations are calculated as market expectations from the Central Bank’s FOCUS survey, 12-months ahead.
Source: BCB.
While the Central Bank has acted independently recently, the effectiveness of monetary policy could be improved by formalising this independence and shielding it from possible future political interference. Setting a fixed term for appointments of the central bank governor and members of the monetary policy committee, not coinciding with the presidential term and during which they cannot be dismissed, would be in line with current practice in most inflation-targeting countries (Hammond, 2012). A draft bill to strengthen the independence of the Central Bank has been approved by the Senate and is currently awaiting approval by the Chamber of Deputies. Furthermore, safeguarding the financial independence of the Central Bank, including through an adequate budget and adequate levels of capital, are key for maintaining strong credibility. Chile and Mexico have had formal Central Bank independence for over 20 years, which include long fixed-term appointments of board members. Costa Rica just strengthened the independence of the Central Bank, clarifying the governor’s appointment and dismissal conditions, and removing scope for political interference.

The fiscal outlook has become much more challenging after COVID-19

Improving fiscal outcomes remains one of Brazil’s principal challenges. COVID-19 is projected to drive up gross public debt by over 15 percentage points to 91.4% of GDP by the end of 2020, and by 20 percentage points to 96.6% of GDP by the end of 2022. This follows an earlier increase of over 25 percentage points of GDP between 2013 and 2019. Interest rates have come down due to improvements in Central Bank credibility and pre-pandemic improvements in fiscal prospects, but interest expenses of almost 5% of GDP are high in international comparison, and are similar to current spending on education.

OECD debt simulations suggest that gross public debt will peak at 101% of GDP in 2026, in a likely baseline scenario where current fiscal plans are implemented as announced and where structural reform plans currently discussed by Congress will eventually be approved (Figure 1.17). The primary fiscal deficit will rise to 10.7% of GDP in 2020 on the account of appropriate emergency spending and lower tax revenues. Fiscal consolidation plans in train before the pandemic are assumed to continue after that as in the draft budget, leading up to a balanced primary result by 2025 and a primary surplus of 2% of GDP by 2030. In the baseline scenario, growth will benefit from some gradual progress in reducing distortions from taxes and domestic regulations and a steady if slow reduction of barriers to trade and investment. This would support potential growth of around 2% per year and will allow a gradual decline of public debt relative to GDP in the second half of the decade, returning to 97% of GDP by 2030.

As Brazil is only at the beginning of its population ageing process, the fiscal costs of population ageing, which are included in the baseline projections, will not have much weight over the next decade. Following the approval of the pension reform, pension spending is projected to be 0.2 percentage points of GDP lower in 2030 than today. Public health expenditures are likely to rise, but only by around 0.15% of GDP by 2027 (Tesouro Nacional, 2019[16]), although this does not account for any implications of the ongoing pandemic. Long-term care expenses are currently not covered by the public sector. Future fiscal challenges related to ageing call for reducing public debt before they materialise.

The debt trajectory is highly sensitive to the implementation of the reform agenda. A more ambitious package of structural reforms whose growth effects are quantified in Table 1.1, would boost potential growth by up to one percentage point and lead to an earlier and more profound decline in public debt relative to GDP, to below 90% by 2030 (the green line in Figure 1.17). At the same time, debt sustainability could be jeopardised if all currently discussed reform projects remained inconclusive, so that productivity would continue to remain stagnant and growth outcomes would decline. Debt would hardly decline in this case, and remain at 107% of GDP (dotted blue line). A combination of less ambition in fiscal adjustment plans and higher financing costs could result in less favourable fiscal outcomes. Assuming that a primary surplus is not achieved before 2030 and then reach only 0.5% of GDP, instead of the 2% assumed in the
baseline, would have severe consequences for the trajectory of public debt, which would then rise without bound and exceed 111% of GDP by the end of the decade (red line).

Figure 1.17. Gross public debt is set to stabilise, but subject to risks

Note: In the baseline scenario, the primary fiscal result improves from -10.7% in 2020 to +2.0% of GDP by 2030, in line with projections by the Treasury and the OECD. After 2021 compliance with the expenditure rule is assumed. The exchange rate and the interest rate are assumed to remain constant after 2022. GDP growth is assumed as in table 1.1 and constant at 2% after 2022. The ambitious reform scenario assumes structural reforms that boost raise growth by around 1 percentage point as of 2022 (see table 1). The no further reforms scenario assumes that none of the currently discussed structural reform plans will be implemented and growth will be 1 percentage point lower. The slower fiscal adjustment scenario assumes a 1.5 percentage point higher fiscal deficit as of 2022.

Source: OECD calculations based on National Treasury, IBGE, Brazilian Central Bank and OECD projections.

With over 95% of gross public debt denominated in domestic currency, exchange rate risks are not a concern for public debt, but as a flip-side of this coin, maturities are relatively short. Shorter maturities imply greater potential rollover risks. Currently, 22% of gross public debt comes due within 12 months, reflecting an average maturity of around 3.9 years. Maturities have become slightly shorter since 2015, when the average maturity of public bonds stood at 4.6 years. The COVID-19 pandemic is expected to decrease the average debt maturity (Tesouro Nacional, 2020[17]).

Additional risks to debt sustainability stem from weak public finances of some of Brazil’s states for which the central government may have to step in. Many state finances suffer from high pension obligations and wage costs. Fiscal relations with the states have been plagued by moral hazard as the central government has repeatedly had to renegotiate debts with states, often rewarding low fiscal prudence due to the lack of effective enforcement mechanisms. A recent draft law submitted to congress aims limiting bailouts in exchange for higher transfers to states by 2026.

**Fiscal adjustment will have to resume after the pandemic**

With public spending of more than 42% of GDP before the pandemic, the size of Brazil’s public sector is closer to the 40% OECD average than to the 28% average of Latin American peers (Figure 1.18). Taxes are characterised by a strong reliance on goods and services taxes, while social benefits, interest payments, education and health are the largest spending items. Social benefits are the spending category that has recorded the strongest increase in recent years.
Figure 1.18. Public sector tax revenues and expenditures

Fiscal accounts deteriorated substantially after 2014, when the primary balance (excluding interest payments) turned negative after more than a decade of primary surpluses (Figure 1.19). This reflected mostly increases in expenditure, but also tax expenditures. Since then, the headline balance had shown improvements until the COVID-19 outbreak, mostly on the back of lower interest expenses and a retrenchment in public investment, which reduced the primary deficit to 0.9% of GDP in 2019.

Source: OECD Economic outlook database, except for Chile: IMF WEO; OECD Revenue Statistics; OECD calculations based on Balanço do setor público nacional (National Treasury).

StatLink  
https://doi.org/10.1787/888934196575
Stabilising public debt and bringing it on a downward trajectory will imply the need to generate a primary surplus of around 2% of GDP by the end of the decade, as assumed in the debt simulations above. Starting from the primary deficit in 2019, this would require a total fiscal adjustment of 2.9% of GDP, compared to 2019. There is also a strong case for public policies to boost investment into people by expanding spending on some well-targeted social benefits to reduce inequality and poverty and invest more into education and training, with a view towards enhancing both productive and inclusive growth. Doing so would reduce inequalities of opportunities and smooth the transition towards a more productive economy that structural reforms can bring about. Part of this, the expansion of the federal education fund FUNDEB, has already been decided. Assuming additional spending of around 1% of GDP on these items, the total fiscal adjustment would need to be around 4% of GDP.

This adjustment could be achieved without raising tax rates or introducing new taxes (Table 1.4). Instead, there is ample scope for raising spending efficiency without jeopardising social and economic objectives (Izquierdo, Pessino and Vuletin, 2018[18]). This could include ending current expenditures that are no longer priority or have proven ineffective, such as subsidies, and by better managing public payroll expenses. Tax
expenditures could also be reduced substantially as many of them create distortions without generating much benefit (World Bank, 2018[19]). Finally, better spending efficiency also hinges on reducing the waste of public resources due to corruption and on avoiding spending on less effective projects for the sake of building political consensus.

Table 1.4. Fiscal impact of recommendations

<table>
<thead>
<tr>
<th>Fiscal recommendation</th>
<th>Estimated impact on fiscal balance, % of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reduce public payroll expenses</td>
<td>+2%</td>
</tr>
<tr>
<td>Reduce subsidies and tax exemptions</td>
<td>+2% (or more)</td>
</tr>
<tr>
<td>Raise spending on Bolsa Família programme</td>
<td>-0.5%</td>
</tr>
<tr>
<td>Raise spending on professional training</td>
<td>-0.3%</td>
</tr>
<tr>
<td>Raise spending on basic education through a higher FUNDEB budget (already decided)</td>
<td>-0.3%</td>
</tr>
<tr>
<td>Resulting change in primary balance</td>
<td>+2.9%</td>
</tr>
</tbody>
</table>

Note: Numbers in this table are estimates and some are subject to uncertainty. Implementation would take several years.

Reducing budget rigidities is key

Over the years, spending patterns on current expenditures have been shaped by automatic rules like widespread revenue earmarking, mandatory spending floors or indexation mechanisms. By now, 93% of spending is mandated by law or the constitution. This has shifted much of spending away from where it is most needed and leaves few resources at the discretion of the centre of government to pursue priority policy objectives. Considerable efforts have been made to improve fiscal outcomes through cuts in discretionary spending not subject to congressional approval, particularly public investment, underpinning a tepid recovery of fiscal outcomes since 2018. But the scope for further reductions in discretionary spending has now been largely exhausted.

Changes in mandatory spending items and indexation rules have become inevitable to deliver the needed fiscal adjustment and to ensure compliance with fiscal rules in the short term. An expenditure ceiling adopted in 2016 is becoming the most binding of Brazil’s various fiscal rules and limits the growth of almost all primary central government expenditures to inflation. Despite in-built enforcement mechanisms, it has so far not generated the expected political momentum for reform to ensure compliance with the rule in the short term. The rule is now at risk of being broken in 2021, which could affect confidence and result in higher financing costs.

Rigidities also affect state and municipality budgets, where specific fractions of revenues and transfers must be spent on education and health. These mechanisms fail to take into account different age profiles across municipalities. Recent proposals to move towards a joint definition of spending floors for health and education would be a step in the right direction, although revenue earmarking should be reconsidered altogether. Often enough, raising spending efficiency in these areas would be at least as important as preserving specific spending amounts. Estimates suggest potential spending efficiency gains of 1.5% of GDP in education and 2.5% in health, without detriment to outcomes (Flamini and Soto, 2019[20]).

Improving the effectiveness of social transfers

Social transfers are a prime example of how automatic rules have reduced spending efficiency and outcomes. Brazil spends over 15% of GDP on social transfers, of which around 13% of GDP on contributory and non-contributory old-age pensions with almost universal coverage of the elderly. This has strongly reduced old-age poverty, but almost half of total social benefits is paid to recipients in the highest income quintile, mostly in the form of pensions (Figure 1.20). Rising benefit levels have been driving pension spending for years, explaining much of the rise of public expenditures.
A pension reform approved in 2019 will raise effective retirement ages and make pensions more progressive (Box 1.3). The pension reform was key for fiscal sustainability as pension spending would have otherwise doubled by 2060 (OECD, 2018[21]; OECD, 2017[22]). Over the next decade, pension spending would have been 10 percentage points of GDP higher without the reform. But while the reform contained pension expenses, these are not projected to fall below current levels before 2025 (IFI, 2019[23]). By 2030, pension spending will be around 0.2% of GDP lower than today and demographic change may require further adjustments in the future. A first step would be to align pension rules among state and municipal employees and military staff with current general provisions. This would also help contain the fiscal risk from subnational governments.

A key priority for the future would be to change the current indexation mechanisms for social security benefits. Pensions and other social security benefits, including non-contributory and survivor pensions, are an important achievement, but they have risen rapidly. The minimum wage constitutes a floor for any individual monthly social security benefit paid, and it has seen real increases of 74% over the last 15 years, while real per-capita-incomes have risen by 18%. This has had strong effects on the fiscal result, and has ultimately proven unsustainable. More than 55% of Brazilians have incomes below the minimum wage, implying that all social security beneficiaries have incomes higher than the median population income (Figure 1.21).
Figure 1.21. Benefits tied to the minimum wage reach only those above median income

By contrast, no automatic adjustment is applied to conditional cash transfers under the Bolsa Família programme, which targets households with monthly per capita incomes below BRL 178 per month and with children enrolled in regular school programmes. These transfers have a strong impact on poverty and inequality, but they have declined by 22% in real terms over the last 15 years. Raising benefits and eligibility thresholds has great potential for reducing poverty further, while ensuring that all those eligible are enrolled with reasonable delays. Brazil only spends 0.5% of GDP on Bolsa Família, which has reduced poverty by 15% (Ferreira de Souza et al., 2019[24]). More than 70% of money spent on conditional cash transfers spending ends up in the hands of the poorest 40% of the population, in contrast to other social transfers (SEAE, 2017[25]). Bolsa Família recipients are mostly families with children and youths, which is where poverty is concentrated (Figure 1.22).

The contrasting indexation mechanisms have implied that the increases in overall social spending that occurred in the past decade have mostly benefited households that are not poor. Simultaneously, these mechanisms have exacerbated the social spending bias to the detriment of children and youths. Preserving the real purchasing power of social security benefits by adjusting them in line with prices could free up resources to raise spending on Bolsa Família, the only transfer where incremental spending would really reach the 52 million of Brazilians with incomes below the World Bank’s USD 5.50 per day definition. A package of reforms that would sever the link between minimum benefit levels and the federal minimum wage while shifting most of the savings to Bolsa Família could have accelerated the declines in the Gini coefficient, a common measure of income inequality, that Brazil experienced in the past. For example, in 2012 when the real value of the minimum wage rose by almost 8%, such a reform package would have allowed Brazil to double the decline in the Gini coefficient of that year (Arnold and Bueno, 2020).
Figures 1.22. Poverty rates are relatively high for young people

Managing high payroll expenses

Scope for savings also exists in staff costs, which at 13% of GDP are high in international comparison (Figure 1.23). While public employment is not higher than in many OECD countries, wage premiums of federal employees have been estimated at 96% to 60% of comparable private sector earnings and are particularly pronounced for high skill levels (Nemer Tenoury and Menezes-Filho, 2017[26]; World Bank, 2019[27]). In part, this reflects rapid growth of civil servant salaries in recent years. Estimates suggest that 0.5% of GDP could have been saved over the past six years if public salaries had not outgrown private sector pay (IFI, 2019[28]). Looking ahead, remuneration could be indexed to inflation for all three branches of the government, instead of today’s discretionary rises. Municipal government employees, which include most teachers, enjoy no wage premium relative to private sector pay.

Upcoming retirements of 39% of civil servants within 10 years present an opportunity to reduce staff spending (World Bank, 2018[19]). This strengthens the case for lowering entry-level salaries, which are much above private sector pay. Freezing staff increases will also help as currently, the ratio of new hires to retirees is at 1.3 (World Bank, 2019[27]).

Unifying the multiplicity of different career paths and strengthening links between performance and pay would allow better adaptation to changing needs and policy priorities, as many civil servants enjoy rapid and automatic career promotions to the top salary scale. Finally, specific privileges could be reviewed, such as the 70 days of annual leave common in the judiciary branch and a generous system of allowances on top of high salaries. Savings from these options have been estimated between 0.4% and 3% of GDP (World Bank, 2019[27]). A reduction of 2% of GDP, which would bring payroll spending close to the average of Portugal and Canada, does not seem out of reach.
Figure 1.23. Public payroll expenses are high in international comparison

A. Compensation of General government employees, in % of GDP, 2018

B. Public sector wage premiums, 2018 or latest available year
(compared to private sector employees)

Source: Government Finance Statistics, IMF, World Bank Bureaucracy Lab, IBGE.

**Reducing inefficient subsidies and tax expenditures**

Subsidies and tax expenditures have risen, especially since 2010 and now amount to 4.8% of GDP (Figure 1.24). Significant progress has been made in containing financial subsidies used for directed credit operations. These have now declined from 1.8% of GDP in 2015 to 0.6% in 2019 (SECAP, 2020[9]). Beyond this, other tax expenditures like the SME tax regime, the Manaus Free Zone or income tax exemptions for private health and education services could be reconsidered. Lost tax revenues have a particularly high incidence on the poorer north-eastern and northern states. On the whole, a reduction of subsidies and tax expenditures on the order of 2% of GDP appears feasible.
Subsidies and tax expenditures have risen

Spending or lost revenues due to subsidies and tax expenditures


Combining regional and industrial policy objectives, the Manaus Free Zone located in the state of Amazonas, far from major consumer markets, has benefited from numerous tax benefits since the 1960s, with a current joint fiscal cost exceeding 0.3% of GDP. Nonetheless, few evaluations and cost-benefit analyses have been undertaken. While employment and industrial activity have risen in the Free Zone, the corresponding fiscal costs are around eight times higher than the total wage bill (World Bank, 2018[19]). Recent empirical work has failed to find significant external effects on human development indicators in the region beyond the Free Zone itself, including on the well-being of women (Cavalcanti Teixeira, 2019[30]).

At a cost of 1.1% of GDP, the targeted tax regime for small and medium enterprises Simples Nacional combines a lighter tax burden with a simplified calculation of tax liabilities based on turnover. This discourages firms to grow beyond the threshold and discourages sourcing intermediate inputs from potentially more efficient external providers. For very small firms, the easier compliance may outweigh these considerations. However, with a high participation ceiling of approximately USD 1 million in turnover per year, the regime is currently used by 74% of Brazilian firms and could be much better targeted, including by reducing the participation threshold.

Filing as a corporate entity under Simples Nacional has also become a preferred choice for high-income professionals, as this can reduce the effective tax burden from almost 50% to as little as 11.5% for those with few deductible expenses (Appy, 2017[31]). One way to reduce these inequities in the short run would be to eliminate the exemption from personal income taxes for distributed profits of companies filing under simplified tax regimes. In the longer run, there may be no strong arguments for maintaining Simples Nacional in the context of a broader tax reform that would simplify the general tax system (see Chapter 2). In that context, Brazil may be sufficiently served with the smaller Microempreendedor Individual programme, with a ceiling of USD 16 000 in turnover. At significantly lower fiscal cost, this programme has contributed to lower informality among low-income entrepreneurs, especially women (OECD, 2012[32]).

The current income tax deductibility of expenditures for private health and education expenses has regressive distributional effects, as 90% of Brazilians have incomes below the threshold where they would
pay income taxes and only 25% of Brazilians are subscribed to private health plans, while most of the population relies on the public health system. Phasing out these deductions could save 0.3% of GDP.

An exemption of “basic goods” from key consumption taxes lacks targeting, as many exempt items are consumed by middle class and high-income families. Part of this 0.3% of GDP could still be spent in a more targeted way, through a targeted tax rebate available only to low-income families registered in the *Bolsa Familia* programme.

**Reforming taxes to boost productivity and enhance fairness**

Brazil stands out for one of the highest tax compliance costs, as discussed in Chapter 2. This wastes resources and hurts the competitiveness of Brazilian companies. A fragmented indirect tax system in which 27 states plus the federal government apply their own tax codes lies at the core of these high compliance costs. Companies wishing to serve the domestic market have to comply with all of these codes. Tax credits for inputs are only granted if the input becomes physical part of the final product, giving rise to legal uncertainty and excessive litigation. A tax reform would have substantial potential for reducing costs and boosting productivity. One avenue would be to consolidate consumption taxes at different levels of government into one value-added tax with simple rules, a broad base, full refund for input VAT paid and zero-rating for exports. A revenue-neutral reform proposal, including temporary compensation schemes for states facing revenue shortfalls, would probably enhance the political viability of this urgent reform agenda, which has been discussed for decades. As a first step, a draft bill to unify two federal consumption taxes and enhance the deductibility of taxes paid on inputs has been submitted to Congress.

**Table 1.5. Past OECD recommendations on macroeconomic policies**

<table>
<thead>
<tr>
<th>Recommendations</th>
<th>Actions taken since the 2018 Economic Survey</th>
</tr>
</thead>
<tbody>
<tr>
<td>Implement the planned fiscal adjustment through permanent spending cuts.</td>
<td>A pension reform will contain future pension spending.</td>
</tr>
<tr>
<td>Gradually raise the retirement age.</td>
<td>Raised to 65/62 for most men/women.</td>
</tr>
<tr>
<td>Index pensions to consumer prices rather than the minimum wage.</td>
<td>No progress made. But minimum wage adjustments followed inflation in 2019.</td>
</tr>
<tr>
<td>Shift more resources towards transfers that reach the poor, including <em>Bolsa Familia</em>.</td>
<td>A 13th benefit payment has been introduced, but monthly benefits or thresholds remained unchanged.</td>
</tr>
<tr>
<td>Consolidate consumption taxes at the state and federal levels into one value added tax with a broad base, full refunds for input VAT paid and zero-rating for exports.</td>
<td>No progress made, but tax reform proposals are now being discussed in Congress.</td>
</tr>
<tr>
<td>Limit dismissal of the Central Bank governor to severe misconduct to rule out political influence in monetary policy decisions in the future. Safeguard the budget autonomy of the Central Bank.</td>
<td>A draft law on Central Bank reform has been submitted to Congress, but has not been voted on.</td>
</tr>
</tbody>
</table>

**Further social progress is possible at reasonable fiscal cost**

During the first decade of the millennium, inequality and poverty declined, while improvements in access to education and in social transfers reinforced well-being. 33 million Brazilians have escaped poverty since 2003, which is a remarkable achievement. Brazil’s social progress resulted from a combination of economic growth, a buoyant labour market, better access to education and social transfers (see Chapter 2 of OECD Economic Survey 2013). In recent years, income inequalities and poverty have been rising again on account of the 2015/16 recession (Figure 1.25). Resuming the social progress of the past is clearly feasible, but will hinge on refinements and more effective spending in social protection, education and professional training. Besides these specific policy levers, raising productivity, for which structural reforms play a key role, holds the key to sustainable improvements in economic prospects through new and better jobs. The end of Brazil’s record-high interest rates will also tend to reduce income inequalities by reducing investment returns of the wealthy, with a potential to reduce high wealth inequality.
Figure 1.25. Income inequality and poverty have started to rise again after a long decline

Note: The GINI coefficient for 2010 is an interpolation.

StatLink 2 https://doi.org/10.1787/888934196708

**Strengthening the social safety net**

Despite all its sophistication, cost and complexity, the social transfer system fails to provide an effective universal and accessible social safety net. Two parallel unemployment insurance schemes serve essentially the same purpose and cost around 1% of GDP, but their limitation to formal sector workers excludes those most in need of protection. Labour informality has recently risen to above 40% (Figure 1.26).

Figure 1.26. Labour informality is high and the labour tax wedge is almost at the OECD average

Source: Ilostat on informality, Brazil SIS IBGE, OECD calculations based on the ENOE for Mexico and the HLFS for Turkey; OECD Taxing Wages 2018.

StatLink 2 https://doi.org/10.1787/888934196727
One scheme called Seguro Desemprego pays up to two minimum wages for a period of 3-5 months. A second scheme called FGTS (Fundo de Garantia do Tempo de Serviço) is based on individual unemployment accounts that are paid out upon dismissal, with top-ups from the employer and the federal government. While individual-account schemes work well in some OECD countries, years of remuneration below market rates have created a deep-rooted distrust in forced savings mechanisms in Brazil, and a culture of cashing out individual balances as soon as possible, for which workers often induce their own dismissal (OECD, 2014[33]). This drives up job turnover and curbs incentives for firms to provide on-the-job training (Figure 1.27). Recent changes to FGTS have allowed workers to opt into a new variant where they can withdraw a certain fraction every year instead of being able to access the whole balance upon dismissal. While this could reduce job turnover, it defies the underlying objective of providing protection against income losses in the case of dismissal. The two schemes could be merged to save resources and reduce contributions and could serve as an individual top-up mechanism for a household-based universal social safety net in which benefits are not conditioned on formal employment.

Figure 1.27. Job turnover rates are high across most sectors

The fundamental task of protecting people against unexpected income losses from dismissals could be transferred to a universal means-tested social safety net, accessible to all Brazilians including informal workers. The successful Bolsa Familia programme is well-placed to fulfil this role with a few refinements and an increase in benefit levels, which would also be an effective tool to reduce poverty. Means-tested social safety nets aim at providing basic support regardless of employment history or work patterns (OECD, 2019[34]). Financed by general revenues, they allow reducing non-wage labour costs of formal jobs, which would foster formalisation (Levy, 2008[35]; World Bank, 2019[36]). They would also help to align non-wage labour costs across employment forms, including different contractual arrangements such as gig-workers (OECD, 2019[34]). Possible disadvantages of such schemes include the possibility of non-take-up (Bargain, Immervoll and Viitalmäki, 2012[37]), although low take-up of social benefits has so far not been a major issue in Brazil. For those with incomes well-above the poverty line, the relatively low benefits will be an incomplete insurance against the risk of job loss (OECD, 2019[34]), but complementing them with a merged and leaner contribution-based unemployment benefit scheme could address this issue.
A key challenge for this transition will be to make Bolsa Família more responsive to changes in beneficiaries’ personal situation by speeding up processing of benefit claims. Currently, these can take months or more, but dismissed workers need immediate income support. Workers would also find it easier to seize employment opportunities if they know that the benefit will resume rapidly should they become unemployed again. A gradual rather than sudden phase-out of Bolsa Família benefits for those who find a formal job would further strengthen job search incentives.

Making the programme more agile and effective would imply more frequent visits to beneficiary households by local social workers. Disbursements of Bolsa Família benefits could also be integrated with other social benefits in one single account to improve monitoring and avoid overlaps (Soares, Bartholo and Guerreiro Osorio, 2019[38]).

In light of the incipient structural transformation of the economy and the resulting movements of jobs across industries and firms, social protection will become of rising importance. In this context, Bolsa Família is a key asset on which Brazil should build to protect the poor more effectively and foster the political viability of reforms. There is also scope for combining income support with better activation policies through better training and job search assistance (see Chapter 3).

Brazil’s high inequality means that for the country as a whole, the cost of making a significant impact on the material wellbeing of the poor would be relatively manageable. Lifting all current poor, defined as those below the World Bank’s USD 5.50 per day poverty line, above that line could cost as little as 0.15% of GDP per year (IBGE, 2019[39]). Eradicating poverty would have significant payoffs. The attached conditionalities of Bolsa Família regarding school attendance and medical check-ups also help to reduce inequalities with respect to education and health, which further strengthens future economic opportunities for those living in poverty.

**Improving labour market policies**

Tackling labour informality remains a key challenge. Labour tax wedges for formal sector workers are high in international comparison and consist principally of social security contributions with no in-built progressivity and an 8% employer contribution to the FGTS (OECD, 2019[40]). Reducing tax wedges for low-skilled workers at risk of informal employment would strengthen formalisation incentives. A recent reduction of social contributions for young people in their first job can help them access formal jobs, but its impact should be carefully monitored and evaluated. If the measure turns out successful, expanding this lower rate to all low-income earners regardless of age would strengthen incentives for formal job creation and add more progressivity into the financing of social security. This could be financed through savings from reforming overlapping unemployment insurance schemes.

Although it is too early for empirical evidence, a 2017 labour market reform may have supported formal job creation as restrictive regulations on formal labour markets have been identified as one factor behind informality (Carvalho Filho and Estevão, 2012[41]). The reform has also reduced legal uncertainty for employers by reducing labour litigation. Further improvements in the ease of registering a business may also improve incentives for firms and their workers to become formal (see Chapter 2). Finally, enforcement efforts also play an important role, but require adequate funding. Recent plans to reduce the labour inspection budget should be reconsidered (Congresso Nacional, 2019[42]).

A highly effective way to raise labour market inclusion would be to foster female labour force participation, which is 20 percentage points lower than for men (ILO, 2020[43]). Women in Brazil perform 71% of unpaid domestic and caretaking activities during the week (ILO, 2020[43]). Their professional development may greatly benefit from expanding access to early childhood education. Access to pre-school has improved as available places doubled in recent years, but most of these improvements have been in high-income neighbourhoods. Prioritising low-income women and single mothers would allow more women to
participate in the labour market. Only 15% of poor families with children below three years have access to child-care, compared to 40% of the more affluent families (World Bank, 2016[44]).

*Raising the quality of education*

Improving access to quality education for all probably is the most effective and sustainable way to foster social and economic inclusion. While access to education has improved in recent decades, the quality of education is highly unequal across schools and regions. Brazil is one of the countries with the highest correlations between socio-economic status and learning outcomes, which is particularly worrisome as this perpetuates existing inequalities (OECD, 2019[45]). Two thirds of children of parents without basic education do not finish basic education themselves. Improvements in the quality of public basic education, including pre-primary, primary and secondary levels, should be a priority for reducing these inequalities of opportunities.

Overall education spending of 6.2% of GDP is above the OECD average (Figure 1.28). Still, Latin American countries such as Colombia, Mexico and Uruguay spend a lower fraction of GDP and perform better in the OECD PISA tests (OECD, 2019[46]). This suggests that spending better is the key priority, both across different areas of education and within. International evidence suggests that public spending in the early years of a child’s life often has higher returns in terms of productivity and equity, particularly pre-primary and primary education (Heckman and Masterov, 2007[47]; UNICEF, 2019[48]). Brazil’s relatively high spending on free public tertiary education, by contrast, tends to benefit students from high-income families as graduates of private secondary schools tend to score better on admission exams.

Municipalities bear the main responsibility for delivering basic education but have widely differing capacities, tax revenues and student numbers. A national system of funds called FUNDEB was established in 2007 to reduce inequalities in education funding across municipalities and states. States contribute fixed fractions of revenues from most education-earmarked state taxes to their own state-specific funds. The federal government has then topped off those state funds with low per-student funding until its total contribution of 10% of state funds (around 0.2% of GDP) was exhausted. The funds are then distributed to municipal school networks according to student enrolment. This relatively small top-up has aligned municipalities’ incentives with expanding enrolment and access to education. Access to education has improved substantially since. FUNDEB currently reduces 76% of spending inequalities across municipal school networks, but not all. Comparing the extremes, per-student spending differences across states would be 10000% without FUNDEB and are currently reduced to 564%, which is still substantial.

In August 2020, Congress approved a constitutional amendment to increase this federal top-up from 10% to 23% of state funds and make FUNDEB permanent. Moreover, a part of the federal top-ups has been linked to learning outcomes in Brazil’s universal standardised tests, which is likely to create incentives for spending better, potentially replicating the success achieved in terms of access. Currently, 80% of the inequalities of opportunities facing students result from differences in spending efficiency and governance and comparisons across states reveal no systematic relationship between per student spending and learning outcomes (Todos Pela Educação, 2019[49]). For example, education spending efficiency in the state of Ceará is exceptionally high due to its unique tying of 25% of school funding to improvements in student learning outcomes, which creates incentives for mayors to spend effectively (Boeke-Giuffrida, 2019[49]). Just how important the right governance incentives are is highlighted by the fact that 70% of Brazilian municipalities use only political appointments as the criterion for selecting school principals.

A more systematic effort is needed to distil lessons from local and (INEP, 2018[50]) international experience for school performance (OECD, 2017[51]). Under Chile’s “Se puede” programme, for example, government officials visit high-performance schools, seeking to apply lessons learnt on a broader scale. Looking ahead, the federal government could also include technical assistance for improving spending efficiency in its support to municipalities, or reward inclusion of students from vulnerable families, such as those who receive Bolsa Familia benefits. This would recognise that these students may require more efforts and
would improve incentives for schools to reduce drop-out rates, which are particularly high among disfavoured students. Finally, Brazil should consider raising teacher remuneration as initial salaries are only 60% of those paid in Chile, for example. This could take the form of temporary bonuses to qualified teachers who accept to teach in difficult schools.

**Figure 1.28. Spending on education is relatively high, but outcomes are poor**

Public education spending in % of GDP, 2017

Many students in Brazil repeat grades and finally drop out of secondary education. Grade repetition has high costs and its benefits are highly disputed (Ikeda and García, 2014[52]). Focusing on early and targeted support to those students with a higher risk of leaving the education system would be more efficient and produce better outcomes, as drop-outs often lack basic cognitive and social skills that are acquired during early childhood (OECD, 2016[53]). As drop-out rates are 8 times higher in the lowest income quintile than in the highest, this suggests a stronger focus on expanding access to early childhood education for children from low-income families. Brazil has reached near universal enrolment of 5 and 6 years old but lags behind in the participation of younger children (OECD, 2019[54]).

Providing more professional training content to those without academic ambitions may also be a way to reduce drop-out rates in secondary education and improve job market opportunities. But training needs also include those that have already left school, especially in the context of upcoming structural changes.
in Brazil’s economy, which calls for improving vocational and professional training. These issues are discussed in chapter 3 of this survey.

Table 1.6. Past OECD recommendations on social and labour market policies and education

<table>
<thead>
<tr>
<th>Recommendations</th>
<th>Actions taken since the 2018 Economic Survey</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bolster training and job search assistance programmes for workers affected by job reallocations across firms and sectors.</td>
<td>The budget of the former professional training programme PRONATEC is being reduced, while new training programmes are being designed, with an aim at better responding to labour market need. See Chapter 3.</td>
</tr>
</tbody>
</table>

**Fighting corruption and economic crimes**

Raising the efficiency of public spending will not be possible without further improvements in the fight against corruption and economic crimes. Corrupt practices and kick-backs such as those revealed in recent years waste public resources, increase the perception of political and litigation risk, deteriorate the investment climate of a country and exacerbate income inequalities by allowing relatively prosperous public officials and business people to divert taxpayer resources. Renewed allegations against powerful politicians, albeit not comparable to corruption revelations of the past, may have deceived those who hoped for imminent improvements in this area.

Comparative indicators of corruption perceptions point to significant challenges in economic governance (Figure 1.29). Beyond perceptions, systematic evidence with respect to high-level corruption is scarce. While not without controversy in some cases, Brazil has uncovered one of the largest corruption schemes under the umbrella of the operation “Lava Jato” (“Car wash”), involving billions of dollars and politicians and companies from several countries. Economic crimes have surfaced in the context of public procurement, including by state-owned companies, credit subsidies or tax expenditures to the benefit of specific companies and sectors. Infrastructure concessions are also vulnerable to collusion among bidders and corruption. Estimates suggest that corporate campaign donations by companies, banned since 2016, have significantly increased the probability of being awarded public contracts in the past (Boas, Hidalgo and Richardson, 2015[55]).

Enforcing laws is a necessary element to prevent impunity and ensure the credibility and legitimacy of institutions. Progress in Brazil’s legal and institutional enforcement framework has been instrumental for recent success. This includes key anti-corruption laws and tools, such as leniency agreements and cooperation agreements (OECD, 2019[66]), in combination with the strengthening of enforcement bodies such as the federal police, the financial intelligence unit, the public prosecutor, the competition watchdog and tax authorities. Strengthening the autonomy of these bodies and insulating them against political interference will be key for building on past progress. Recently, the de-facto autonomy of all of these bodies has been called into question by alleged political interferences in the selection process for key vacancies. Avoiding political interference in the future through clearer rules-based selection processes and formalising the operational and budget autonomy of these bodies will be crucial to avoid setbacks in the fight against corruption. A recent decision to move the Financial Intelligence Unit under the helm of the Central Bank further strengthens the case for formal Central Bank independence.

A well-functioning justice system is fundamental for business activity and productivity. Institutions that ensure property rights and their enforcement are the basis for market-transactions and one of the main determinants of economic development (Acemoglu, Johnson and Robinson, 2005[57]). In Brazil, the effectiveness of the judiciary in its crucial role to enforce the law and support the business climate is hampered by an extensive array of appeal possibilities that creates court congestion. In particular, a broad mandate of the Supreme Court implies that a high share of cases arrives at the Supreme Court. Defendants in all areas of law use these extensive appeal possibilities to postpone sentence execution. In penal cases,
this practice has allowed Brazil’s wealthy criminal convicts with access to sophisticated legal support to exploit court congestion and procedural mistakes to escape imprisonment for decades. This contributed to a widespread culture of impunity among powerful elites, which was fundamentally challenged in 2016 when the Supreme Court ruled that sentences could be executed once a trial went into the second instance of appeal. Most defendants of the *Lava Jato* operation have not yet fully exhausted their appeal possibilities but have been imprisoned after losing a first appeal, bringing the delay between sentence and its execution more in line with international practice. A recent Supreme Court ruling has challenged the constitutionality of this practice, thus requiring a constitutional amendment to uphold the possibility of sentence execution as of the second instance of appeal. Passing this amendment would be one possibly quick way to avoid set-backs in the prosecution of corruption and other criminal cases, and enhance judicial efficiency more broadly. Alternatively, reviewing appeal procedures, including narrowing the mandate of the Supreme Court, would be another potential avenue, although it may take longer to implement.

**Figure 1.29. Corruption indicators in international comparison**

<table>
<thead>
<tr>
<th>A. Corruption Perceptions Index</th>
<th>B. Control of corruption</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scale: 0 (worst) to 100 (best), 2019</td>
<td>Scale: -2.5 (worst) to 2.5 (best), 2019</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>C. Evolution of “Control of Corruption”</th>
<th>D. Corruption by sector, “Control of Corruption”</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scale: -2.5 (higher) to 2.5 (lower corruption), 2019</td>
<td>Scale: 0 (worst) to 1 (best), 2019</td>
</tr>
</tbody>
</table>

Note: Panel B shows the point estimate and the margin of error. Panel D shows sector-based subcomponents of the “Control of Corruption” indicator by the Varieties of Democracy Project.

Source: Panel A: Transparency International; Panels B & C: World Bank, Worldwide Governance Indicators; Panel D: Varieties of Democracy Institute; University of Gothenburg; and University of Notre Dame.

Full disclosure of information on the ultimate beneficiary behind private companies to relevant authorities and private sector bodies is important to prevent asset hiding. Tax authorities and financial institutions have collected such information since 2003, but measures to facilitate data sharing, including a single public registry, would support anti-money-laundering efforts (Berkhout, 2019[58]). Confiscating ill-obtained assets would also be made easier by criminalising illicit enrichment, which is currently only an offence but not a crime (Berkhout, 2019[58]).
Protecting whistle-blowers and officials involved in anti-corruption investigations against the criminalisation of and retaliation for their activities is crucial. First, despite some recent progress in 2018 and 2019 that strengthened transmission channels and protections for whistle-blowers, whistle-blowing procedures often continue to be hampered by concurrent competences and parallel systems for similar offences, which make it difficult to protect whistle-blowers effectively. Most OECD countries have dedicated whistle blower protection laws, like the one implemented by Australia in 2019, while Brazil does not (OECD, 2016[59]). Whistleblowing procedures have recently been strengthened but coordination among different agencies could be further improved. Second, a new law on the abuse of authority is unnecessarily vague (OECD, 2019[56]), leaving room for retaliation from powerful suspects by allowing prosecution of officials if they prosecuted a case “without just cause”. More precise rules are needed to protect public officials working on potentially highly political anti-corruption cases and avoid setbacks due to intimidation of officials.

Public procurement is usually one of the government activity most at risk to waste, mismanagement, collusion and corruption (OECD, 2016[60]). Efforts to combat corruption should include a thorough assessment of how public procurement laws could be improved further, in particular how their many complexities and exemptions affect integrity and competition in the tendering process. Brazil is currently conducting such a review with the support of the OECD. Rules pertaining to conflicts of interests, incompatibilities and impartiality in public procurement could be streamlined and strengthened. Building on recent progress with unified electronic procurement platforms can also enhance transparency and reduce the scope for economic crimes.

Constructing political consensus often builds on the widespread practice of budget amendments for parliamentarians, which these can use for projects in their constituency. The 2018 OECD Economic Survey called for reducing them and enhancing their transparency. Audits of the expenditures are still not systematic and empirical evidence suggests links between these amendments and corruption (Sodré and Alves, 2010[61]). These budgets are essentially used for coalition building (World Bank, 2018[62]). For example, in the run-up to the parliamentary vote on the presidential impeachment in May 2016, on lifting the president’s immunity in July 2017 or on the pension reform in 2019, these budgets rose visibly (Figure 1.30). This practice creates room for effectively audit-free spending, enhances the dependency of local authorities on members of congress, strengthens political patronage and reduces spending efficiency.

Figure 1.30. Budget amendments for parliamentarians have peaked around key voting dates


StatLink https://doi.org/10.1787/888934196803
Table 1.7. Past OECD recommendations on fighting corruption

<table>
<thead>
<tr>
<th>Recommendations</th>
<th>Actions taken since the 2018 Economic Survey</th>
</tr>
</thead>
<tbody>
<tr>
<td>Limit political appointments, especially in state-owned enterprises. Strengthen performance incentives in public companies.</td>
<td>Stricter selection requirements for management positions in state-owned enterprises have limited the scope for political appointments.</td>
</tr>
<tr>
<td>Undertake more systematic audits of all expenditures, including parliamentary budget appropriations.</td>
<td>Audits are being undertaken following a risk-based approach. More resources for the internal auditing body would allow more auditing. In practice, only a very small fraction of parliamentary budget appropriations is subject to audits.</td>
</tr>
<tr>
<td>Review public procurement laws. Use more centralised purchasing bodies.</td>
<td>Procedures for electronic auctions in the acquisition of goods and contracting of common services have been improved in 2019 and 2020. Brazil is currently conducting a procurement review with the support of the OECD.</td>
</tr>
<tr>
<td>Strengthen whistle-blower and leniency procedures.</td>
<td>Whistle-blower protection was strengthened in 2019. Data exchange between different public bodies, however, was temporarily halted by a supreme court ruling.</td>
</tr>
</tbody>
</table>

Making economic growth greener and more sustainable

Brazil’s greenhouse gas (GHG) emissions are comparatively low in per capita terms, and have been broadly stable since 2010 (Figure 1.31). Meeting the pledges made in the Paris accord for 2025, however, will imply cutting GHG emissions by 37% of 2005 emissions. As emissions have recently been on a slight upward rather than downward trend, this will be challenging and requires stepping up policy efforts. The three largest emission components are agriculture (34%), energy (32%) and land use and forestry (22%).

Figure 1.31. Total greenhouse gas emissions have been stable

Net greenhouse gas emissions by sector of origin

![Graph showing greenhouse gas emissions by sector of origin](http://educaciima.mma.gov.br/wp-content/uploads/2020/06/Estimativas-Anuais-5-2020.pdf)


Emissions from agriculture, the largest component, have been increasing slowly but steadily over the last 30 years. Livestock emissions, which account for more than half of these emissions, consist largely of
methane, which is 28 times more harmful to global climate than carbon dioxide (IPCC, 2013[63]). These emissions have grown at a much slower pace than meat or milk production, suggesting significant efficiency improvements and advances in low-carbon agriculture, which should be further pursued. In the longer run, however, curbing livestock emissions may require stronger economic incentives to move resources from livestock and cattle production towards crops or other forms of agriculture with lower emissions. Already, Brazil is far ahead on this as it does not subsidise cattle production, in contrast to many advanced economies. Pricing the external effects of cattle on global climate through corrective taxes, however, may be an interesting next step for the future that has recently been pursued by New Zealand.

Energy-related emissions have declined since 2014 in line with economic activity, but structural reductions will be more difficult to achieve than elsewhere as Brazil’s energy matrix is already remarkably clean. 45% of primary energy comes from renewable sources, as opposed to 10% across OECD countries, and 62% of electricity comes from hydroelectric sources. Further scope for expanding renewables may exist in solar energy, wind energy, where it will require easing import restrictions on relevant equipment, and in biofuels. The latter includes the move towards second-generation ethanol and the processing of by-products and biomass from agriculture, where a recently revamped biofuels policy is a step in the right direction.

The third largest emission component, land use and forestry, has shown a strong link to deforestation. In fact, annual deforestation numbers from the Amazon biome alone can explain 98% of the annual variation of this emission component and 96% of the variation in total emissions, according to OECD analysis based on the decomposition of variance. Bringing illegal deforestation down to zero by 2030, one of Brazil’s intentions in the Paris accord, is and has been a key environmental challenge for Brazil (Table 1.8), along with restoring and reforesting some previously deforested areas.

Table 1.8. Past OECD recommendations on green growth

<table>
<thead>
<tr>
<th>Recommendations</th>
<th>Actions taken since the 2018 Economic Survey</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ensure continuous decreases in deforestation, including through stronger enforcement and maintaining the status of areas currently under environmental protection.</td>
<td>Deforestation has risen rather than declined. Enforcement staff numbers have declined and the executive branch initiated discussions about less stringent rules for areas under environmental protection. A February 2020 decision to place deforestation-related policies under the responsibility of an inter-ministerial council headed by the Vice President may help to reduce deforestation.</td>
</tr>
</tbody>
</table>

Halting illegal deforestation in the Amazon region

The economic significance of Brazil’s forests, especially in the Amazon region, goes much beyond GHG emissions. The Amazon forest is a unique natural asset with a future economic potential that is hard to evaluate today. Protecting it for future generations makes good economic sense, particularly when taking into account that primary forest cannot be restored and that today’s deforestation generates private gains that are far below social value. A sustainable use of these natural assets is crucial for helping people in these regions to fulfil their productive potential, including people of indigenous origin who depend on the natural environment for their livelihoods and whose lifestyles are dependent on the preservation of Brazil’s natural habitats. Moreover, some researchers have expressed concerns that the Amazon forest may not be far from a series of tipping points, beyond which it could stop producing enough rain to sustain itself (Sampaio et al., 2007[64]; Lovejoy and Nobre, 2019[65]; Nobre et al., 2016[66]; De Bolle, 2019[67]). This is related to the Amazon’s role as a driver of atmospheric circulation and precipitation across South America and beyond (Werth and Avissar, 2002[68]).

Deforestation was on a declining trend between 2004 and 2012, following the establishment of a specific policy action plan to curb deforestation, supported by legal changes, significant investments into law enforcement and the use of real-time satellite imagery to direct enforcement interventions. Since 2013, however, this trend has become more erratic until deforestation rose significantly in 2019, and again in
2020. Without a strong drought, the number of fires peaked during August 2019 at a level nearly three times higher than in August 2018 and was hence significantly above normal (Barlow et al., 2019[69]).

Figure 1.32. Deforestation in the Amazon has picked up after a long decline

Brazil has the highest proportion of preserved native vegetation and 60% of national territory are under preservation (OECD, 2015[70]). The legal protection framework, including the 2012 forest law, natural reserves and indigenous areas, is well-developed (OECD, 2015[70]), and almost all recent deforestation was illegal. This strong framework has proven successful when coupled with strong enforcement efforts. The resurgence of deforestation, and in particular the strong pick-up in 2019, is related to a decline of resources dedicated to enforcing the forest law across the vast Amazon biome. Many retirement-related vacancies at the federal enforcement agency IBAMA have been left unfilled for years and enforcement staff has fallen by 55% since 2010. Leading enforcement officials have openly warned that implementing enforcement objectives set out in IBAMA’s Annual National Protection plan may be in jeopardy unless rapid action is taken and have called for more dissuasive enforcement action. Fines have declined, the destruction of illegal logging equipment has been questioned and loggers have come to feel less threatened by prosecution. Even when penalties are imposed, 97% of them have traditionally remained unpaid (Abromovay, 2019[71]).

Raising enforcement efforts through larger budgets and increased hiring of enforcement staff is an important pillar for stopping illegal deforestation. After some mixed signals, political messages about enforcement have recently become more consistent. A February 2020 decision to place deforestation-related policies under the responsibility of an inter-ministerial council headed by the Vice President may help to strengthen this pillar. Deployment of the armed forces to fight illegal deforestation has shown positive effects recently.

Given the immense global external effects of protecting the Amazon, international funding should be part of this strategy, possibly to a much larger extent than in the past. The Amazon Fund has so far disbursed USD 500 million, mostly from donations by Norway and Germany. In the absence of an agreement about the operative governance structure of the Fund, uncommitted funds have been frozen since August 2019.
Resuming this type of cooperation should be a priority, and will depend upon a reduction in deforestation in the Amazon, as well as on an agreement on a strategy for, and governance structure of, the Fund. Preserving past institutional advances is also crucial, including the forest law, the prohibition of logging in protected and indigenous areas and the sectoral agreement of a soy moratorium from 2006, which bars soy production in the Amazon.

In addition, incentives can also be used to foster compliance. Besides payments for environmental services, one way to do this would be by tying subsidised rural credit even closer to compliance with environmental regulations. These conditionalities have led to a substantial reduction in deforestation since 2008, mostly in municipalities where cattle ranching is the leading economic activity (Assunção et al., 2019[72]). For example, individual borrowing limits could be expanded for companies that are fully compliant with the forest code, including legal preservation requirements (Assunção and Souza, 2019[73]). Rural credit could also be used to promote the transition to low-carbon agriculture.

Neither economic development of the Amazon region nor agricultural production run counter to zero illegal deforestation and there is no trade-off between livelihoods and preservation. Brazil’s agricultural production, especially its most productive part, is in regions other than the Amazon. Most of the deforested areas in the Amazon are used for low-productivity and low-intensity cattle grazing and an estimated 12 million deforested hectares in the Amazon region are completely unused, often leading to degradation. The problem is not a lack of usable land, but a lack of economic incentives for more intensive land use, which will persist as long as current incentives, including weak enforcement, makes newly deforested land available at low prices.

The Amazon region also has significant untapped economic potential based on preservation rather than deforestation. This includes biological and medical research, pisciculture and eco-tourism. This opens up opportunities for high-end bio-industries in Brazil and elsewhere. In addition, Brazil has pledged to reforest 12 million hectares and reforestation has significant potential for job creation (Scaramuzza et al., 2017[74]).

The Central Bank has recently included a new sustainability dimension into its strategic agenda. Main issues in this area include improved regulations and the establishment of incentives for green rural credit, the creation of green instruments such as a green liquidity facility, increased monitoring of climate risks and the development of new stress tests, as well as enhanced transparency disclosure practices and risk management procedures based on recommendations by the Task Force on Climate-related Financial Disclosures.

### Table 1.9. Policy recommendations from this chapter (key recommendations in bold)

<table>
<thead>
<tr>
<th>MAIN FINDINGS</th>
<th>RECOMMENDATIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improving macroeconomic policies, governance and social protection</td>
<td>Keep interest rates low until inflationary pressures become clearly visible.</td>
</tr>
<tr>
<td>COVID19 has caused a strong recession. Inflation and inflation expectations are below target and monetary policy has been relaxed.</td>
<td>Apply fixed-term appointments for the Central Bank governor and directors and limit earlier dismissal to severe misconduct. Safeguard the budget autonomy of the Central Bank.</td>
</tr>
<tr>
<td>The Central Bank has conducted monetary policy in an independent way but formalising this independence would strengthen monetary policy effectiveness.</td>
<td>Ensure fiscal sustainability by continuing to comply with current fiscal rules, including the expenditure ceiling.</td>
</tr>
<tr>
<td>Fiscal outcomes require significant improvements as the pandemic has added to high public debt.</td>
<td>Strengthen spending efficiency by reviewing civil service pay structures, ineffective subsidies, special tax regimes and tax expenditures.</td>
</tr>
<tr>
<td>Better spending would allow savings without jeopardising policy objectives.</td>
<td>Reduce budget rigidity by reviewing revenue earmarking, mandatory spending floors and indexation mechanisms.</td>
</tr>
<tr>
<td>Mandatory spending items have reduced the room for fiscal policy as over 90% of the budget is now determined by law.</td>
<td>Index social security benefits to consumer prices rather than the minimum wage.</td>
</tr>
<tr>
<td>Spending on social transfers has increased, but most of it has failed to reach the poor, except for recent emergency benefits.</td>
<td></td>
</tr>
<tr>
<td>Proposed Improvement</td>
<td>Result</td>
</tr>
<tr>
<td>---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
<td>---------------------------------------------------</td>
</tr>
<tr>
<td>Despite large social transfers, there is no universal social safety net to protect dismissed workers against income losses. Recent emergency benefits improved this temporarily.</td>
<td>Increase benefits and accelerate benefit concessions in the <strong>Bolsa Família</strong> programme, while withdrawing benefits only gradually.</td>
</tr>
<tr>
<td>Labour informality affects 40% of workers and labour tax wedges are high in international comparison.</td>
<td>Reduce labour tax wedges for low-skilled workers by levying social security contributions at progressive rates, starting at low rates.</td>
</tr>
<tr>
<td>Exemptions, deductions and special regimes reduce revenues and progressivity of personal income taxes.</td>
<td>Eliminate the income tax deductibility of expenditures for private health and education expenses and lower the participation threshold in the SME tax regime Simples Nacional.</td>
</tr>
<tr>
<td>The exemption of basic goods from key consumption taxes is poorly targeted on poor households.</td>
<td>Convert the exemption of “basic goods” from consumption taxes into a targeted tax rebate available only to low-income families.</td>
</tr>
<tr>
<td>Overlapping unemployment insurance schemes raise the cost of formal job creation and fail to cover the 40% of workers in informal employment.</td>
<td>Merge the two current formal-sector unemployment schemes and reduce fiscal spending and employer contributions on these.</td>
</tr>
<tr>
<td>Corruption wastes public funds and exacerbates inequalities. Despite much progress in the fight against corruption, enforcement bodies have been subject to alleged political interference.</td>
<td>Strengthen the legal autonomy of all anti-corruption enforcement bodies.</td>
</tr>
<tr>
<td>Lengthy appeal procedures lead to court congestion and long delays between sentences and their execution. In penal cases, wealthy defendants can avoid serving prison sentences over many years.</td>
<td>Consider creating the legal basis for executing sentences as of the second instance of appeal, or limit the number of appeals, including to the Supreme Court.</td>
</tr>
<tr>
<td>A new abuse of authority law is unnecessarily vague, leaving room for retaliation against officials by powerful suspects.</td>
<td>Clarify and limit the circumstances under which public officials working on anti-corruption cases can be prosecuted.</td>
</tr>
<tr>
<td>Full disclosure of information on the ultimate beneficiary behind private companies to relevant authorities and private sector bodies is important to prevent asset hiding.</td>
<td>Facilitate data sharing across public agencies engaged in anti-money laundering efforts, including a single public registry.</td>
</tr>
<tr>
<td>Confiscating ill-obtained assets would also be made easier by criminalising illicit enrichment, which is currently only an offence but not a crime.</td>
<td>Make illicit enrichment a crime and not only an offence, to facilitate the confiscation of ill-obtained assets.</td>
</tr>
<tr>
<td>Whistle-blowing procedures are presently hampered by concurrent competences and parallel systems for similar offences, which make it difficult to protect whistle-blowers effectively.</td>
<td>Implement a dedicated whistle-blower protection law.</td>
</tr>
<tr>
<td>Public procurement is the government activity most at risk to waste, mismanagement and corruption. Recent efforts to centralise purchases online are promising steps.</td>
<td>Build on recent progress to review public procurement laws and strengthen provisions about conflicts of interests, incompatibilities and impartiality in public procurement.</td>
</tr>
<tr>
<td>Budget amendments are used by parliamentarians for projects in their constituency, but audits of these expenses are very rare.</td>
<td>Reduce parliamentarian budget amendments and audit these expenditures systematically.</td>
</tr>
<tr>
<td><strong>Making growth greener and more sustainable</strong></td>
<td></td>
</tr>
<tr>
<td>Brazil has a strong legal framework to protect forests. Deforestation declined up to 2014 but has risen particularly in recent years. Enforcement action has declined significantly, reflecting budget and staff cuts.</td>
<td>Build on past success in fighting illegal deforestation by strengthening enforcement efforts to combat illegal deforestation and ensuring adequate staffing and budget of environmental enforcement agencies.</td>
</tr>
<tr>
<td>Political discussions have sent mixed signals about the commitment to the existing environmental protection framework.</td>
<td>Avoid a weakening of the current legal protection framework, including protected areas and the forest code, and focus on the sustainable use of the Amazon’s economic potential.</td>
</tr>
<tr>
<td>Conditioning subsidised rural credit extended by public on compliance with environmental laws has helped to curb deforestation.</td>
<td>Consider raising borrowing limits in rural credit programmes for companies that are fully compliant with the forest code, or to finance the move towards low-carbon agriculture.</td>
</tr>
<tr>
<td><strong>Improving skills, education and professional training</strong></td>
<td></td>
</tr>
<tr>
<td>High secondary dropout rates reflect a lack of basic social and cognitive skills. Female labour force participation is hampered by lack of childcare facilities, particularly in low-income areas.</td>
<td>Continue expanding access to early-childhood education, prioritising access for low-income families and single mothers.</td>
</tr>
<tr>
<td>Low teacher salaries in international comparison make it difficult to attract talent, especially in low-income areas.</td>
<td>Consider raising teacher remuneration through temporary bonuses to qualified teachers for teaching in difficult schools.</td>
</tr>
<tr>
<td>Structural reforms like stronger competition and global integration will reallocate jobs across firms and sectors.</td>
<td>Scale up resources for professional training courses, but ensure their alignment with local labour market needs.</td>
</tr>
</tbody>
</table>
References


Cavalcanti Teixeira, L. (2019), Les impacts sociaux de l’ouverture commerciale au Brésil: Une analyse de la Zone de Libre Echange de Manaus et des reformes macroéconomiques des années 90, Universit'e Paris-Dauphine, https://www.dauphine.psl.eu/fr/recherche/soutenances-de-these/detail-dune-soutenance-de-these/soutenance/les-impacts-sociaux-de-louverture-commerciale-au-bresil-une-analyse-de-la-zone-de-livre-echange-de.html.


http://documents.worldbank.org/curated/en/449951570645821631/Gest%C3%A3o-de-Pessoas-e-Folha-de-Pagamentos-no-Setor-P%C3%BAbrico-Brasileiro-o-Que-Os-Dados-Dizem (accessed on 15 January 2020).


World Bank (2018), “Reforma do Estado”, in *Por um ajuste justo com crescimento compartilhado - Uma agenda de reformas para o Brasil*, World Bank Group, Washington, D.C., USA,

http://pubdocs.worldbank.org/en/156721534876313863/Sum%C3%A1rio-Notas-de-Pol%C3%ADtica-P%C3%BAbrica.pdf.

World Bank (2016), *Brazil - Systematic country diagnostic: retaking the path to inclusion, growth and sustainability.*