International
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STUDIES ON
GROWTH WITH EQUITY

BRAZIL

AN INNOVATIVE INCOME-LED STRATEGY

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The International Institute for Labour Studies (IILS) was established in 1960 as an autonomous facility of the International Labour Organization (ILO) to further policy research, public debate and the sharing of knowledge on emerging labour and social issues of concern to the ILO and its constituents — labour, business and government.

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FOREWORD

The ILO's Declaration on Social Justice for a Fair Globalization provides scope for assisting Members in strengthening their research capacity, empirical knowledge and understanding of how the strategic objectives of employment, social protection, social dialogue and rights at work interact with each other and contribute to social progress, sustainable enterprises, sustainable development and the eradication of poverty in the global economy.

In accordance with this plan of action, the 304th Session of the Governing Body set in motion a plan to strengthen the ILO's knowledge base through a series of pilot country studies conducted under the aegis of the International Institute for Labour Studies. The purpose of these studies is to (i) document examples where employment and social policies have successfully contributed toward mitigating the impact of the global financial crisis; (ii) extract policy lessons which could be useful to other countries; and (iii) examine country-specific challenges in the context of the crisis and moving forward.

This report on Brazil has been prepared by Janine Berg (ILO Country Office for Brazil), Byung-jin Ha, Naren Prasad and Steven Tobin (International Institute for Labour Studies) with contributions from Daniela Prates of the University of Campinas. The study has been coordinated by Steven Tobin under the supervision of the Director of the Institute, Raymond Torres. A draft summary of the report on Brazil was presented at a seminar organized by the ILO Brazil Office on 3 September 2010. The final report takes into consideration many of the comments received from national authorities, the social partners and other stakeholders during the seminar.

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LIST OF ABBREVIATIONS

BB	Banco do Brasil
BCB	Banco Central do Brasil (Central Bank of Brazil)
BNDES	Banco Nacional de Desenvolvimento Econômico e Social (National Social and Economic Development Bank)
BPC	Beneficio de Prestação Continuada (Continued Benefit Provision)
CAGED	Cadastro Geral de Empregados e Desempregados (Monthly data on formal job creation and destruction, Brazil)
CCT	conditional cash transfer
CDES	Conselho de Desenvolvimento Econômico e Social (Economic and Social Development Council)
CEF	Caixa Econômica Federal
CMN	Conselho Monetário Nacional (National Monetary Council)
CODEFAT	Conselho Deliberativo do Fundo de Amparo ao Trabalhador (FAT Deliberative Council)
Cofins	Contribuição para o Financiamento da Seguridade Social (Social Security Tax)
Copom	Comitê de Política Monetária (Monetary Policy Council of the Central Bank)
CRB	Commodity Research Bureau
DIEESE	Departamento Intersindical de Estadísticas y Estudios Socioeconómicos (Inter-Union Department of Statistics and Socio-Economic Studies)
FAT	Fundo de Amparo ao Trabalhador (Worker's Protection Fund)
FGC	Fundo Garantidor de Crédito (Credit Guarantor Fund)
FGTS	Fundo de Garantia por Tempo de Serviço (Guarantee Fund for Time of Service)
FIDC	Fundos de Investimentos em Direitos Creditórios (receivables investment funds)
FPM	Fundo de Participação dos Municípios (Municipalities' Participation Fund)
GDP	Gross Domestic Product
GNP	Gross National Product
IFS	International Financial Statistics (IMF database)
IILS	International Institute for Labour Studies
IBGE	Instituto Brasileiro de Geografia e Estatística
IMF	International Monetary Fund

INPC	Índice Nacional de Preços ao Consumidor (National Consumer Price Index)
IOF	Imposto Sobre Operações Financeiras (Tax on Financial Operations)
IPEA	Instituto de Pesquisa Econômica Aplicada
IPI	Imposto sobre Produtos Industrializados (Tax on Industrial Products)
IRPF	Imposto de Renda da Pessoa Física (Personal Income Tax)
MPS	Ministério da Previdência Social (Ministry of Social Security)
MTE	Ministério do Trabalho e Emprego (Ministry of Labour and Employment)
PAC	Programa de Aceleração do Crescimento (Growth Acceleration Programme)
PES	Public Employment Service
PLANFOR	Plano Nacional de Formação e Qualificação (National Plan for Training and Vocational Qualification)
PME	Pesquisa Mensal de Emprego
PNAD	Pesquisa Nacional por Amostra de Domicílios (National Household Survey)
PNQ	Plano Nacional de Qualificação Profissional (National Professional Qualification Plan)
PROGER	Programa de Geração de Emprego e Renda Rural (Programme for the Creation of Rural Employment and Income)
PRONAF	Programa Nacional de Fortalecimento da Agricultura Familiar (National Programme to Strengthen Family Agriculture)
RAIS	Relação Anual de Informações Sociais (an administrative database of formal employment that includes public sector workers)
RDB	Recibo de Depósito Bancário (Bank Deposit Receipt)
RET	Regime Especial de Tributação (Special Tax Regime on Real Estate)
RGPS	Regime Geral de Previdência Social (General Regime of Social Security)
RPC	Regime de Previdência Complementar (Complementary Pension Regime)
RPPS	Regimes Próprios de Previdência Social (Pension Regime for Government Workers)
Selic	Sistema Especial de Liquidação e Custódia de Titulos Públicos (Special System for Settlement and Custody)
SINE	Sistema Nacional de Emprego (Public Employment Service)
SME(s)	small and medium-sized enterprises
TJLP	Taxa de Juros de Longo Prazo (Long-term Interest Rate)

EXECUTIVE SUMMARY AND POLICY RECOMMENDATIONS

Economic growth with equity is possible – as the case of Brazil demonstrates – if policies are well-designed and sufficiently integrated.

It is often argued that policies to promote social inclusion and equity affect economic growth, suggesting the inevitability of a trade-off between economic and social goals. The case of Brazil, however, shows that there is no such trade-off – provided that the right policies are implemented.

The present review shows concretely how the growth-cum-equity strategy was designed and implemented in Brazil. It also analyses the extent to which the strategy helped Brazil overcome the global financial and economic crisis which erupted in the aftermath of the collapse of Lehman Brothers in 2008. Finally, the review identifies key pending challenges and formulates possible policy responses.

Initially, the global crisis had a significant impact in Brazil…

Brazil was by no means immune to the effects of the crisis. It was hit principally through three contagion channels: (i) the fall in the value of exports due to the collapse of external demand and the decline in commodity prices; (ii) the ensuing credit crunch that cut off external credit lines (including trade lines) and resulted in the outflow of portfolio investments; and (iii) a sharp reduction in the domestic supply of credit. The economy – which had been growing at an annual rate of nearly 7 per cent in the third quarter of 2008 – contracted by 2.0 per cent (annually) in the first quarter of 2009. Industrial production was hit hardest with particularly acute impacts on credit-sensitive sectors such as consumer durables. In fact, output in the industrial sector fell nearly 20 per cent in the last quarter of 2008 and the first quarter of 2009. The labour market was also considerably affected:

- In November and December 2008 alone, nearly 700,000 formal jobs were lost – 3.6 times higher than during the same months of the preceding year.
- Among the six metropolitan areas of Brazil, 594,000 jobs were lost (or 2.8 per cent of employment) between December 2008 and April 2009. In response to the job losses the unemployment rate rose to 9.0 per cent in March 2009 (0.4 percentage points above the March 2008 level).
- The impact on the industrial sector was particularly acute: between the months of November 2009 and March 2010, half a million formal manufacturing jobs were lost in the country.

… but recovery resumed soon after the start of the crisis…

The recession, however, lasted only two quarters – the economy grew by 4.2 per cent in the fourth quarter of 2009 and is expected to have grown more than 7 per cent in 2010, a pace that surpasses pre-crisis levels. Differently from other countries, the labour market recovery started before the recovery in GDP. This helped to stimulate aggregate demand and, by most metrics, erased most of the losses incurred as a result of the crisis:

- Employment started to grow as early as February 2009, and by the end of the year Brazil had added one million new formal jobs. Job growth continued at a strong pace in 2010, with 2.2 million (6.7 per cent) formal jobs added in the first ten months of the year (in comparison, during the previous crisis in 1999 there was a net job loss of nearly 200 thousand formal jobs).
- The unemployment rate in the six major metropolitan regions started to decline in April 2009 and continued to fall steadily throughout 2009, reaching 6.8 per cent in December. In early 2010 it rose again – as more people entered the workforce in search of jobs – but as of November 2010 the rate had fallen to 5.7 per cent – far below the pre-crisis rate of 7.6 per cent in September 2008.
- The weaker performance of manufacturing was in part compensated by stronger job growth in services, where employment was relatively unaffected and continued to grow almost without interruption.

Brazil also managed to avoid a sustained increase in informal employment – as measured by workers without a contract. During crises, workers often resort to informal employment to compensate for income loss. Experience shows that it is often difficult to reverse such trends after an extended period. In Brazil, however, the increases in informal employment were short-lived and have continued their downward trend over the course of the crisis. For instance, within the six major metropolitan areas, the number of employees without a contract fell by approximately 280 thousand (or 6.5 per cent) between August 2008 and August 2010.

...due, first, to solid initial conditions combined with a quick, job-centered response...

The pace of the recovery and the success in mitigating the effects of the crisis are owed to a number of factors:

1. *Pre-crisis experience and initial conditions*: Following the 1999 crisis, Brazil strengthened its macroeconomic fundamentals and continued to enhance its social protection system. In particular, it introduced a new macroeconomic regime – although criticized at the time – that focused on reducing external vulnerabilities and building fiscal surpluses. The Government also introduced – in cooperation with the social partners – mandated increases in the minimum wage and streamlined delivery of social assistance. As a result, at the onset of the crisis the Government was able to respond quickly by enacting a number of countercyclical measures and enhancements to existing social protection schemes – both made possible by the improved fiscal position.

2. *Addressing the origins of the crisis*: The financial crisis significantly affected the flow of credit in Brazil. The Government reacted decisively to restore credit to the financial system to ensure that credit continued to flow to individuals and businesses. These measures, included, but were not limited to: (i) a reduction in the policy rate target of 5 percentage points (from 13.75 per cent to 8.75 per cent) between January and September 2009; (ii) securing the flow of credit by introducing credit lines for key sectors of the economy, including small and medium enterprises (SMEs), and boosting

the availability of credit in the three public financial institutions; and (iii) a series of initiatives undertaken by the Central Bank to smooth exchange rate volatility and ensure US$ liquidity for firms, banks and exporters.

3. *Stimulating domestic demand in employment-intensive sectors*: The Government also adopted a number of measures to stimulate activity in employment-rich sectors, notably: (i) expansion of the Growth Acceleration Programme (PAC) with the majority of funding allocated to infrastructure investments that boosted job creation. This programme accounted for over 40 per cent of the stimulus efforts; (ii) the introduction of the Minha Casa, Minha Vida (My House, My Life) programme, which aimed to build one million new homes in 2009 and 2010 to stimulate growth and employment in the construction sector, which had been hit badly by the crisis; (iii) reductions in the industrial production tax (IPI) on motor vehicles and other products (some of which was intended to promote environmentally-friendly consumption).

4. *Stimulating demand and protecting the most vulnerable via enhancements to social protection*: Brazil made changes to two key social protection measures, notably the Bolsa Familia programme as well as the unemployment insurance system: (i) extended the duration of unemployment insurance benefits by two months for workers whose sector of economic activity was badly affected by the recession (such as mining and steelmaking); (ii) reiterated its commitment to the Bolsa Familia programme by improving benefit levels and extending coverage. The cost of both these amendments together was only 0.026 per cent of GDP. While comparably small in size in relation to other measures, the expansion of the coverage of Bolsa Familia helped 1.3 million additional families to benefit from the programme and an estimated additional 310,000 workers were able to receive extra support in the form of unemployment insurance. In addition, the Government also maintained scheduled increases in the minimum wage in February 2009 and January 2010, although these were not considered as part of the stimulus package. More than 20 per cent of the population benefited from these increases, as the minimum wage is also the reference for a number of social benefits.

5. *Ensuring that supply responded to demand incentives*: The Government made sure that the economy could respond to the above-mentioned stimulus measures and social policies. First, business investment was supported through the availability of credit from the three public banks, which stepped in at a time when private banks were weary of lending. The credit policies not only facilitated investments by large industries, but those of SMEs as well, as special lines of credit were developed for this business segment. Second, a stable business climate was established via social dialogue that prioritized consultation with business and union leaders in policy design, particularly regarding tax reductions. Third, product markets were made more responsive to the new incentives through the reduction in taxes and the boost in disposable income that enabled low- and middle-income families to increase their purchasing power, providing support to the economies of small, rural cities. Finally, at the start of the crisis the exchange rate was competitive, which helped support consumption of domestically produced goods and services.

…second, policy coherence between labour market and social policies on the one hand, and macroeconomic policies on the other.

One of the keys to Brazil's success, and an example of how countries can best design policies, was in recognizing the interplay between employment and social policies on the one hand and macroeconomic policies and economic growth on the other. Indeed, well-designed policies can have important mutually reinforcing effects – as the case of Brazil demonstrates:

- *Macroeconomic policies with employment multipliers*: The reductions in the industrial production tax (IPI) on motor vehicles, due to strong forward and backward linkages, gave an important boost to job creation. An estimated 25 million jobs – direct and indirect – are reliant on car manufacturing and the cut in IPI is estimated to have contributed to maintaining between 50,000 and 60,000 jobs in the Brazilian economy. Moreover, the Instituto de Pesquisa Econômica Aplicada (IPEA) estimates that each R$1.00 spent on cars has a multiplier effect of R$3.76 on aggregate output. Similarly, considerable support was given to the agriculture sector which in 2009 accounted for 16 per cent of the country's labour force compared to 5.2 per cent of 2009 GDP.

- *Well-designed social policies*: A preliminary estimate from IPEA demonstrates that the increased spending on the social cash transfers – Bolsa Família, Continued Benefit Provision (Beneficio de Prestação Continuada, BPC), and the General Regime of Social Security (Regime Geral de Previdência Social, RGPS) – had important multiplier effects. For instance, the BPC is estimated to have a multiplier effect of 2.2 on family income and 1.4 on GDP. In fact, enhanced social transfers are estimated to have led to an injection of US$30 billion into the economy and created (or saved) potentially 1.3 million jobs. These measures not only helped to mitigate the impact of the crisis on the most vulnerable, but also contributed to domestic demand growth by spurring local economic dynamism in employment-intensive sectors. They will also contribute to the longer-term development of Brazil.

In this respect, the lesson from Brazil is that social protection measures and macroeconomic policies, if well-designed, can contribute to economic growth, employment creation and equity. Moreover, for programmes to be effective they do not have to be costly.

Moving forward, however, the role of labour market policies could be strengthened…

Even in Brazil, where the recovery is well under way, there are areas for improvement and a number of challenges remain. One of the gaps in the crisis response concerns the area of labour market policies. Looking ahead, more attention and resources should be devoted to labour market intermediation and job training – two areas that received no additional resources during the current crisis. This would give jobseekers more opportunities to upgrade skill levels and remain attached to the formal labour market. Similarly, the temporary extension of unemployment insurance benefits could have been more widespread to include workers from other areas also hard hit by the crisis. Some consideration should be given to a number of reform areas:

- *Re-design unemployment insurance*: Efforts are needed to improve the overall coverage of the programme so that more workers are insured from job loss – fewer than 7 per cent of Brazil's unemployed received benefits during the crisis, while some key segments of the workforce, such as domestic workers, had essentially no coverage.
- *Employment retention schemes*: Given that the crisis was comparably short-lived, many companies could have benefited from employee retention schemes, particularly since dismissals can have detrimental effects on productivity and overall morale. In some instances social dialogue was used to lessen the number of dismissals by, for example, offering temporary lay-offs where workers underwent training courses and received unemployment benefits, or by organizing collective holidays. Policies such as work-sharing – whereby workers accept to work reduced hours, in some cases with government compensating the wage reduction – could have been effective in lessening the number of dismissals and the economic and social impact of unemployment. In this respect, and bearing in mind the importance of cost-effectiveness, Germany's Kurzarbeit programme could be considered a potential model of short-time working arrangements.
- *Enhanced educational attainment*: The lack of adequate skills is a serious obstacle to Brazil's future development and threatens productivity growth. Though primary and secondary enrolment has expanded notably over the past two decades, the quality of public education is of concern. Illiteracy has been reduced dramatically, but the level of functional illiteracy remains at troublesome levels, compromising the labour market prospects of a large proportion of the labour force as well as the country's competitiveness.
- *Improved integration*: More generally, Brazil needs to strengthen other labour market policies such as labour market intermediation and job training, as well as improve the integration of these programmes with the unemployment insurance system. Indeed, Brazil has an array of labour market policies, some of which have been in existence for many decades, but they could be leveraged to greater use.

Importantly, the Global Economic Linkages (GEL) Model developed at the International Institute for Labour Studies demonstrates that investments in the area of labour market policies, such as unemployment insurance, employment retention, labour market intermediation or public employment services, have important positive effects on output, employment and wages. And while such investments require expenditures in the short term, the model demonstrates that if such policies are well-designed, public debt levels recover to values similar to the baseline scenario over the medium term. Indeed, over time the fiscal position improves, due to overall improvement in employment and wages via an improved tax base and fewer expenditures on benefits such as unemployment assistance.

... and the effectiveness of the Public Employment Service increased…

For labour market policies and programmes to be effective, it is important to have a well-functioning public employment service (PES). A recent evaluation of Brazil´s PES, however, revealed some important deficiencies. First, only a small number of jobseekers are given referrals for labour market intermediation – in 2009 only 2.1 per cent of unemployed workers received support from the SINE (Sistema de Intermediação de Mão de Obra) during their job search. Moreover, even if referred, the placement rates from SINE are low, at around 18 per cent of the nearly six million workers registered over the period 2007–2009.

… complemented by continued improvements to integrate employment and social objectives...

Over the past couple of decades, Brazil has made substantial progress in reducing poverty and income inequality – aided by a comprehensive social protection system. However, poverty and inequality remain high by international standards. Promoting the creation of more formal jobs should help to improve social protection coverage and thus contribute to reducing the incidence of income inequality and poverty. Improving the effectiveness and delivery of labour market policies should help in this regard. However, more needs to be done to design social protection measures with labour market objectives in mind.

For example, while it is certainly laudable that more than 12 million families benefit from Bolsa Familia, the mere fact that one-quarter of the population qualifies for the programme is cause for concern. And though the social and economic benefits of the programme are well-established and well-documented in this report, future reform efforts could consider how best to integrate the beneficiaries into productive, quality and decent employment. Greater investments in basic skills and vocational training, labour market intermediation, and increased availability of child care services, could help to improve the access of workers to the new opportunities available in Brazil´s booming economy.

…while further improving productive investment, the tax system and the management of capital flows.

The challenge for Brazil is to ensure that recovery is sustained and that economic growth rates remain strong over the medium to long term. Though Brazil has many leading sectors – aeronautics, biotechnology, automobile manufacturing – it needs to increase its investment rates and improve its physical and social infrastructure in order to sustain and develop leading sectors and move away from its reliance on commodity exports for economic growth. Policies to increase overall investment, redesign the tax system and ensure a competitive exchange rate would be beneficial for improving the country's competitiveness and its development prospects moving forward.

- *Increase investment rates*: Although the Government has increased its investment levels over the past years, overall levels of investment are low – at about 17 per cent of GDP – which compares unfavourably with the period of import-substitution industrialization, and is well below the levels of emerging countries in Asia. Furthermore, investment in research and development is a low 0.5 per cent of GDP.
- *Redesign the tax system*: Tax revenues in Brazil at roughly 35 per cent of GDP are comparable to some OECD countries, and well above the average for Latin America. While this is beneficial because it means the

Government has the resources to finance its many expenses, the design of the tax system is regressive, as many taxes are levied on production and consumption. This is problematic because it hinders the growth of domestic demand and accentuates the already high level of inequality that exists in the country.

- *Ensure a competitive exchange rate*: Prior to the collapse of Lehman Brothers the Brazilian Real (R$) had become over-appreciated, but with the flight of capital at the onset of the crisis the R$ devalued by nearly 40 per cent. The positive growth scenario for Brazil, coupled with one of the world's highest interest rates, has renewed the flow of capital to the country, particularly of short-term portfolio investment. This investment has continued despite the 2 per cent tax levied on capital inflows in October 2009. As a result, the R$ appreciated steadily over the course of 2009 and 2010, returning to its pre-crisis highs. This is problematic, as an over-appreciated currency compromises the country's competitiveness, hurting domestic industry and thus job creation. More capital controls may be needed in the country. Brazil, as a member of the G20, could play a prominent role in advocating the regulation of international capital flows, to the benefit not just of the Brazilian economy but the world economy as well.

Social dialogue as a key factor of successful crisis recovery and for the future.

Key elements of Brazil's success in the context of the crisis, such as increases in the minimum wage and extension of unemployment insurance, are owing to social dialogue. This reaffirms the notion that social dialogue can play a critical role in the achievement of mutually reinforcing labour market and social objectives. Social dialogue can also – as evidenced by the Economic and Social Development Council (Conselho de Desenvolvimento Econômico e Social, CDES) – help improve the design of policies around programme reforms.

In sum, Brazil has made remarkable progress in the past decade – particularly in the context of the financial and economic crisis that started in 2008 – but moving forward, it should build on the success to date by continuing to ensure that the recent unprecedented economic growth is both inclusive and equitable.

CHAPTER 1
ECONOMIC AND LABOUR MARKET PERFORMANCE

INTRODUCTION

As of late 2010, the financial and economic crisis that began more than two years earlier continued to disrupt markets globally. At the height of the crisis in 2009, world GDP had fallen by nearly three per cent and tens of millions of jobs had been lost – threatening social and economic progress on a number of fronts. But not all countries were affected in the same manner or to the same degree. Similarly, as world economic output returned to positive territory in the second half of 2009, the pace of the recovery – especially as regards the labour market – has varied considerably.

Brazil, while not immune to the effects of the financial and economic crisis, has fared reasonably well compared to many countries – even within Latin America – in terms of economic and labour market performance. The purpose of this chapter is to examine economic, labour and social developments in Brazil during and leading up to the crisis that began with full force in 2008.

A MACROECONOMIC DEVELOPMENTS AND CRISIS TRANSMISSION MECHANISMS

Brazil was not immune to the crisis – external demand collapsed and domestic credit dried up...

Given that the eruption of the financial and economic crisis originated with the bankruptcy of Lehman Brothers and the near failure of other financial institutions in developed countries, notably the United States, the spillover to emerging and developing economies was initially small. Nevertheless, the crisis soon spread through financial, investment and trade linkages, leading to a significant depreciation in overall confidence in the global system – albeit to varying degrees (Box 1.1).[1]

Box 1.1 Crisis transmission channels in Brazil

Latin American countries were affected in various ways by the crisis, with the extent of their integration with the United States, where the crisis originated, playing a key role. Countries such as Mexico were hit first, through its close trade links to the United States as well as through a decline in workers' remittances, as many migrant workers from Mexico were affected by job losses in the United States.

Brazil was hit principally through three channels. First, the collapse in external demand and the fall in commodity prices led to a significant reduction in the value of exports. Second, the international credit crunch resulted in reduced external credit lines (including trade lines) and in an outflow of portfolio investment. Third, a sharp reduction in the domestic supply of credit came about as a result of panic among domestic banks due to the losses of approximately 220 leading Brazilian firms in over-the-counter foreign exchange derivative markets, following the abrupt devaluation of the Real (R$).

In fact, between August and December 2008 alone, the Real to the US dollar (US$) depreciated by approximately 48 per cent. However, as the Brazilian economy stabilized, coupled with remarkably low interest rates in the advanced economies, the R$'s value in terms of US$ appreciated throughout 2009 and has since stabilized to pre-crisis levels (aided by a tax imposed by the Brazilian Government on portfolio inflows).

Sources: ILO Country Office for Brazil; Nissanke (2009); Prates and Cintra (2010).

[1] IILS (2009)

Brazil, like most countries, experienced a significant decline in output, but one that – according to domestic growth figures which measure growth in each quarter compared to the previous quarter – lasted only two quarters. As Figure 1.1 illustrates, GDP had already started to slow in advanced economies at the end of 2007, turning negative in late 2008 and reaching a trough in the first quarter of 2009 in which GDP (quarter-over-quarter) fell by over 4.5 per cent. The deceleration in economic activity, however, was delayed somewhat in Brazil and Latin America (and other emerging economies) where GDP growth continued to improve until the last quarter of 2008. Nevertheless, for Brazil the relative impact on GDP was quite severe, with growth falling from an annual rate of nearly 7 per cent to approximately -2.0 per cent in just two quarters.

...but the fall in output was comparably low and short-lived.

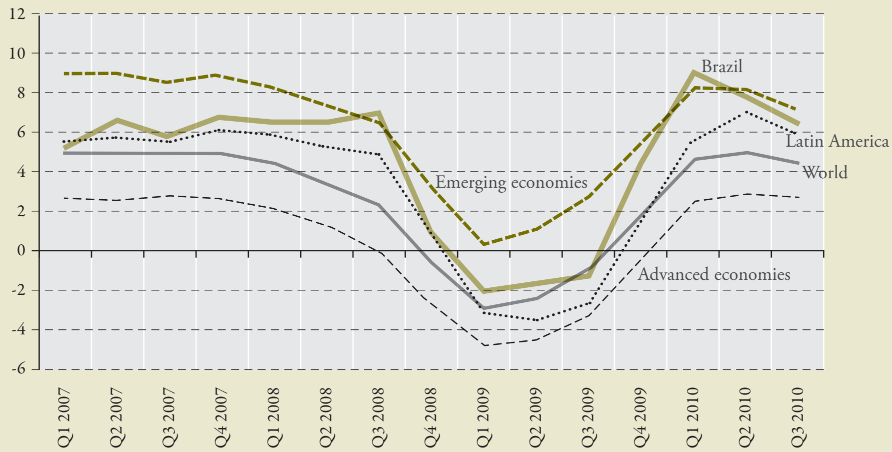
By the fourth quarter of 2009 GDP growth had rebounded to 4.4 per cent in Brazil, rising to nearly 9 per cent in the first quarter of 2010. For 2010, GDP growth is expected to hit 7.5 per cent for the year, surpassing pre-crisis levels.[2] In comparison, the downturn in both Latin America as a whole, and advanced economies, was more severe:

- The recession in Latin America was deeper, with growth falling to around -3.0 per cent between the first and third quarters of 2009. The recovery was also a little more tepid, with GDP growth of 1.2 per cent at the end of 2009;
- Growth in advanced economies remained in negative territory for the whole of 2009, returning to positive growth rates only in the first three months of 2010 – albeit at a moderate pace.

In emerging economies, although the rate of growth began to slow as early as the first quarter of 2008, it remained positive throughout the crisis and by early 2009 had already begun to improve.

[2] IMF (2010a)

Figure 1.1 GDP growth, quarterly real GDP rate, 2007–2010 (percentage change from one year earlier)

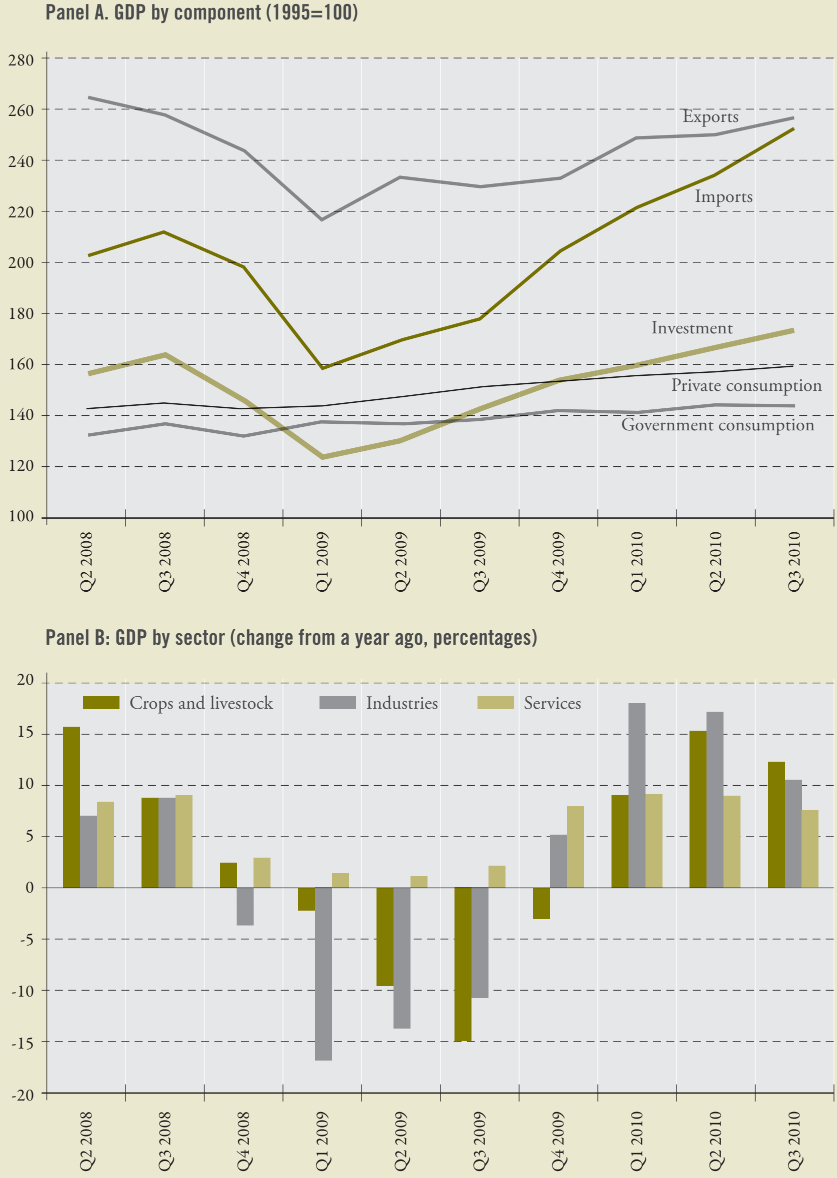


Source: IMF (2010a).

Nevertheless, industrial production was hit hard – offset by continued gains in services.

In Brazil, among the different components of GDP it was imports, exports and investment that experienced the steepest declines – roughly 15 per cent in the first quarter of 2009 compared to the same quarter of the previous year (Figure 1.2, panel A). Private and government consumption – which account for over 80 per cent of GDP – remained relatively stable over the period of the crisis. In terms of sectoral performance, domestic credit constraints hit industrial production first and hardest, with particularly acute impacts on credit-sensitive sectors such as consumer durables. Compared to the previous year, industrial production fell moderately in the last quarter of 2008 (3 per cent) but the pace quickened and output dropped more than 10 per cent in each of the first three quarters of 2009 (Figure 1.2, panel B). Agriculture and livestock production also fell to a similar degree but the decline was more gradual. On the other hand, services – which account for around 59 per cent of GDP – were relatively stable throughout the crisis, remaining positive year on year.

Figure 1.2 **GDP growth by component and sector, Q2 2008–Q2 2010**



Source: Banco Central do Brasil, the Time Series Management System (SGS). Data are seasonally adjusted.

Investment and trade activity rebounded strongly in 2010: investment and imports grew by over 25 and 40 per cent respectively in the first quarter of the year, approaching or surpassing pre-crisis levels. And as external and domestic demand recovered (notably the latter), the industrial sector followed in late 2009, growing by over 5 per cent in the first quarter of 2010 compared to a year earlier.

B LABOUR MARKET PERFORMANCE

The impact on employment has varied significantly for a given fall in output...

There have been significant differences in the impact of the global financial and economic crisis on employment across both developing and emerging economies (Figure 1.3). Among the advanced G20 and European Union economies analysed, the best-off (relative to the median) include Australia, Canada and the Republic of Korea.[3] Those hardest hit to date are Ireland, Japan and Luxembourg in terms of output losses, with Ireland and Spain most affected in terms of job losses.[4] Among the emerging G20 and European Union economies, Argentina, Brazil, Indonesia and Turkey have fared comparably well in terms of employment losses and GDP (China has performed exceptionally well as regards the latter). On the other hand, Estonia, Latvia and Lithuania have been most severely affected in terms of GDP growth and employment losses.

...but on a seasonally adjusted basis, Brazil incurred the fewest job losses...

Within Latin America the impacts of the crisis on employment have also varied considerably, with Ecuador, Jamaica and the Bolivarian Republic of Venezuela incurring employment losses of 5 per cent or more (Figure 1.4). In other countries such as Argentina, Brazil and Colombia, job losses were much less severe at 2 per cent or less on a seasonally adjusted basis. In fact, among the group with available information, Brazil incurred the fewest losses as a percentage of employment (0.7 per cent).[5]

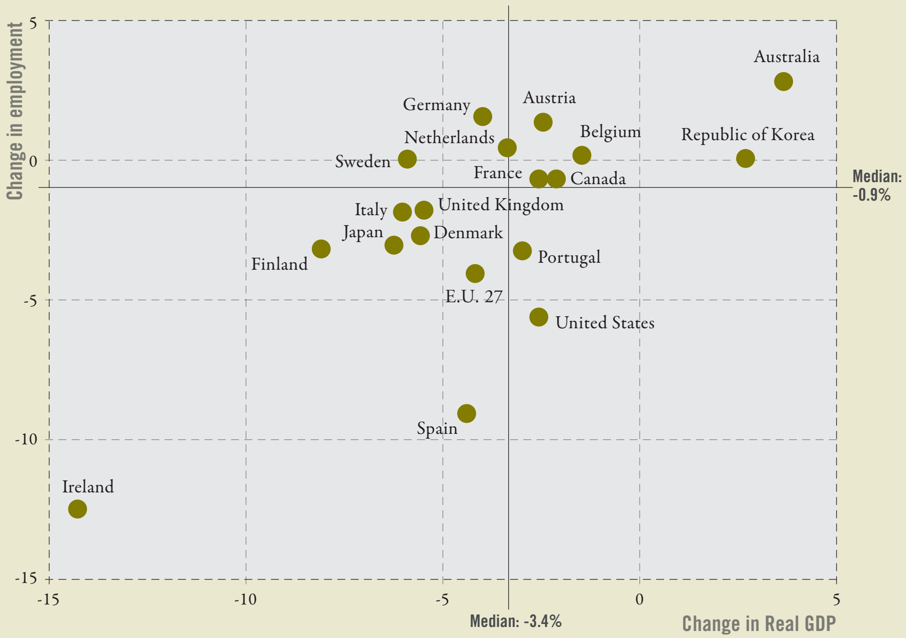
[3] High or low growth reductions or employment losses were analysed relative to the median of growth and employment changes. It is also important to note that the countries highlighted are compared only with other countries in the same group.

[4] During the course of 2010, countries such as Greece, Ireland, Portugal and Spain are also confronted with a number of fiscal challenges as pressures to reign in government spending mount.

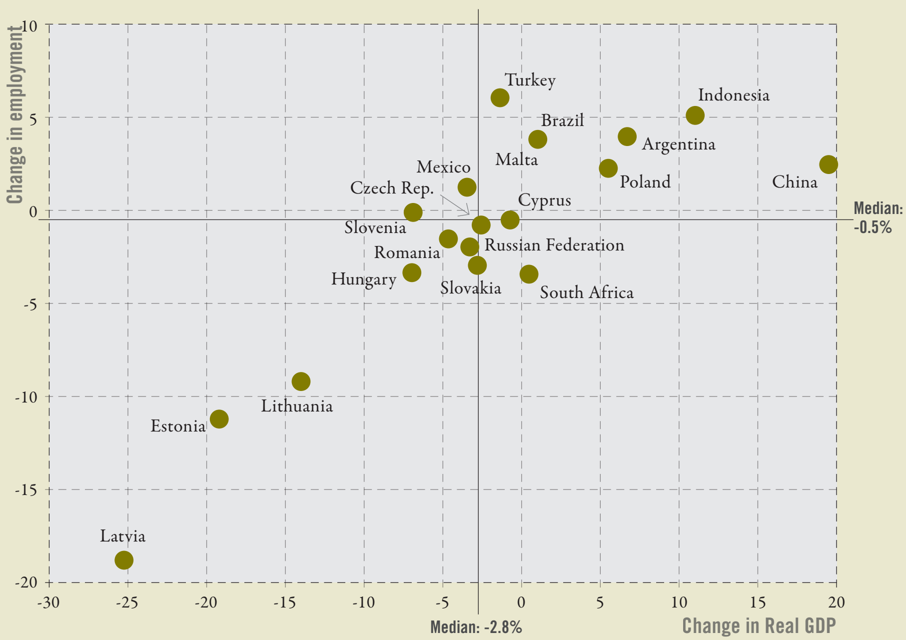
[5] Data for Brazil refer to the six major metropolitan areas, notably Belo Horizonte, Porto Alegre, Recife, Rio de Janeiro, Salvador and São Paulo. Data in these areas account for approximately 25 per cent of the country´s labour force.

Figure 1.3 Variations in real GDP and total employment between Q2 2008 and Q2 2010 (percentages)

Panel A. Advanced G20 and European Union countries



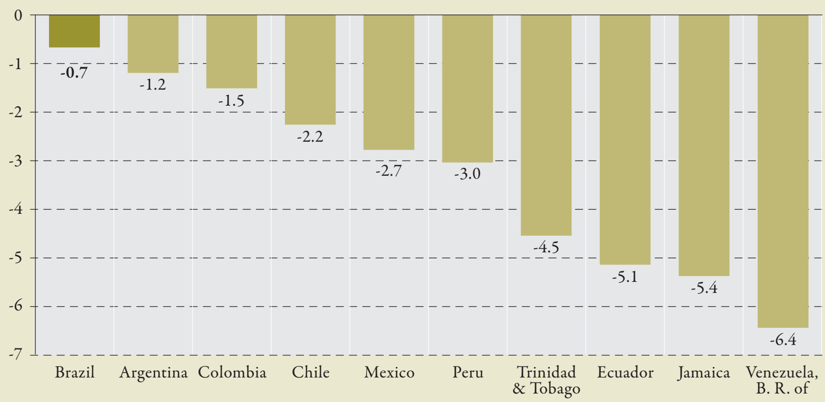
Panel B. Emerging G20 and European Union countries



Note: The division between advanced and emerging G20 countries is based on a median calculated on per capita GDP for the period. The comparison across countries in the same group is made relative to the median of the group.

Sources: IILS estimates based on OECD (2009); Eurostat database; ILO, Laborsta database; and IMF, IFS database.

Figure 1.4 Change in employment from peak to trough by country (percentages)



Note: Figures for Argentina, Brazil, Ecuador and Peru refer to job losses in urban or metropolitan areas as a share of employment in those areas. Data are seasonally adjusted.
Source: IILS estimates based on ILO, Laborsta database.

.. with employment attaining pre-crisis levels already in late 2009.

For patterns of employment losses within Brazil, there are essentially two sources of information that track up-to-date labour market developments: the first is the household survey of urban areas – the Pesquisa Mensal de Emprego (PME) – undertaken by the Brazilian statistical institute (IBGE), and the second is the administrative database compiled by the Ministry of Labour (MTE) which documents formal monthly job creation and destruction data (CAGED) in the whole of Brazil. In terms of jobs lost – on a non-seasonally adjusted basis – the two surveys reveal that:

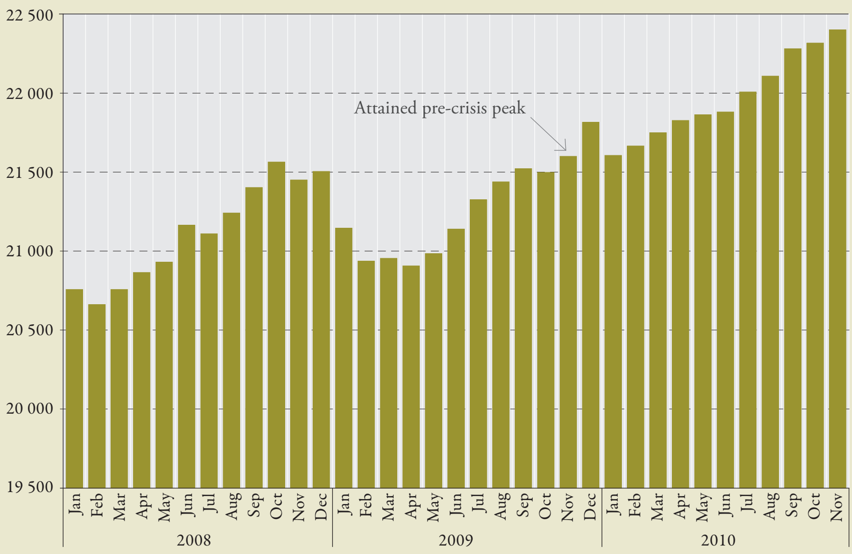
- In November and December 2008, nearly 700,000 formal jobs were lost in the country, according to CAGED data. Although the end of the year is typically associated with job losses owing to the end of the harvest season, the 2008 losses for these months were 3.6 times higher than during the same months of the preceding year.
- Among the six metropolitan areas of Brazil surveyed by the PME, 594,000 formal and informal jobs (or 2.8 per cent of employment) were lost between December 2008 and April 2009 (Figure 1.5).

While the employment loss was significant, employment growth in the six metropolitan areas began to recover quickly, as Figure 1.5 illustrates. It began to pick up in the second half of 2009 and already in November 2009 had surpassed the pre-crisis peak. It fell marginally in January 2010 – as is typical of the season – but has since continued to grow. Indeed, as of November 2010, employment was 3.9 per cent above its pre-crisis peak in October 2008, with nearly 1.5 million jobs (nearly 7 per cent) added since February 2009 in urban areas. Similarly, according to CAGED data, net employment creation turned positive in February 2009 with 3.6 million net formal jobs created nationwide by November 2010.

The unemployment rate has also fallen even as people have reentered the workforce in light of improved prospects...

Similar trends are apparent with respect to the unemployment rate, which started to rise in late 2008. In the six major metropolitan regions it increased from a pre-crisis low of 6.8 per cent in December 2008

Figure 1.5 Employment in urban areas of Brazil, 2008–2010
(unadjusted, 000s)

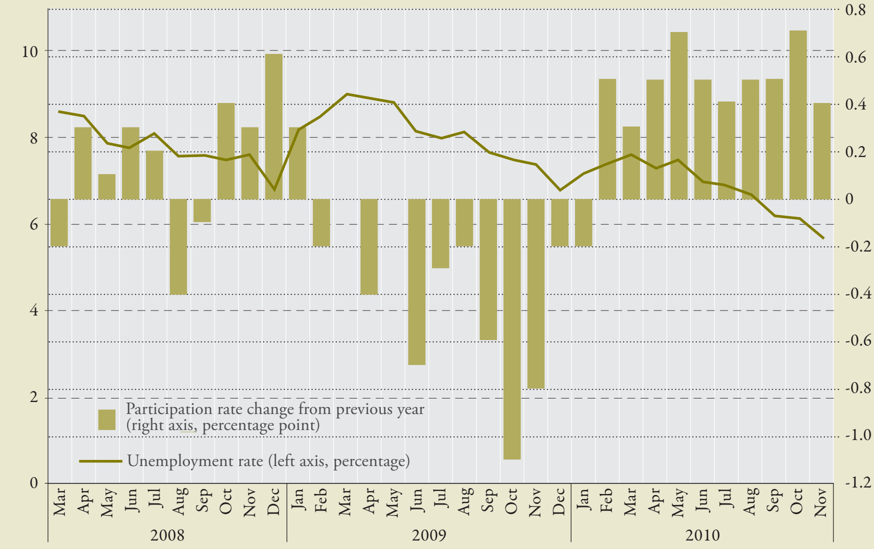


Note: Data refer to the six major metropolitan areas.
Source: Instituto Brasileiro de Geografia e Estatística (IBGE), Pesquisa Mensal de Emprego (PME).

to 9.0 per cent in March 2009 (Figure 1.6), but then declined steadily throughout 2009, reaching its pre-crisis low of 6.8 per cent in December 2009. Part of this fall was due to the fall in participation rates. At the beginning of 2010, however, even though employment continued to grow the unemployment rate began to rise marginally as more people entered the labour market looking for work. It thus edged up to reach 7.4 per cent in May 2010 – still well below the crisis high of 9 per cent. By November 2010 the rate had fallen to 5.7 per cent, well below its pre-crisis low.

In terms of the impact on employment, the effects mirror to a great extent the sectoral impact on GDP. Indeed, the losses in employment were very much concentrated in manufacturing: within the six metropolitan areas some 117,000 industrial jobs were lost between January and February 2009 alone. With respect to services, employment was relatively unaffected and continued to grow – indeed, the weaker performance of manufacturing was in part compensated by stronger job growth in services (see also Chapter 3).

Figure 1.6 Monthly unemployment rate and participation rate changes from previous year, 2008–2010



Note: Data refer to the six major metropolitan areas.
Source: Instituto Brasileiro de Geografia e Estatística (IBGE), Pesquisa Mensal de Emprego (PME).

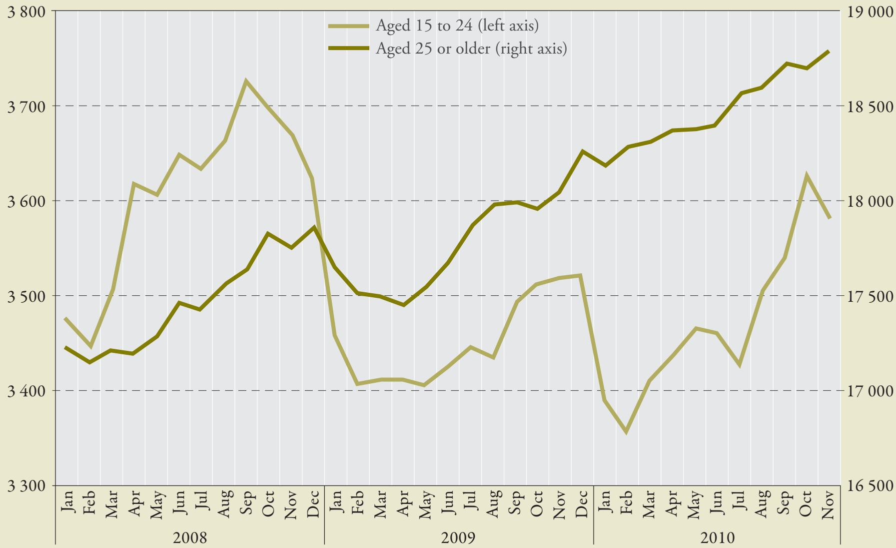
And with men over-represented in the secondary sector of the economy, particularly manufacturing, employment fell steeply for this group during January and February 2009. With manufacturing employment remaining suppressed for the first half of 2009, so did male employment. Both began to recover slowly in the second half of 2009, and despite seasonal job losses in December 2009, employment among men has continued to grow throughout 2010, reaching pre-crisis levels in the second quarter. Employment among women began to fall sooner – probably due to the fact that they are over-represented in precarious work in Brazil. However, employment recovered quickly for women – already by the second quarter of 2009 female employment growth was positive; it attained pre-crisis levels in August of that year – six months earlier than male employment.

... but youth continue to struggle.

In the major metropolitan areas, both adults (aged 25 years or older) and youth (aged between 15 and 24 years) experienced employment losses in late 2008 and early 2009 but the magnitude of the decline was particularly acute among youth. In fact, employment among youth fell by over 300,000 – which accounts for half the total job losses during this period. Although adult employment rebounded during the latter half of 2009 and the first half of 2010, employment for workers aged 15 to 24 fell again in early 2010 and still has not recovered to pre-crisis levels (see Figure 1.7). As of November 2010, youth unemployment rates in Brazil – at 13.6 per cent – are 3.3 times higher than those for adults aged 25 and over. Indeed, empirical evidence from past financial crises suggests that youth unemployment rates tend to rise significantly and remain higher for some years after a crisis.[6] For example, among countries able to restore youth unemployment rates to pre-crisis lows, it took 11 years for this to occur.[7] In another group of countries where only a new low could be attained, it took more than 17 years to reach it.

[6] Ha et al (2010).
[7] See IILS (2010).

Figure 1.7 Employment levels by age group, 2008–2010
(thousands)



Note: Data refer to the six major metropolitan areas.
Source: Instituto Brasileiro de Geografia e Estatística (IBGE), Pesquisa Mensal de Emprego (PME).

Despite a modest increase during the crisis, informal employment has continued to decline...

In developing countries informal employment is often an important labour market consideration.[8] In the context of the Brazilian labour market, informal employment encompasses (i) wage workers without a signed labour card and (ii) self-employed workers (not contributing to social security).[9] However, the share of informal workers – both those without a signed labour card and the self-employed – has been declining for a numbers of years and importantly, as Figure 1.8 shows, this trend has continued throughout much of the crisis, notably throughout the first half of 2009. In both instances, the share of informality rose briefly in the latter half of 2009, but has since continued its downward trend.

[8] Informal employment is defined by the ILO as encompassing those workers who are not recognized under the law, or who are employed informally either in an informal or formal enterprise, and therefore receive no legal or social protection and are unable to enforce contracts. See ILO (2002).
[9] Employees in Brazil must hold a carteira de trabalho assinada (a signed labour card) which guarantees workers access to formal labour protection. For the purposes of the analysis in Figure 1.8, however, self-employment is treated as informal given that only 15 per cent of the self-employed contribute to the social security system (*previdência*).

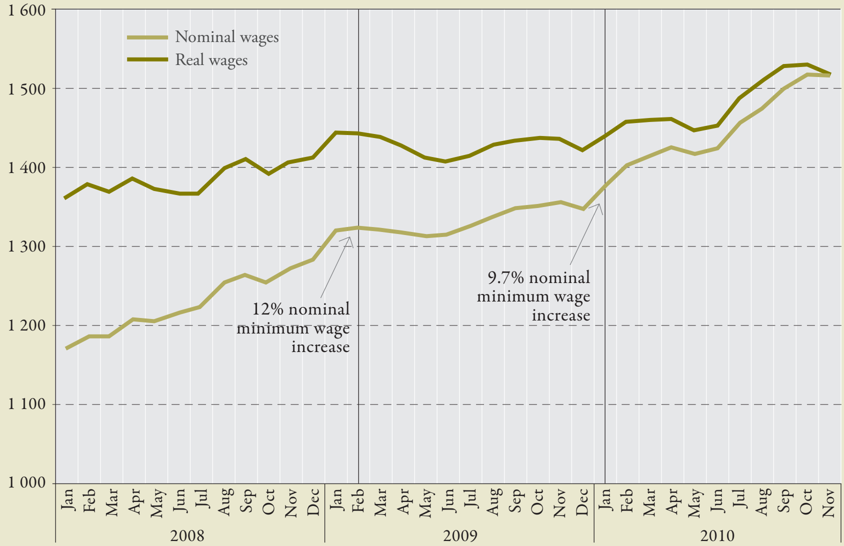
Figure 1.8 **Informal employment as a share of total employment, 2008–2010**
(percentages)

Note: Data refer to the six major metropolitan areas.
Source: Instituto Brasileiro de Geografia e Estatística (IBGE), Pesquisa Mensal de Emprego (PME).

... and real wages have grown, aided in part by increases in the minimum wage...

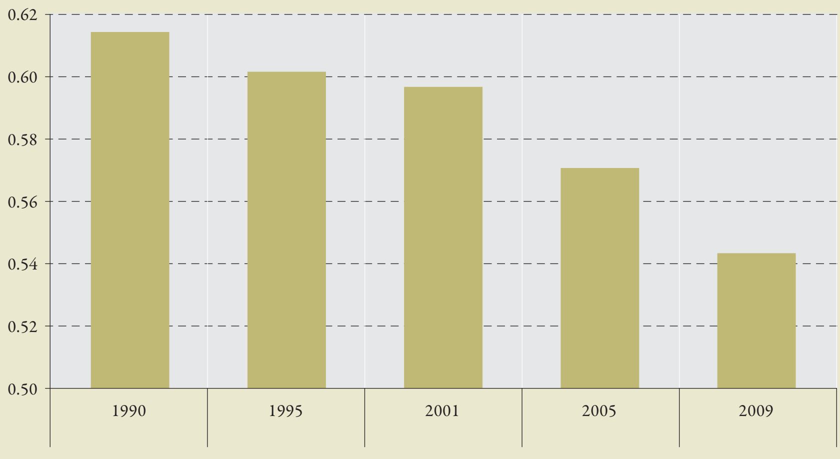
The existence of a minimum wage has had important implications for Brazil during the crisis (see also Chapters 3 and 4). This is because the minimum wage in Brazil sets the level of remuneration for formal wage employment in both the private and the public sectors but can also influence informal worker earnings, as negotiations are often made using the minimum wage as a benchmark. The minimum wage in Brazil also serves as a benchmark for a number of social security policies, including pensions and unemployment benefits (see Chapter 4).

Figure 1.9 **Evolution of average nominal and real wages, 2008–2010**
(R$ per month)



Source: Instituto Brasileiro de Geografia e Estatística (IBGE), Pesquisa Mensal de Emprego (PME).

Figure 1.10 **Inequality in Brazil, 1990–2009**
(measured in Gini coefficient)



Source: Instituto de Pesquisa Econômica Aplicada (IPEA).

Prior to the crisis, in 2006, a decision was made by the Brazilian Government – in consultation with the social partners – which specified the dates and the formula for minimum wage increases, beginning in April 2007 through to 2011. As Figure 1.9 illustrates, this has helped support overall wage growth in Brazil: average nominal and real wages have risen over the course of 2009 and early 2010. Importantly, during the crisis the scheduled increases were maintained, with the first nominal increase in February 2009 of 12 per cent (6 per cent real increase) lifting the minimum wage to R$465 (US$234) per month. In January 2010 the minimum wage was further increased by 9.7 per cent (5.7 per cent in real terms) to R$510 (US$283) per month.

...which has accompanied improvements in income distribution.

At the same time, income inequality – as measured by the Gini index – continued to fall (Figure 1.10). In fact, income inequality has been on a downwards trend since 1990, with the decline particularly dramatic in the past decade: between 2001 and 2009 the Gini fell from 0.60 to 0.54. In comparison, the index fell only marginally in the previous decade. More importantly, income inequality has continued to decline during the crisis.

C CONCLUDING REMARKS

As the financial and economic crisis accelerated in the second half of 2008, few countries or regions – including Brazil and Latin America – were isolated from its effects. However, Brazil has sustained the shock of the global recession relatively well. The impact on growth and employment, while substantial, was comparably low and relatively short-lived.

As of the first quarter 2010, economic growth had returned to pre-crisis levels. Job growth in fact led the recovery, with employment in the six metropolitan areas surpassing the pre-crisis peak already in November 2009. The unemployment rate edged up at the beginning of 2010, mainly due to more workers entering the labour market in search of employment, but has since decreased to below pre-crisis levels.

This economic and labour market success has been accompanied by improvements in overall social conditions. Poverty and income equality – though high – have continued to decline over the course of the crisis. In addition, real wages are rising and the rate of informality has continued to fall. Much of the success is to due to existing policies and programmes, but also to special efforts by the Government to mitigate the effects of the crisis. Chapter 2 presents a brief overview and broad assessment of Brazil's response to the global financial and economic crisis and the subsequent chapters examine the role of the range of policy levers, including labour market and social policies, in mitigating the impact of the crisis, and the key design features underlying their success.

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CHAPTER 2
BRAZIL'S POLICY RESPONSE TO THE CRISIS

INTRODUCTION

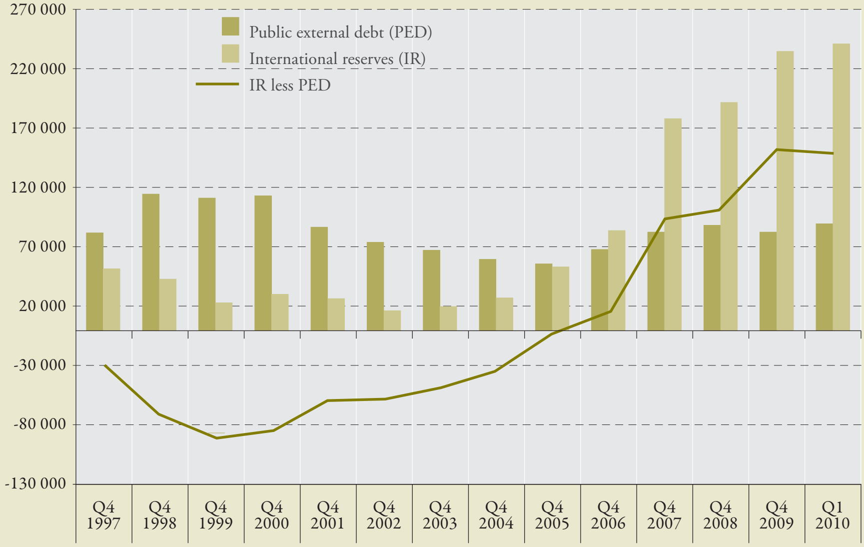
Brazil was severely affected by the global financial and economic crisis that started in 2008, but the impact on output and employment – as Chapter 1 illustrates – was short-lived. Brazil's success in weathering the crisis is a departure from past experiences, and the nature of its response documented in this chapter demonstrates how different policy levers, such as monetary, credit, fiscal and labour market and social policies, can complement and reinforce one another if designed and implemented effectively. Although Brazil's fiscal stimulus package at 1.2 per cent of GDP is among the lowest of the G20 countries, it was effective precisely because it was implemented alongside a significant expansion of credit funnelled through the country's public banking system, and an easing of monetary policy. This was complemented by tax exemptions to support business activity, and improvements to social safety programmes that, along with wage growth, bolstered domestic demand. In many ways, however, such a comprehensive response was made possible via a number of pre-crisis reforms that took place in the decade prior to the crisis.

This chapter documents the various policy initiatives in more detail. Beginning (section A) with a brief discussion of how this crisis differs from those of the past, it provides (section B) a review of the monetary, credit and exchange-rate policies undertaken. Section C examines the fiscal stimulus package introduced in early 2009, including a comparison with other G20 countries. This will set the stage for examining in more detail how well-designed employment-oriented policies and social protection measures can have mutually reinforcing benefits while stimulating enterprise development and growth (the purpose of Chapters 3 and 4, respectively). In addition, section D will document the role of social dialogue as a support mechanism for responding to the crisis and the final section will conclude by discussing a number of policy considerations.

A WHY THIS CRISIS WAS DIFFERENT

The impact of the international financial crisis and the Brazilian response to it represents in many ways a break from the past. Indeed, had the external shock occurred during 1994–2002, the effect on output and employment might have been much more severe. The increased resilience of the Brazilian economy was in large part due to improved macroeconomic fundamentals, in particular reduced external vulnerability of the public sector. This relates as much to the increase in international reserves as to the fall in the public external debt that made the Government a creditor in foreign currency as of January 2006. After that date debt levels remained stable, but as reserve accumulation accelerated, the creditor position continued to increase until the onset of the crisis (Figure 2.1).

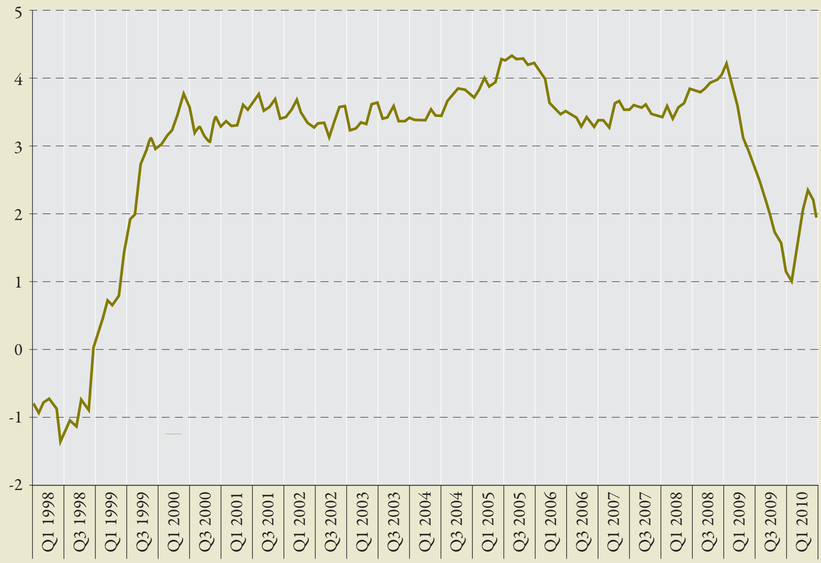
Figure 2.1 Public external debt and international reserves, 1997–2010
(US$ million)



Source: Banco Central do Brasil, the Time Series Management System (SGS).

Figure 2.2 **Primary surplus as a percentage of GDP, 1998–2010**

(flows accumulated over 12 months)



Source: Banco Central do Brasil, the Time Series Management System (SGS).

A second favourable condition was the sizeable primary surplus in the country's fiscal accounts. As shown in Figure 2.2, the primary budget has been in surplus since 1999 (between 3 and 4 per cent of GDP until 2008), when the Government began to pursue a specific target for this. The target increased successively between 1999 and 2007 (3.1 per cent in 1999, 3.4 per cent in 2000 and 2001, 3.88 per cent in 2002 and 4.25 per cent from 2003 to 2007). In 2008 it was reduced to 3.8 per cent as result of the launch of the Growth Acceleration Programme (Programa de Aceleração do Crescimento, PAC). In 2009, in response to the fiscal stimulus and the fall in tax revenues owing to the lower level of activity, the Government reduced the public-sector primary surplus target to 2.5 per cent. For 2010, the target for the public-sector primary surplus was set at 3.3 per cent.

In contrast, during the last crisis episode (the currency crisis of 1998/1999), Brazil's macroeconomic situation was fragile, both internally as well as externally. In 1998 the Government was a debtor in foreign currency and had a domestic primary deficit of around 1 per cent of GDP. Thus, when speculative attacks occurred on its currency in the second semester of 1998 (and resulted in the exchange rate devaluation of January 1999), the Government resorted to a loan from the IMF. The loan, however, called for pro-cyclical (that is, restrictive) monetary and fiscal policies that reinforced rather than alleviated the negative impact of the currency crisis.

During the recent crisis, however, the Brazilian Government was able to cope with the contagion effect without relying on external funding or related conditionalities. As a result, it had greater space to adopt policies aimed at mitigating the negative effects of the crisis, as opposed to instituting pro-cyclical austerity policies. The improved macroeconomic condition not only blunted the impact of the external shock, but allowed for additional monetary injections to stimulate economic activity.

In addition, Brazil entered this crisis with a far more developed social safety net. New social assistance programmes and an expansion of already existing pension and assistance programmes during the last decade (discussed in Chapter 4) meant that households were better able to protect themselves from the crisis. It also allowed the Government – at little additional cost – to increase benefits to assist households while providing an effective policy tool for boosting consumption and aggregate demand in the economy.

The Government could afford to finance spending on social protection and other measures of the fiscal stimulus package because of its improved fiscal position, which to large extent was driven by its effort to pursue a primary surplus following the 1999 currency crisis. Following that crisis the Government adopted a new macroeconomic regime that consisted of a floating (dirty) exchange-rate mechanism, the pursuit of primary surplus on the country's fiscal accounts, and inflation targeting. Moreover, during the 1990s, the Government put in place a number of reforms to strengthen the financial sector, including for example increased capital requirements and improved risk management systems. This new regime, concomitant with strong global economic growth between 2003 and 2007 characterized by an abundance of international liquidity and favourable trade conditions, facilitated the improvement in Brazil's macroeconomic situation and more sound financial institutions. Thus, capital inflows and the trade account surplus (resulting mainly from growth in trade with China and higher commodity prices) brought about a reduction in the public external debt and an accumulation of international reserves, which increased the country's overall capacity to resist and respond to external shocks.

The improved "policy space" is also related to two other dimensions of the recent crisis: first, the origin of the current crisis, notably the United States; and second, the adoption of countercyclical policies by advanced economies. In previous crises, one of the specific aims of the adoption of pro-cyclical policies by developing countries was to regain credibility in financial markets, a precondition seen as necessary for the resumption of external capital flows.[10] Due to the systemic nature of the current crisis, governments of emerging countries were cognizant that pro-cyclical policies would be ineffective in attracting capital flows, as they were no longer viewed as a necessary, much less favourable, policy response. And since the advanced economies at the epicentre of the crisis had implemented countercyclical policies, these policies gained greater acceptance among the economic orthodoxy. Thus, although subject to an external shock in common with a number of emerging market economies, Brazil was able to take a more proactive rather than reactive policy stance.

[10] Ocampo (2000).

B MONETARY, CREDIT AND EXCHANGE-RATE POLICY

The immediate impact of the international financial crisis on Brazil was a credit crunch. Given the uncertainty with respect to financial contagion, banks withdrew credit not only from companies and individuals but also from banks on the interbank market. The Government responded with a series of measures to restore liquidity in the economy, including monetary, credit and exchange-rate policies. In particular, the Central Bank of Brazil (Banco Central do Brasil, BCB) undertook measures almost immediately to increase liquidity in the interbank market which had suffered strong liquidity contractions related to the losses from exchange derivatives by companies following the devaluation of the Real (R$):

- On 24 September 2008, the BCB decided to postpone the timetable for implementation of the increase in reserve requirement of leasing companies. According to the schedule established by the BCB in January 2008, the reserve requirement would be increased from 15 to 20 per cent in November and to 25 per cent in January 2009. The modifications postponed these changes to January and March 2009. On 12 October 2008, the BCB also established that leasing companies could deduct from the reserve requirement the amounts referring to foreign currency acquired from the BCB. These currency transactions would be formalized under a resale commitment by the financial institution and a repurchase commitment by the Central Bank.
- From September 2008 to December 2008, the BCB reduced reserve requirements on cash deposits and time deposits and the additional liability compliance which affected cash, time and savings deposits. The rules for additional liability compliance were also changed: after 1 December 2008 withdrawals would no longer be made in cash, but rather would be fulfilled by federal public bonds indexed to the policy rate. With this change, BCB attempted to ensure that the demand for federal public bonds would not be affected by the change in the withdrawal rule for time deposits.[11] Compulsory reserves were reduced by R$99.8 billion

[11] The BCB began to increase reserve requirements again on 26 February 2010. By June 2010 the process had not yet ended.

(US$54.2billion) and the liquidity for smaller institutions was increased by R$41.8 billion (US$22.7 billion) in the last quarter of 2008. By changing the requirements related to reserve ratios, the BCB influenced the volume of funds available for financial institutions to lend.

- To stimulate purchases of credit portfolios from small and medium-sized banks by the major banks, on 2 October 2008 the BCB allowed banks to deduct 40 per cent of the reserve requirements on time deposits for purchases of credit portfolios from financial institutions (with net worth up to R$2.5 billion (US$1.4 billion)). On 13 October 2008 the BCB once again changed the rules for compulsory collection on term deposits, raising the percentage of the compulsory resources that banks could deduct for the purchase of other banks' credit portfolios from 40 to 70 per cent. It also extended the range of eligible assets that banks could buy with compulsory resources, authorizing bond acquisitions from investment fund portfolios, credit rights resulting from leasing, fixed-income instruments issued by private non-financial entities, assets that make up Receivables Investment Funds (fundos de investimentos em direitos creditórios, FIDC) or shares in FIDC organized by the Credit Guarantor Fund (Fundo Garantidor de Crédito, FGC), the national private deposit insurance institution.[12]
- The Government created a new liquidity assistance line whereby the BCB could acquire credit portfolios from financial institutions. The aim was to extend authority for the BCB to assist Brazilian financial institutions that faced cash shortages, mainly small and medium-sized banks. Access would be given through the rediscount window, and the range of assets accepted as guarantee for these loans was also expanded.
- On 28 October 2008 the Banco do Brasil (BB) and the Caixa Econômica Federal (CEF), both financial institutions controlled by the Brazilian Federal Government, were authorized to directly or indirectly acquire ownership interest in private and public financial institutions in Brazil, including insurance companies, social welfare institutions and capitalization companies, with or without the acquisition of the capital stock control.

[12] Initially, the end date of this measure was to be 30 June 2010. In June 2010, the BCB postponed the end date to 31 December 2010.

- In March 2009 the Government instituted the Bank Deposit Receipt (Recibo de Depósito Bancário, RDB) with the special guarantee of the FGC. Through this measure the deposit insurance on time deposits was increased from R$60,000 (US$30,000) to R$20 million (US$10 million). The measure was adopted to stimulate interbank lending or the purchase of credit portfolios by major banks, which had remained limited to that point. Given the preference for liquidity by private banks and the possibility of liquid, profitable and very low-risk investments in public bonds, the banks simply did not expand interbank credit.[13] In fact, only the state-owned banks (BBB and CEF) acquired substantial credit portfolios. With the RDB, liquidity in the interbank market began to flow again. This last measure was thus effective.

1 INTEREST RATE POLICY

The interest rate reduction in Brazil started with delay. Indeed, at the November 2008 meeting of the Monetary Policy Council of the Central Bank (known as the "Copom", Comitê de Política Monetária), it was argued that the threat of inflation caused by the devaluation of the Real was too high to allow a reduction. By December, the threat of the crisis on economic activity outweighed the threat of inflation and a series of cuts started, which reduced the policy target rate, known as the Selic,[14] by 5 percentage points, from 13.75 per cent in December 2008 to 8.75 per cent in September 2009. BCB's rigidity in conducting monetary policy in the last quarter of 2008 strongly contrasted with the actions of its colleagues in the principal advanced and emerging economies. In all, five cuts were made: on 21 January 2009, from 13.75 to 12.75 per cent; on 11 March 2009 to 11.25 per cent; on 29 April 2009 to 10.25 per cent; on 10 June 2009 to 9.25 per cent; and on 23 July 2009 to 8.75 per cent.[15] This was the lowest level in over 20 years (equivalent

[13] Although no takeovers took place, significant mergers were announced in the banking sector in the fourth quarter of 2008: one between the private banks Itaú and Unibanco, which became the largest bank in Brazil, and another between BB (publicly owned) and Nossa Caixa (state-owned). BB also acquired an ownership interest (49.9 per cent) in Votorantim Bank (privately owned).

[14] Sistema Especial de Liquidação e Custódia de Titulos Públicos (Special System for Settlement and Custody).

[15] On 28 April 2010, the Copom began to raise the policy rate target again.

to a real annual rate of less than 5 per cent), given projected inflation of 4.0 per cent. However, the rate remains far above that of other countries.

2 CREDIT AND FINANCIAL POLICY

In addition to the measures of monetary policy, the Brazilian Government decided to use the three major federal public banks – Banco Nacional de Desenvolvimento Econômico e Social (BNDES), CEF and BB – to expand credit and thereby play a countercyclical role in a context of tightening credit conditions by private banks.

Besides the two measures mentioned above (authorization for BB and CEF to acquire ownership interest in private and public financial institutions in Brazil, and the capitalization of BNDES), on 6 November 2008 the Ministry of Finance announced a series of new initiatives that together provided R$19 billion (US$10 billion) in credit lines for various sectors via BNDES and BB, and in August 2009 the Government made an additional contribution of R$500 million (US$250 million) to the endorsement funds of these two banks, which guarantee loans to small and medium-sized enterprises. Furthermore, the state-owned banks established new credit lines to some sectors, as detailed below.

The countercyclical action of state-owned banks was extremely important in maintaining the supply of credit to individuals and companies in a context of the high-liquidity preference of private banks, and so to avoid a sharp drop of economic activity (see also Chapter 3). Other measures of credit policy included a cut in the long-term interest rate (Taxa de Juros de Longo prazo, TJLP) used for the BNDES loans from 6.25 to 6 per cent, the lowest level in history, thereby reducing the cost of BNDES' long-term loans.

3 EXCHANGE-RATE POLICY

Because of the liquidity problems in the currency market that surfaced during the early months of the crisis, the BCB adopted a series of initiatives that included:

- foreign exchange swap auctions: the contracts included a commitment to resell dollars to BCB, thus maintaining the current level of reserves (between 19 September 2008 and November 2008, R$18.8 billion (US$ 10.2 billion));
- spot market sale of dollars (R$26.7 billion (US$14.5 billion) between October 2008 and February 2009);
- resumption of forward sales of foreign exchange in the market (R$65.7 million (US$33 billion) in sales and clearing of the Central Bank swap position in June 2009);
- provision of export financing: BCB provided dollar lending to exporters (R$28.3 billion (US$14.2 billion) between October 2008 and June 2009);
- offers of credit lines in dollars to refinance the foreign debts of Brazilian firms, allocating up to R$36 billion (US$20 billion) of the country's reserves. This measure benefited approximately 4,000 enterprises;
- tax reduction from 1.5 to 0 per cent on financial operations (Imposto Sobre Operações Financeiras, IOF) established in March 2008 on foreign portfolio investments in fixed income (bonds and private fixed income and derivative transactions that result in yield index). Exchange settlement transactions relating to the entry and return of foreign loans (subject to rate of 0.38 per cent since January 2008) were also exempted from the IOF.

Several of these mechanisms were used, but once credit lines were reestablished demand tapered off. By December 2009 Brazil had unwound almost all the emergency foreign exchange liquidity facilities implemented during the crisis. The measures had several positive results: (i) smoothing exchange-rate volatility and alleviating short-term foreign exchange pressure; (ii) providing forward dollar liquidity to alleviate pressure on corporations, thus deterring them from unwinding hedged positions; (iii) increasing the availability and reducing the cost of foreign exchange for Brazilian corporations and banks over the terms of swap, and stemming depreciation in the short term; (iv) providing dollar financing for exporters. It is also worth mentioning that a US$ swap facility with the United States also bolstered the external liquidity of Brazil.

4 SOVEREIGN WEALTH FUND

In early 2009 the Government created a sovereign wealth fund, with an initial amount of 0.5 per cent of GDP (around R$12 billion (US$6 billion)). It intends to use these funds to provide the country with savings to compensate for any future economic fluctuations and finance the internationalization of Brazilian companies. The fund announced that R$5 billion (US$2.5 billion) would be released for infrastructure investments.

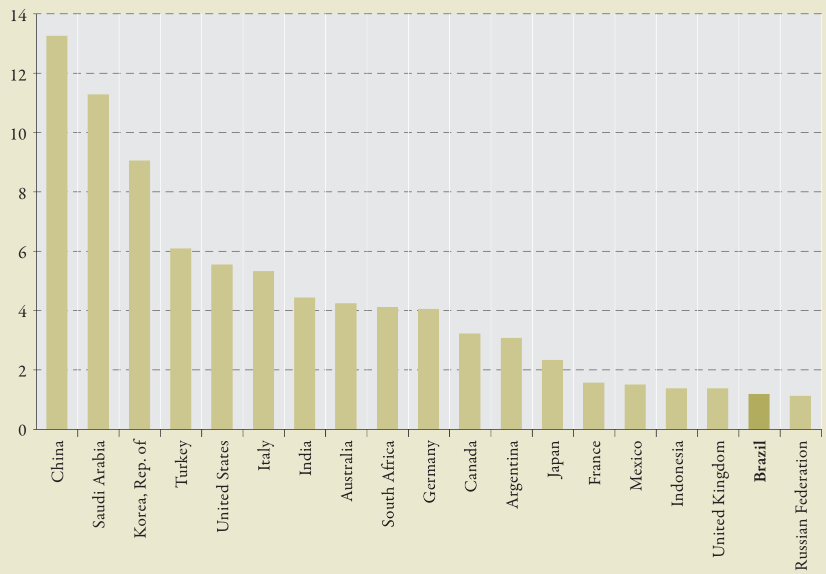
C THE FISCAL STIMULUS PACKAGE

In addition to the monetary, exchange-rate and credit policy actions, fiscal measures aimed at boosting economic activity via both the private and the public sectors were also undertaken.

1 OVERVIEW

The Government adopted a fiscal stimulus package at a cost of R$37.9 billion (US$20.6 billion), equivalent to 1.2 per cent of Brazil's GDP in 2008. In terms of magnitude, however, the overall stimulus efforts were small in comparison to other G20 countries (Figure 2.3). In fact, only the Russian Federation had a smaller stimulus package as a percentage of 2008 GDP.

Figure 2.3 **Fiscal stimulus in G20 countries as a percentage of GDP**



Source: IILS estimates based on national sources.

Table 2.1 Components of the fiscal stimulus package

Stimulus package	US$ billion	% of GDP	Share of stimulus package (%)
Infrastructure	**8.3**	**0.51**	**40.3**
Increase in Growth Acceleration Programme (PAC)	5.0	0.31	24.3
Minha Casa, Minha Vida	3.3	0.20	16.0
Tax cuts	**7.6**	**0.40**	**36.9**
Subsidies	**3.1**	**0.20**	**15.0**
Agriculture	2.2	0.14	10.7
BNDES	0.9	0.06	4.4
Transfers to municipalities	**1.1**	**0.07**	**5.3**
Social protection	**0.5**	**0.03**	**2.4**
Expansion of Bolsa Familia	0.3	0.02	1.5
Extension of unemployment insurance benefits	0.2	0.01	1.0
Total	**20.6**	**1.21**	**100**

Source: ILO, based on information from the Ministry of Finance.

As Table 2.1 illustrates, the package was relatively varied in composition with (i) 40.3 per cent in infrastructure; (ii) 36.9 per cent in tax cuts; (iii) 15 per cent in subsidies; (iv) 5.3 per cent for transfers to municipalities; and (v) 2.4 per cent in measures related to social protection.

2 INCREASE IN GOVERNMENT SPENDING ON INFRASTRUCTURE

In periods of downturn, public spending on infrastructure stimulates economic activity and generates employment, with little risk of deterring private investment. Public infrastructure investment also enhances long-term growth prospects and has a large multiplier effect on economic activity through backward and forward linkages, although the employment impact varies considerably depending on, for example, the structure of the economy, the types of public works undertaken (whether they are capital or labour-intensive) and the country's capacity to implement projects rapidly and successfully.

Taken together, emerging economies have dedicated a much higher proportion of stimulus spending to infrastructure, about 50 per cent for 2009–10, than advanced economies at about 21 per cent.[16] On average, emerging G20 economies are spending close to 1 per cent of GDP in 2009 and 2010 for infrastructure projects, compared with advanced G20 economies which are spending close to 0.4 per cent of GDP.

In the Brazilian stimulus package, the increase in infrastructure investment accounts for 40.3 per cent of the total, equivalent to R$15.3 billion (US$8.3 billion) or 0.5 per cent of GDP. Its aim was to boost investment which, as Chapter 1 illustrated, was hit hard by the crisis. In particular, it included two elements to support job creation and promote investment in employment-intensive sectors, notably (i) an expansion of the Growth Acceleration Programme (Programa de Aceleração do Crescimento, PAC), which existed prior to the crisis; and (ii) government incentives and subsidies for housing construction, called Minha Casa, Minha Vida (My House, My Life), a new policy unveiled in response to the crisis and targeted at low- and middle-income households.

Expansion of the Growth Acceleration Programme (PAC)

The Growth Acceleration Programme (PAC), launched by the Brazilian Government in January 2007, is a government programme with three main objectives: (i) to increase government investment in infrastructure; (ii) to stimulate private investment; and (iii) to remove the main obstacles to economic growth (bureaucracy, inadequate norms and regulation).

The programme also aims to raise productivity and reduce regional inequalities within Brazil. When launched, the total forecasted infrastructure investment was R$423 billion (US$235 billion) between 2007 and 2010, of which R$369 billion (US$205 billion) would be provided by state-owned companies and the private sector, with the remaining R$54 billion (US$30 billion) financed by the Federal Government. Three areas were prioritized: logistics, energy, and social and urban infrastructure (Table 2.2).

[16] ILO (2010).

Table 2.2 **Planned investment in infrastructure: The Growth Acceleration Programme (PAC)**

	US$ billion	% of GDP
Logistics	**27.3**	**0.58**
Federal budget	15.4	0.33
Government enterprises and other sources		
Energy	**128.6**	**2.71**
Federal budget	-	-
Government enterprises and other Sources	**128.6**	2.71
Social and urban infrastructure	**79.9**	**1.69**
Federal budget	16.3	0.34
Government enterprises and other sources	63.6	1.34
Total	**235.8**	**4.97**
Federal budget	31.7	0.67
Government enterprises and other sources	204.1	4.3

Source: www.brasil.gov.br/pac.

After the onset of the crisis, the Government committed to maintaining its planned outlays and the stimulus package included an increase of R$9 billion (US$5 billion) (or 0.3 per cent of GDP, representing 24.3 per cent of the stimulus package) in PAC investments.

Minha Casa, Minha Vida (My House, My Life)

The new housing programme Minha Casa, Minha Vida to subsidize low-income housing construction was announced by the Brazilian Government in March 2009. The programme is expected to cost the Federal Government R$34 billion (US$17 billion), or approximately 1.2 per cent of GDP. The cost in 2009, included in the stimulus package, was R$6.6 billion (US$3.3 billion), equivalent to 0.2 per cent of GDP and representing 16.0 per cent of the overall package.

Financing for this programme will come from the Federal Government (R$2.5 billion or US$1.3 billion) and from the Guarantee Fund for Time of Service (Fundo de Garantia por Tempo de Serviço, FGTS) (R$7.5 billion or US$43.8 billion), a monthly fund accessible at dismissal, retirement, or for the purchase of the home, financed by payroll.

The programme seeks to build one million new homes in 2009 and 2010 for low-and middle-income families, with a maximum income equivalent to ten times the minimum wage. A principal objective of the programme is to reduce the housing deficit in the country, estimated at 7.2 million houses, by 14 per cent. It is expected that 400,000 houses will be built for families with monthly incomes up to three times the 2009 prevailing minimum wage (R$1,395 or US$701). Families in this income bracket will be expected to contribute 10 per cent of their income to the mortgage, for a period of ten years, with a minimum monthly payment of R$50 (US$25). The remaining costs, including insurance, will be subsidized by the Government, with an expected cost of R$16 billion (US$8 billion). An additional 400,000 houses will be built for families who earn between three and six times the minimum wage (R$1,395–R$2,790 or US$701–US$1,402) per month. For these families, mortgage contributions will not exceed 20 per cent of monthly income, and the families will benefit from a guarantee fund in the case of unemployment.

3 TRANSFERS TO MUNICIPALITIES

In order to avoid the adoption of pro-cyclical policies in municipalities – due to the fall in tax revenues caused by the lower level of activity – the stimulus package also included extraordinary budgetary transfers to local governments in 2009, amounting to 5.3 per cent of the package (R$2.2 billion (US$1.1 billion) or 0.07 per cent GDP in 2009).

The Federal Government committed to maintaining a stable nominal value of constitutional transfers to municipalities, equivalent to the value of 2008 despite the drop in federal revenues in 2009. The municipalities were therefore compensated for the decrease in funds from the Municipalities' Participation Fund (Fundo de Participação dos Municípios, FPM) due to the cut in federal taxes. By supporting municipalities, the Government guaranteed the maintenance of municipal services, many of which are an important source of formal jobs in small cities.[17]

[17] Cardoso (2007).

4 TAX CUTS

A series of tax cuts – equivalent to 36.9 per cent of the stimulus package (R$15.1 billion (US$7.6 billion) or 0.4 per cent of GDP) – was announced in order to boost consumption and give support to sectors most hit by the crisis (Table 2.3). It included a reduction in the Personal Income Tax (Imposto de Renda da Pessoa Física, IRPF) through a revision of the income tax tables whereby new lower rates were created (7.55 and 22.5 per cent), which favoured middle-class families, that is, those who earn up to R$1741 (US$875) per month.[18] In addition, the Tax on Financial Operations (IOF) was cut from 3 to 1.5 per cent for direct consumer credit operations and the overdraft credit line; the Tax on Industrial Products (Imposto Sobre Produzidos Industrializados, IPI) was temporarily cut; and a Special Tax Regime on Real Estate (Regime Especial de Tributação, RET) was introduced whereby the tax on real estate costing up to R$110.6 million (US$55.6 million) (Minha Casa, Minha Vida) was reduced from 7 to 1 per cent and from 7 to 6 per cent for all other cases.

The largest component of the tax reductions was the reduction in IPI. In December 2008, this tax was cut for motorcycles, trucks and automobiles (up to 1,000cc from 7 to 0 per cent and for those up to 2,000cc from 13 to 6.5 per cent). The tax cut for cars, scheduled originally to end in December 2009, was extended until March 2010, although the vehicles needed to be energy-saving (flex cars) to qualify for the reduction, in an effort to promote

Table 2.3 Tax reductions included in the stimulus package

Tax reductions in 2009	US$ billion	GDP (%)
IRPF (Personal Income Tax)	2.7	0.14
IPI (Tax on Industrial Products)	3.2	0.17
IOF (Tax on Financial Transactions) – credit	1.4	0.07
Cofins (Social Security Tax) – motorcycles	0.2	0.01
RET (Special Tax Regime on Real Estate)	0.1	0.01
Total	**7.6**	**0.4**

Source: Ministry of Finance.

[18] The reduction in personal income tax had been planned prior to the crisis but was put into effect as a response to it.

environmentally-friendly consumption. In the first semester of 2009 the IPI tax cut was also extended to household electrical appliances, building construction materials and capital goods. Moreover, the Social Security Tax (Contribuição para o Financiamento da Seguridade Social, Cofins) on the production of small motorcycles (up to 150 cc) was reduced from 3.65 per cent to 0.65 per cent and the exemption of a tax levied on wheat, wheat flour and bread that had been scheduled to end in July 2009 was extended to December 2010.

In addition, in November 2008 the Government extended payment deadlines for various federal taxes in an attempt to ease pressure on corporate cash flows, such as withholding income tax, Cofins, and the IPI. The income tax was postponed from the 10th to the 20th of each month; the IPI was postponed from the 15th to the 25th of each month and the Cofins from the 20th to the 25th. The change responded to a prior demand of the productive sector and had gained prominence during the crisis owing to credit constraints.

5 SUBSIDIES

Subsidies account for 15.0 per cent of the stimulus package (equivalent to R$5.6 billion (US$3.1 billion) or 0.2 per cent of GDP). Two policy actions provided them:

- The Government capitalized the BNDES (the state-owned development bank) with more than R$100 billion (US$56 billion, 3.3 per cent of GDP) to ensure resources for private investment. This measure was off budget: it was a below-the-line loan to BNDES and is not considered to be part of the stimulus package.[19] What is included in the package is the subsidy on interest costs worth R$1.6 billion (US$0.9 billion, 0.06 per cent of GDP). BNDES lends at an interest rate of around 6 per cent, well below the yield on government bonds of 12 per cent, which the Treasury needs to raise resources for BNDES's capitalization. The extra resources

[19] IMF (2009).

from the R$100 billion (US$56 billion) capitalization allowed BNDES to increase its volume of credit by 85 per cent.

- The Government reduced the cost of loans to the agricultural sector through subsidies on the interest rate at a cost of R$4 billion (US$2.2 billion), equivalent to 0.14 per cent of GDP.

Extension of unemployment insurance benefits

In order to alleviate the reduction in workers' income in the crisis, the Ministry of Labour extended the duration of unemployment insurance benefits by two months for workers whose sector of economic activity was badly affected by the recession (such as mining and steelmaking). This element represented 1 per cent of the stimulus package (R$0.4 billion (US$0.2 billion) or 0.012 per cent of GDP). In March 2009 the extension was granted to workers in these sectors who were laid off in November and December 2008 (103,707 workers). In May 2009, the extension was also granted to those laid off in January 2009 and February 2009 (an additional 216,500 workers). In 2009, the average unemployment benefit was R$595 (US$299), or 1.3 times the minimum wage prevailing at the time (R$465 (US$234). Importantly, this measure was the result of social dialogue between the Government, enterprises and labour unions.

Extension of the Bolsa Familia

Countries that have social protection systems have a valuable built-in mechanism for stabilizing their economies and addressing the social impact of the crisis. Since 2003 the Brazilian Government has had a conditional cash transfer (CCT) programme called Bolsa Familia that seeks to reduce poverty and hunger and improve social development, by means of a direct income transfer to poor and extremely poor families. As explained in greater detail in Chapter 4, at the onset of the crisis the Government reiterated its commitment to the programme and announced its expansion. Although this expansion had already been in the pipeline, the crisis gave the Government greater impetus to follow through with it. In total, this measure cost R$0.5 billion (US$0.3 billion), equivalent to 1.5 per cent of the stimulus package.

As recommended by the Global Jobs Pact, the Brazilian Government strengthened the social protection system to provide income support and protect persons and families affected by the crisis, particularly the most vulnerable. However, the discretionary social protection expenditure as a percentage of total stimulus and of GDP was one of the smallest among G20 countries.[20]

6 SECTOR-SPECIFIC POLICIES

In addition to the policies listed above, the Government also adopted sector-specific measures for small businesses, as well as for construction, agriculture and manufacturing, which were badly affected by the crisis.

Assistance to SMEs

Small and medium-sized businesses (SMEs) are important employers and represent a very large slice of the Brazilian economy (as is true of most other economies). In Brazil they represent almost 98 per cent of all enterprises, 60 per cent of formal employment and 22 per cent of GDP.

The Brazilian Government recognized the contribution of SMEs to job creation and adopted specific measures for this segment, including access to affordable credit and tax benefits, in order to ensure a favourable environment for their development. The main measures were:

- Credit line from BB: (i) the creation in November 2008 of a credit line of R$5 billion (R$2.7 billion) for working capital to small and medium-sized enterprises (those with annual revenues of up to R$3.5 million

[20] ILO (2010).

(US$1.9 million)); (ii) the extension in June 2009 of this credit line to R$11.6 billion (US$5.8 billion). This credit line benefited around 303,000 SMEs.

- In August 2009 the Government made an additional contribution of R$500 million (US$251 million) to the endorsement funds of BB and BNDES, which guarantees loans to small and medium-sized enterprises. These funds allowed the state-owned banks to boost their credit operations, as they provide an extra guarantee against default.

Construction sector

Besides the launch of Minha Casa, Minha Vida and the change in the Special Tax Regime on Real Estate (RET), the credit lines to the construction sector were also expanded:

- On 29 October 2008 the CEF announced that it would provide a credit line for working capital of R$3 billion (US$1.6 billion) for construction companies.
- On 29 October 2008 the Government allowed Brazilian banks to direct 5 per cent of their savings deposits (earmarked for real estate financing) for working capital to builders. Banks were already required to apply 65 per cent of those deposits to real estate financing. Thus 5 per cent (about R$18 billion or US$10 billion) could be deducted from the total.
- On 11 November 2008 the CEF raised the ceiling of its credit line Construcard/FGTS, for the acquisition of construction material, from R$7,000 (US$3,804) to R$25,000 (US$13,587). This line uses resources of FGTS (Guarantee Fund for Time of Service) and has an interest rate of 6 to 8.16 per cent per annum, depending on the borrower's income range;.
- A real estate credit line was created for public servants (including staff of public enterprises and mixed public–private firms), as a means to stimulate construction.
- Real estate loans were made at below-market rates by BB and the CEF.

Agriculture

Beyond the Federal Government subsidies to agriculture integrated in the stimulus package and the Agriculture Plan "Safra" 2009/2010 (R$15 billion (US$8.3 billion)), the Government launched a set of initiatives to increase rural credit, which was implemented by two state-owned banks, BB and BNDES. The main initiatives were:

- an increase on 14 October 2008 from 25 to 30 per cent of the reserve requirement on demand deposits earmarked for rural credit (an R$4.8 billion (US$2.4 billion) increase in resources), and an increase from 65 to 70 per cent of the reserve requirement on rural savings deposits (an R$2.2 billion (US$1.1 billion) increase in resources);
- the announcement on 6 March 2009 by the National Monetary Council (Conselho Monetário Nacional, CMN) of the release of an additional R$12.3 billion (US$6.2 billion) in loans for agribusinesses by BNDES;
- the use of R$100 million (US$200 million) in resources from constitutional funds for rural credit and R$200 million (US$400 million) in assistance for agricultural cooperatives;
- the allocation of R$75 million (US$150 million) to family agriculture using resources from the Worker's Protection Fund (Fundo de Amparo ao Trabalhador, FAT).

Manufacturing

Some credit lines to the manufacturing sector were also provided, including:

- the programme Pro-Trucker of BNDES, launched in September 2009, that increased the finance period to 96 months and cut interest rates from 13.5 to 4.5 per cent. These operations would be guaranteed by the guarantee fund credit of BNDES;

- the approval in November 2009 by CODEFAT (Conselho Deliberativo do fundo de Amparo ao Trabalhador, FAT Deliberative Council) of the creation of a credit line for taxi drivers to buy new cars. The conditions included a five-year payment period; a ceiling of R$60,000 (US$30,151) on the loan, with funding of up to 90 per cent of the car; and an annual interest compounded by the long-term interest rate (currently 6 per cent per annum) plus 4 per cent. The credit line is operated by BB with resources coming from the FAT.

7 GREEN-RELATED INITIATIVES

It is important to recognize that promoting the consumption of automobiles and other carbon-emitting products (through reductions in IPI discussed above) have important environmental considerations and potential costs in terms of pollution. And, while not an initial focus of the stimulus package, by early 2009 the Government had opted to convert a number of the incentives that had been put in place to stimulate economic activity into green initiatives. As a result, a number of the fiscal policy measures had the effect of promoting the growth of green jobs while fostering environmentally sustainable development. Most of these measures were introduced early in 2009 and many have been made permanent. In particular, in March 2009 the Government extended the reduction in the IPI on cars, but only for flexible-fuel vehicles that can run on either ethanol or gasoline. Similarly, in the same month the Government limited the extension of the IPI on home appliances to energy-efficient appliances. Moreover, the cutback in the IPI on refrigerators also provided support to an existing programme through which low income people were able to trade old and ecologically inefficient refrigerators for new ones certified as ecologically efficient.

In addition, in December 2009 the Government reduced to zero the IPI on electricity generated by wind power. This measure, which has become permanent, is intended to promote the domestic production of windmills. The reduction in the IPI on machines and capital goods used in the recycling industry was also made permanent.

Green measures have also been integrated into housing programmes. As part of the federal housing programme Minha Casa, Minha Vida the Government adopted the use of solar-powered water heaters. In cooperation with the ILO the Government has developed a programme to train labourers in the installation and maintenance of these heaters. In a related move, loans for solar-powered water heaters, energy-efficient light bulbs, individual gauges of water and gas consumption, tree planting, and water-saving gadgets have also been included in the federal housing financing programme, thus boosting the acquisition of energy-saving devices in new homes.

D SOCIAL DIALOGUE TO SUPPORT THE CRISIS RESPONSE

Another key characteristic distinguishing this crisis from past crises in Brazil is the important role given to social dialogue. In 2003, the Presidency convened the Economic and Social Development Council (Conselho de Desenvolvimento Econômico e Social, CDES) to provide advice concerning long-term strategic policies for social and economic development. The CDES is a national, multipartite council with representation from government, employers, trade unions and civil society. While it has no legal authority per se, it contributes to the national policy debate and helps shape government intervention, for example regarding the PAC. And in the context of the crisis, the CDES created a special group in early October 2008 to (i) monitor the evolution of the financial crisis and its effects on the Brazilian economy; (ii) gauge the effectiveness of adopted countercyclical policies; and (iii) propose new measures.

Following its meeting on 14 October 2008, the CDES published a resolution suggesting several policy changes, namely:

- furthering the role of the Central Bank (BCB) in stabilizing currency exchange rates;
- expanding credit lines for the productive and commercial sectors through private and public banks;
- curbing the ascent of the general interest (policy) rate determined by the Central Bank (the SELIC index); and
- maintaining public investment rates, especially through the PAC programme.[21]

In January 2009 the CDES issued a Declaration stating that it was the moment for a "national understanding, involving all levels and spheres of government, employers, workers and civil society, to assure the continuity of a virtuous cycle of investment and growth with equity, environmental responsibility, employment generation and distribution of income, based on productive activities, on work and on solidarity".[22] Among others, the

[21] CDES (2008).
[22] CDES (2009).

agreed proposals included a reduction in interest rates to reduce the cost of credit, stimulating consumption and investment, defending employment and national production, and strengthening the internal market as a critical factor for growth and for the generation of employment and income.

In March 2009, the CDES also held a joint session with the Senate Committee designated to monitor the crisis. The recommendations – which are non-binding – were nevertheless eventually incorporated by the government into its crisis response package. Moreover, the CDES continues to act as an important forum for gathering information and gauging the various opinions of actors outside of the government, helping to forge policies that are more attuned to the needs of the real economy.

E POLICY LESSONS AND CONSIDERATIONS

The Brazilian response to the financial and economic crisis was multi-faceted; it covered monetary, credit and exchange-rate policies as well as micro-level policy interventions aimed at stimulating investment, production, spending and ultimately, job creation. Unlike past crises, the Brazilian Government entered the 2008/2009 crisis with favourable macroeconomic conditions that allowed it to finance its policy response using domestic resources, freeing the Government from the conditionalities typically attached to external financing. Though the Central Bank was slow to reduce interest rates, it acted quickly to increase liquidity in the interbank market and to expand the availability of credit through the three main public banks, the BNDES, the Banco do Brasil and the Caixa Econômica Federal.

The fiscal stimulus package, at 1.2 per cent of GDP, was small by international standards, yet effective. It included increased spending on infrastructure investment, through an increase in resources dedicated to the PAC and the launching of a new housing programme, Minha Casa, Minha Vida. It also included subsidies on BNDES loans to stimulate investment and job creation, and to the agricultural sector. Municipalities were not forced to cut spending, as their budgets were maintained via inter-government transfers, thereby avoiding pro-cyclical policies at the local level. And finally a number of automatic stabilizers were reinforced, notably the increase in the coverage and level of benefits of the Bolsa Familia CCT programme, and the extension of unemployment insurance benefits by two months for redundant workers employed in sectors most affected by the crisis. The multi-partite CDES was an important forum for social dialogue that consolidated disparate views on how best to respond to the crisis, acting as a unique advisory board for the Government.

In sum, one of the principal lessons of Brazil's response is that it leveraged effectively a number of complementary policy initiatives – both macro and micro – in a cost-effective manner. Moreover, as the following chapters will demonstrate, if properly designed the various sets of policy instruments can serve multiple objectives.

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CHAPTER 3
SUPPORTING EMPLOYMENT BY LEVERAGING KEY SECTORS

INTRODUCTION

The aim of Chapter 3 is to demonstrate how properly designed policies can be cost-effective to the public purse while supporting employment objectives and enterprise development. Brazil leveraged effectively a number of policy initiatives that required little or no outlays in expenditures but contributed significantly to stimulating industrial activity and employment creation. Indeed, the private sector in Brazil played a critical role in spurring economic activity and supporting job creation and stability over the course of the crisis. In particular, section A discusses a number of policy initiatives that provided support to employment-intensive sectors and business activities with high multipliers. Section B examines a range of measures to support employment creation, while the final section (section C) discusses a number of policy considerations.

A SUPPORT TO EMPLOYMENT-ORIENTED ACTIVITIES

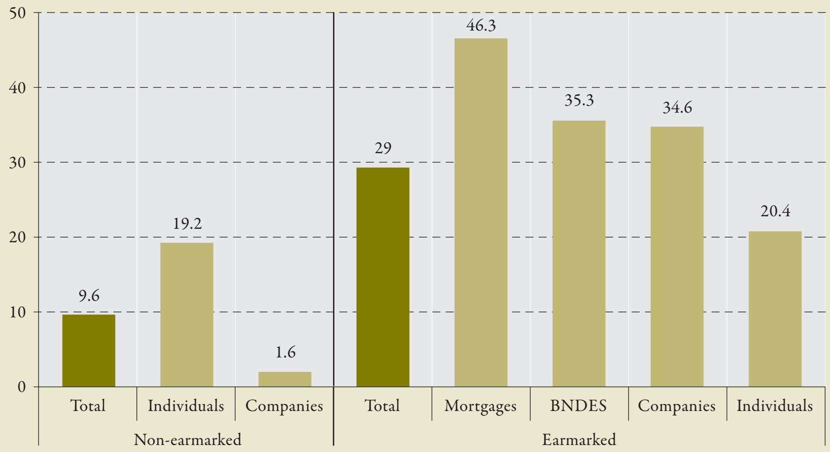
Credit supply to the real economy was made possible via strong public financial institutions...

Although Brazilian financial institutions were not exposed to financial instruments linked to the sub-prime mortgages in the U.S., Brazil was affected by the contagion effects of the global financial crisis through various transmission channels, as previously discussed. Amidst the high level of uncertainty (reinforced by the losses of various corporations in the derivatives market), the preference for liquidity by private financial institutions in the country became quite elevated. As a consequence, individuals, households and enterprises were faced with considerable credit constraints. However, public financial institutions responded counter-cyclically, expanding the availability of credit to the real economy.

Before the crisis Brazil already had a strong presence of state-run financial institutions, notably Banco Nacional de Desenvolvimento Econômico e Social (BNDES), Caixa Econômica Federal (CEF) and Banco do Brasil (BB) that accounted for over one-third of total loans. During the crisis their relative position was strengthened, as the public financial institutions were authorized to acquire ownership of private financial institutions and insurance companies (discussed in more detail in Chapter 2).

As a result, the Government acted quickly to restore liquidity to the inter-bank market, as well as increasing the supply of credit to the real economy through a series of new initiatives – principally through earmarked loans. Lending by public banks grew by 26 per cent in 2009, compared to an increase of only 5.8 per cent by private banks. As of December 2009 the share of total loans from public banks had risen to 39.4 per cent from less than 34 per cent in October 2008. The rise in lending was principally concentrated in transactions with earmarked resources (government funds for specific sectors), which grew by 29 per cent compared to 9.6 per cent for non-earmarked credit growth (Figure 3.1). Among earmarked funds,

Figure 3.1 **Domestic credit growth, 2009**
(percentages)



Source: Banco Central do Brasil.

growth was concentrated in mortgage lending (46.3 per cent growth) but also in lending to companies, driven by BNDES whose portfolio included lending to micro, small and medium-sized enterprises.

…with earmarked financing for SMEs…

On 6 November 2008 the Ministry of Finance announced a series of new initiatives that together provided R$19 billion (US$10 billion) in credit lines for various sectors via BNDES and BB. A significant part of the BNDES credit lines – amounting to R$2.4 billion (US$1.3 billion) in 2009 – were dedicated to micro and small and medium-sized enterprises (SMEs) through the credit line "Cartão BNDES".[23] In addition, in 2009 the BNDES also granted these enterprises R$9.1 billion (US$4.6 billion) to finance investments and R$31.3 billion (US$15.7 billion) for working capital – an increase of 32.3 per cent compared to a year earlier. The Government made an additional contribution of R$500 million (US$251 million) to the endorsement funds of BB and BNDES, which guarantee loans to SMEs.

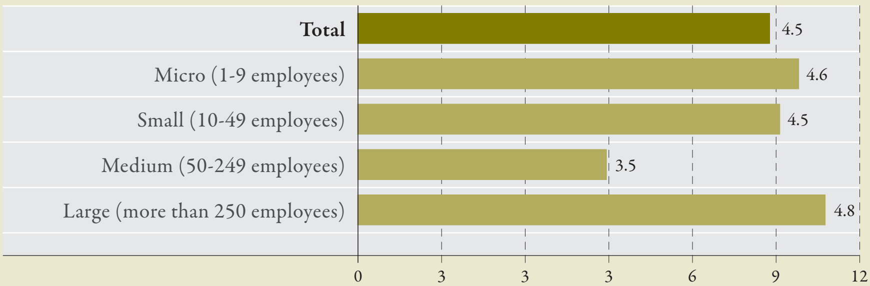
[23] These loans were limited to micro, small and medium-sized enterprises with maximum annual gross sales of R$90 million.

The new credit lines and the endorsement fund created by BB in response to the crisis (see Chapter 2) contributed to boosting the credit operations of micro, small and medium-sized companies. Ninety-three thousand operations came under the protection of this fund, which guaranteed up to 80 per cent of loans; the fund reached R$2.7 billion (US$1.4 billion) by the end of 2009.

This support to micro, small and medium-sized enterprises was an important consideration for employment creation. In 2008, micro and small enterprises alone constituted more than one-third of formal employment in the country.[24] During 2009, employment in micro and small enterprises grew by 4.5 and 4.6 per cent respectively, compared to only 3.5 per cent among medium-sized enterprises (Figure 3.2).

Job growth was also strong in large enterprises. Indeed, employment in firms with 250 or more employees grew by 4.8 per cent in 2009. Although special efforts were made to provide credit to SMEs, large firms also benefited substantially from government efforts to increase access to credit.

Figure 3.2 Change in formal employment by size of establishment, 2009
(percentages)



Sources: Ministry of Labour and Employment (MTE); Relação Anual de Informações Sociais (RAIS).

[24] If medium-sized enterprises are included, the share of formal employment rises to just over 55 per cent. The figures are based on Relação Anual de Informações Sociais (RAIS), an administrative database of formal employment that includes public-sector workers.

When direct and indirect credit allocation by BNDES is taken into consideration, larger firms benefited to a greater degree – their share of overall credit disbursements rose from 76 per cent in 2008 to 82.5 per cent in 2009, owing to the higher value of loans awarded to larger firms.[25]

Addressing the credit constraints clearly had important employment effects and ensured that viable enterprises remained in operation. In fact, according to the IMF, the intervention of public banks was estimated to add an additional 3 per cent to GDP in 2009 – more than through the fiscal stimulus.[26]

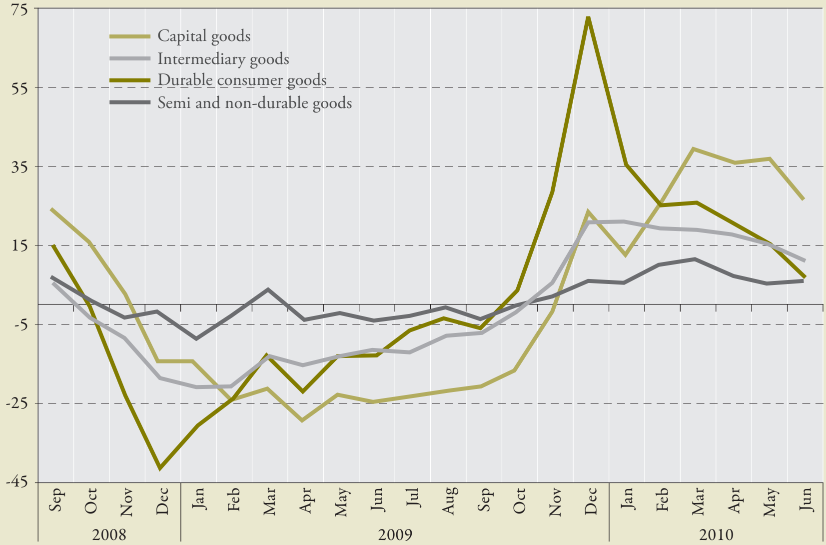
…and well-targeted tax cuts had important employment multiplier effects.

Industrial production in Brazil accounts for nearly one-quarter of gross national product. It also drives growth in a number of other areas owing to its highly diversified structure and its tight integration with various production supply chains. However, the crisis severely affected output and employment in the sector. In turn, the Government introduced a number of tax reductions and exemptions, notably for the purchase of motor vehicles. These reductions accounted for more than a third of the stimulus package, of which the largest component was changes to the IPI. As outlined in Chapter 2, in December 2008 the IPI was cut for motorcycles, trucks and automobiles from 7 to 0 per cent (for vehicles up to 1,000 cc) and from 13 to 6.5 per cent (for vehicles up to 2,000 cc). It is estimated that the reduction of the IPI tax on automobiles accounted for 13.4 per cent of car sales in the first half of 2009.

This stimulated activity and demand in other areas, both directly and indirectly. For example, given the forward and backward linkages with other industries, capital and intermediary goods production recovered strongly in the second half of 2009 (Figure 3.3). Durable consumer goods also benefited indirectly from the renewed industrial activity. In fact, IPEA estimates that each R$1.00 spent on cars has a multiplier effect of R$3.76 on output.[27] With an estimated 25 million jobs (direct and indirect) reliant on

[25] BNDES: see www.bndes.gov.br.
[26] IMF (2009).
[27] Bahia (2009); IPEA (2009).

Figure 3.3 Manufactured industrial production, change from the same month of the previous year, Q4 2008–Q2 2010 (percentages)



Source: Ministry of Labour and Employment (MTE).

car manufacturing, in the first half of 2009 the IPI cut is estimated to have contributed to maintaining between 50,000 and 60,000 direct and indirect jobs in the Brazilian economy. The rise in capital goods production was also stimulated by the recovery in infrastructure investment, which had positive impacts in the construction sector.

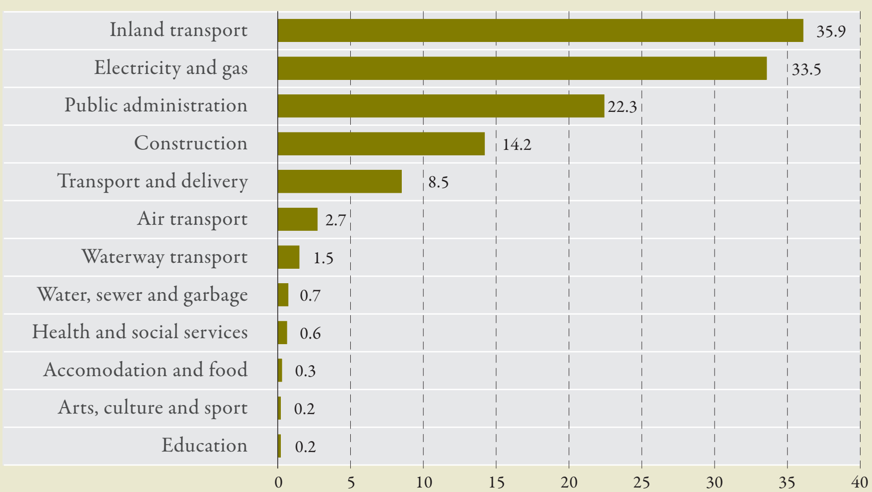
B MEASURES TO SPUR EMPLOYMENT CREATION

In addition to the measures discussed above, the Government also expanded the Growth Acceleration Programme (PAC) and introduced Minha Casa, Minha Vida. Together these programmes accounted for just over 40 per cent of the total stimulus package.

Expansion of the PAC boosted investment in employment-intensive sectors…

In magnitude, the PAC – although present prior to the onset of the crisis – was second only to the tax cuts implemented by Brazil. The programme aimed, among other things, to increase government investment in infrastructure, particularly transport networks and public utilities. Approximately 40 per cent of disbursements in 2009 financed investments in transport and one-third was directed towards electricity and gas (Figure 3.4). Importantly, the private sector plays a critical role in the PAC, related investments and disbursements. For example, of the more than 600 PAC projects announced for 2011–2014, approximately one-third include the involvement of Petrobas.

Figure 3.4 Change in PAC disbursements to each sector, 2009
(percentages)



Source: Banco Nacional de Desenvolvimento Econômico e Social (BNDES).

…especially in the construction sector via the introduction of Minha Casa, Minha Vida…

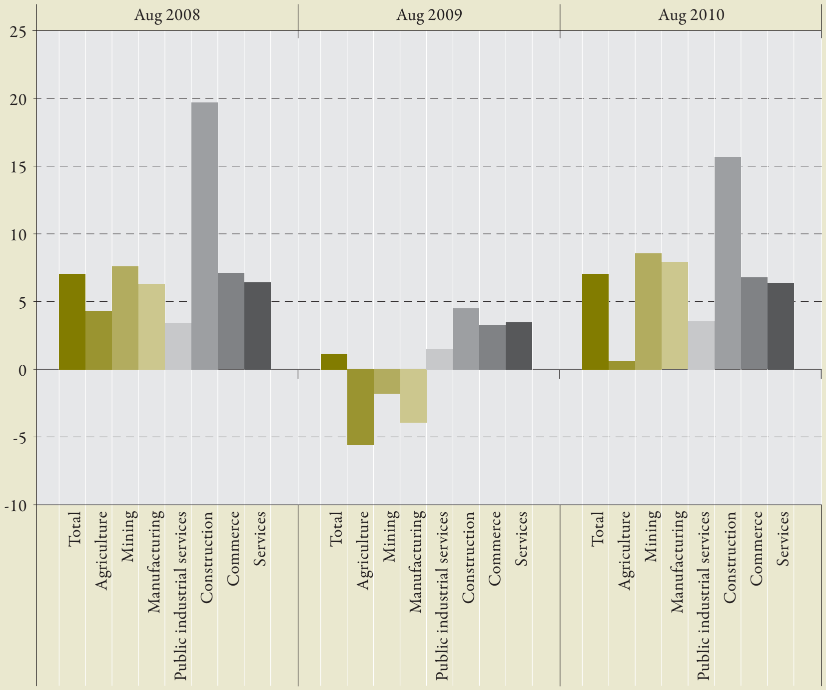
The Minha Casa, Minha Vida programme consisted of government incentives and subsidies for housing construction and accounted for more than 16 per cent of the total stimulus package. The programme – targeted at low- and middle-income households – aims to build one million new homes in 2009 and 2010. By September 2010, 630,886 housing units had been contracted, of which 160,883 had been delivered to their owners (25 per cent of the total). The benefit to lower-income households was two-fold. First, the programme built affordable houses for the poor, helping to reduce the existing housing deficit (57 per cent of the units were destined for families with monthly income of three to six times the minimum wage, while 70 per cent of the total contracts were signed in the south and southeast of Brazil).[28] Second, it helped – together with the PAC and the improved economic outlook –to spur employment creation in the construction sector. In fact, job growth in construction was relatively robust during the crisis (on a year-on-year basis), outpacing growth in all other employment sectors (Figure 3.5, panel A). Even as job growth in farming, manufacturing, and mining turned negative in August 2009 compared to the previous year, jobs in the construction sector grew by nearly 5 per cent. And in August 2010 over 15 per cent growth was recorded, far exceeding the growth realized in other sectors.

…with strength in domestic demand driving service-sector employment gains...

The service sector accounts for three-quarters of total employment in metropolitan areas and 72 per cent of formal employment. Throughout the crisis it acted as a buffer, softening the impact on the economy and on the domestic labour market. In fact, employment in the service sector – both public and private – sustained positive growth rates (with the exception of January 2009) throughout the crisis (see Figure 3.6).

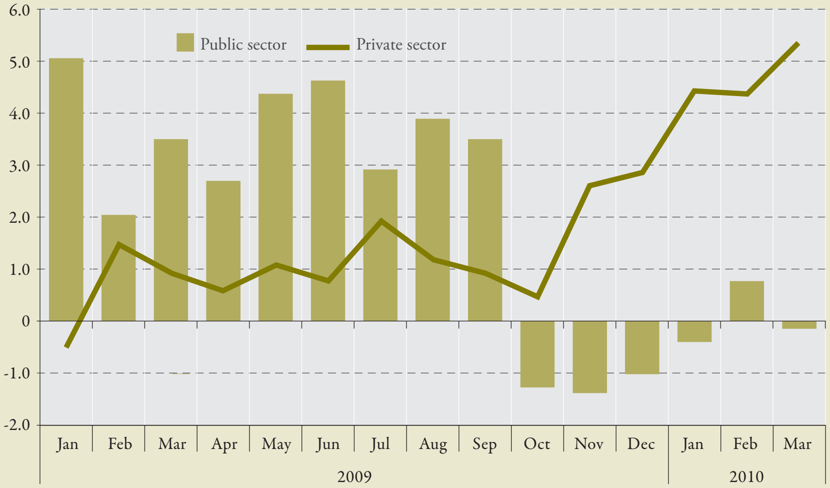
[28] Ministério das Cidades (Ministry of Cities). See http://www.cidades.gov.br.

Figure 3.5 Change in formal employment by sector, 2008–2010
(change from the same month of previous year, percentages)



Source: Ministry of Labour and Employment (MTE), CAGED database.

Figure 3.6 Service employment in the six major metropolitan areas, 2009–2010
(change from the same month of the previous year, percentages)



Note: Public-sector employment includes public administration, defence, social security, education, health and social services. Private-sector employment includes repair of motor vehicles, personal goods and appliances.

Source: Instituto Brasileiro de Geografia e Estatística (IBGE), Pesquisa Mensal de Emprego (PME).

The resilience of employment in the service sector is due largely to the countercyclical measures that sustained private consumption (which represents more than 60 per cent of Brazilian GDP).[29] In particular, the demand for non-durable goods such as food items, beverages and tobacco, which are employment-intensive sectors, maintained positive growth during the recession and gained momentum in the second quarter of 2009. The strong demand was due to improving the purchasing power of low-income individuals and households through improvements to the Bolsa Familia programme and the increases maintained in the minimum wage (see Chapter 4).[30] This helped sustain overall retail commerce activity, which is dominated by employment-rich SMEs. While these are welcome developments, it is important to take note – as discussed previously – the important role that household debt linked to over-consumption, often a result of income inequalities, has played in the onset of the current global crisis.

The service sector was also buoyed by job growth in the public sector which now accounts for nearly one-quarter of all service jobs: between December 2002 and April 2010 the number of federal employees grew by over 10 per cent and the sector benefited from strong wage growth.[31] Financial services, which represent 6.2 per cent of the services sector and 10.6 per cent of GDP, benefited from the countercyclical action of public banks as well as from the recovery of the São Paulo Stock Exchange (Bovespa) which rose 82.7 per cent in 2009 following the drop of 38.5 per cent in 2008.

…and investments to upgrade employment-intensive agriculture...

Although agriculture accounts for a relatively small share of Brazil's GDP (5.2 per cent in 2009), the sector accounts for 16 per cent of the country's labour force, making it a major employer in Brazil. Agricultural products also figure prominently among Brazil's US$150.2 billion of exports in 2009. Over half the export value is accounted for by commodities of which agriculture constitutes a significant share (US$35 billion).[32] The crisis and a sharp deterioration in global economic prospects in the third quarter of 2008 abruptly ended the commodity price boom of recent years.[33]

[29] Schettini et al. (2010).
[30] IPEA (2010a).
[31] During the period of the two administrations headed by President Lula, more than 127,430 employees were hired by the Brazilian Federal Government (a growth rate of 13.3%).
[32] FUNDAP (2010).
[33] IMF (2009).

The price reduction was sharp and rapid: in the second half of 2008 the Commodity Research Bureau (CRB) index fell 160.9 per cent and the foodstuffs sub-index fell 166.6 per cent. As for soybean (the second largest Brazilian export product, which accounts for 16.4 per cent of total exports), the price dropped 160 per cent.

The declining external demand and drop in commodity prices hit the agricultural sector hard. In response, the Government put in place initiatives to bolster the agricultural sector, the main one being the Plan Safra 2009/2010 that granted R$107.5 billion (US$59.4 billion) to 4.1 million rural units, of which R$15 billion (US$8.3 billion) was dedicated to family farmers. This represented an increase of 37 per cent compared to the amount of R$78.2 billion (US$43.3 billion) invested in the former Plan Safra which ran from 2007 to 2008. The resources were devoted to four major objectives: (i) increasing credit to finance costs; (ii) creating a credit line for the purchase of tractors and vehicles by family farmers; (iii) diversifying agricultural activities covered by the plan; and (iv)strengthening the insurance granted by the programme against crop shortfall and price declines.[34]

The rebound in commodity prices since the beginning of 2009 and the set of initiatives launched by the Government to assist the agriculture sector (through cost reductions and increased rural credit) helped the sector recover. Some of the initiatives provided much-needed support to the family-run farms which provide 70 per cent of the food consumed by Brazilian households and 10 per cent of Brazil's GDP. The sector is also, of course, the main source of livelihood for rural families.[35]

...coupled with attempts – although limited in scope – to mitigate dismissals via collective bargaining.

One of the more well-known and successful experiences in Brazil to retain employment during a period of crisis occurred in the early 1990s in the ABC region of São Paulo. The metalworking industry of that region had been negatively affected by the liberalization of trade and the difficult mac-

[34] Ministério do Desenvolvimento Agrário (Ministry of Agricultural Development), see http://www.mda.gov.br/portal/.
[35] IPEA (2010b).

roeconomic environment. The then-president of the metalworkers' union proposed the formation of a chamber to find solutions to the crisis. The Government promised reductions of taxes on automobiles and parts and the employers agreed to retain employment in the sector, resulting in the retention of approximately 100,000 workers. The experience of the sectoral chamber was later followed by the creation of a Regional Chamber of the Greater ABC region that worked during the mid-1990s to promote regional development through infrastructure renewal and redefinition of commodity chains, including more attention given to small and medium-sized businesses, training of dismissed workers and attraction of new investments.[36]

In 1998 the Bolsa Qualificação (Training Scholarship) programme was developed that granted leave from jobs for a period of two to five months to participate in a training course, during which participants receive unemployment benefits. Employers are not required to pay salaries or make payroll contributions during this period. When the training course is complete, participants return to their place of work. They are guaranteed employment for three months upon return to the workplace, but after this time can be dismissed; the unemployment benefit period is then reduced by the months that the worker participated in the training course (although there is a minimum guarantee of one month of benefits). In 2008 only 7,700 workers participated in this programme, but during the crisis the number of participants in 2009 jumped to over 20 thousand. The Bolsa Qualificação must be negotiated through collective agreement or accord.

Other measures – not requiring government support – to retain workers include collective holidays and reductions of working hours coupled with reductions in pay. A number of firms in the industrial sector negotiated collective holidays, though these were typically short in duration. Another policy, used particularly in the metalworking sector, was a negotiated reduction in working hours in exchange for reduced pay, usually stretching over a period of several months. These agreements typically resulted in reductions of around 10 per cent of salary, though in some instances it rose to 25 per cent. The agreements were often coupled with guarantees for retain-

[36] Leite (2003).

ing employees for a specific number of months. In the industrial pole of Manaus, the state government entered into an agreement with employers and unions to retain workers in exchange for tax reductions. According to the Labour Secretariat of the State of Manaus, the agreement avoided the dismissal of at least 30,000 workers.[37]

Generally, however, during the crisis of 2009 firms did not enter into negotiated retention schemes, even though many firms viewed the programmes as potentially effective. Indeed, a survey by the Federação das Indústrias do Estado de São Paulo (Industrial Federation of the State of São Paulo, FIESP) of 586 companies (55 of which had 500 or more employees) during the period February–March 2009 found that 47 per cent of firms had dismissed workers in response to the crisis, equivalent to 19 per cent of their labour force on average. At the time of the survey, nearly 40 per cent planned further dismissals, representing about 14 per cent of their labour force. The survey asked employers whether they thought the following policies could be useful in avoiding dismissals: broad agreement on hour banks, collective holidays, reduction of working time with reduction in pay, and use of the Bolsa Qualificação.[38] It is interesting to note that with the exception of collective holidays, in over 50 per cent of the cases the other three policies have the potential of avoiding some or all dismissals (Table 3.1).

Table 3.1 Opinion on whether the following policies could contribute to avoiding dismissals, 586 industrial firms from the State of São Paulo, February–March 2008

Policies	WOULD AVOID ALL DISMISSALS	WOULD PARTIALLY AVOID DISMISSALS	WOULD NOT AVOID DISMISSALS	TOTAL
Broad agreement on bank of hours	19	43	39	**100**
Collective holidays	9	35	56	**100**
Reduction of working time with reduction in pay	27	52	22	**100**
Use of Bolsa Qualificação	22	37	41	**100**

Note: Row totals may not add due to rounding.
Source: Federação das Indústrias do Estado de São Paulo (FIESP) (2009).

[37] Caldas (2009).
[38] FIESP (2009).

Given the short-term nature of the crisis, policies such as work-sharing – whereby workers accept to work reduced hours with the government compensating part of the wage reduction in some cases – could have been leveraged to greater effect in lessening the number of dismissals and the economic and social impact of unemployment (see Chapter 5 for further discussion of the use of work-sharing in Germany). As it stood, there was a net loss of 212 thousand manufacturing jobs between November 2008 and March 2009 in the State of São Paulo; wider use of these policies could have helped to lessen this number. Moreover, if reduced working hours had been accompanied by government compensation for the reduction in pay incurred by workers, it might have enhanced the acceptability of this practice among trade unions. Alternatively, the employers could have been offered tax incentives to retain employment, as was done in the industrial pole of the Amazon region. A more proactive stance by the Government to support employee retention policies, accompanied by financial incentives and more active social dialogue, could contribute to their usefulness in future downturns, helping to mitigate the negative effects on employment.

C POLICY LESSONS AND CONSIDERATIONS

This chapter has shown how employment in a number of key sectors was supported through a variety of well-designed and targeted policies – which complemented an already dynamic private sector. In the first instance it leveraged a number of key initiatives that required little direct expenditure outlays. In particular, soon after the first impacts of the crisis became evident, the Government of Brazil took swift action to restore the flow of credit; this provided much-needed support to viable, employment-intensive sectors, notably SMEs. In addition, it enacted a series of tax cuts – but these were focused principally on industrial products with large multiplier effects. As a result, when vehicle sales were given a boost because of these tax reductions, economic activity and jobs in other areas were stimulated due to the forward and backward linkages with the automotive industry. In this regard, the private sector also played a key role in reinvigorating economic activity and supporting employment during the crisis.

To complement these measures, the Government allocated resources for the expansion of the Growth Acceleration Programme and the creation of the Minha Casa, Minha Vida programme. These initiatives provided direct support and helped boost employment creation in key sectors of the Brazilian economy, particularly construction. The growth in domestic demand – supported by a range of countercyclical measures – and a strong public sector helped sustain job growth in services. In addition, agriculture activity – a sector which accounts for only a small share of Brazil's GDP but which employs a relatively larger share of the country's labour force – was bolstered through the Plan Safra by addressing credit constraints, enhancing diversification and strengthening insurance against price declines, with special attention given to family farms. And while there were some attempts to limit dismissals through a range of pre-existing programmes, they were limited in scope and could be leveraged to greater use in the future.

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CHAPTER 4
STIMULATING AGGREGATE DEMAND THROUGH SOCIAL PROTECTION[39]

INTRODUCTION

Social protection and social transfers serve many functions including fulfilling human rights and contributing to economic growth.[40,41] With respect to the latter, by providing adequate income support social protection can help individuals smooth consumption over the life-cycle, especially during downturns such as the current financial and economic crisis that started in 2008. In particular, programmes such as unemployment assistance and other forms of cash transfer can provide much-needed income replacement, and if combined with active support can facilitate job mobility and matching. Moreover, if properly designed, social protection measures can also help to spur aggregate demand and facilitate human capital formation for long-term growth.

This chapter looks at the income transfer policies and social protection measures in Brazil which helped cushion the impacts of the global economic and financial crisis of 2008. Indeed, in the midst of the crisis, Brazil took permanent steps towards deepening the coverage and effectiveness of social protection schemes and social assistance programmes. Chapter 2 documented a number of policies relating to social protection measures that were enacted as part of Brazil's crisis response, including (i) extending protection and support to unemployed workers; (ii) expanding the conditional cash transfer (CCT) programme Bolsa Familia; and (iii) maintaining the scheduled increase in the minimum wage in spite the crisis. A number of related measures were also introduced, such as providing financing for housing, protection of migrant workers and ratification of the ILO Social Security (Minimum Standards)Convention, 1952 (No. 102).

[39] The authors would like to acknowledge excellent research assistance by Yelena Reznikova.
[40] Social protection includes any social insurance or social assistance schemes that protect people from certain economic shocks or risks. The data drawn on for this chapter does not include general education spending, provision of medical goods and services or untargeted labour market programmes.
[41] See for example Townsend (2009).

It is important to note that social protection and income transfer programmes such as the CCT programme were well established in Brazil before the onset of the crisis. The initial starting conditions thus played a significant role in facilitating a response to the crisis by enabling the Government to ramp up or modify existing programmes, which in turn acted as automatic stabilizers. The first part of this chapter (section A) gives a broad overview of social protection in Brazil and its role in society. Section B examines in more detail the various policy initiatives undertaken in support of the crisis, while section C concludes with policy considerations.

A SOCIAL PROTECTION IN BRAZIL

Social transfers can have a positive impact on reducing poverty and income inequality. Moreover, with a strong social protection system in place, support for individuals and households is automatically scaled up as the impacts of a crisis take hold. This is in fact the role and purpose of automatic stabilizers –to provide stabilization (income support, active measures, and so on) when it is needed most. In this respect, automatic stabilizers are often easier and more efficient to implement than discretionary measures, which can be challenging to roll out appropriately and may often only become effective after a certain time lag.

Social policy has been a key component of the development of the welfare system in Brazil, which is organized under three principal pillars: (i) universal provision of education and health; (ii) social assistance (including social pensions) for the poor and for rural households; and (iii) contributory social security schemes and provision by the private sector.[42]

Social spending in Brazil, especially in the area of social protection, is comparably high...

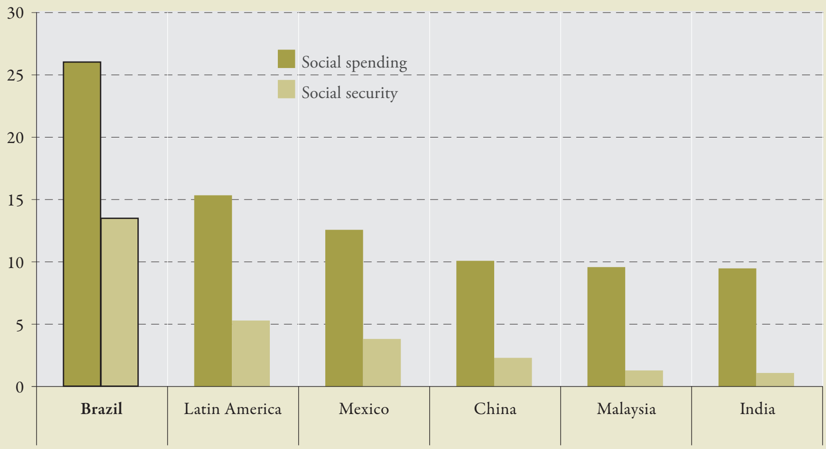
Social spending, which includes central government expenditures on education, health, social protection and housing is comparably high in Brazil (Figure 4.1). As of 2008, total social spending in Brazil amounted to approximately 26 per cent of GDP, compared to only 15 per cent, on average, in other Latin American countries. In other large emerging economies such China and India – although GDP per capita is comparably lower – social spending is less than 10 per cent of GDP. Other emerging economies at comparable phases of development also spend significantly less on social measures than Brazil does; for example, Mexico and Malaysia allocate 12 and 9.4 per cent of GDP to social spending, respectively. The largest component of social spending in Brazil is social security, which includes social assistance, pensions, unemployment insurance and training; these account

[42] See Draibe (2007) and Barrientos (2003).

for over half of all social spending and explain the gap with the other Latin American countries (spending on education accounts for 5.5 per cent, health 4.9 per cent and housing 2.1 per cent).[43] Indeed, while expenditures as a share of GDP are similar for education, health and housing in other Latin American countries, spending on social security, at 13.4 per cent of GDP in 2008, is more than double in Brazil.

Social security expenditure in Brazil has been rising constantly for over a decade – from around 11 per cent of GDP on average in the late 1990s to over 12 per cent of GDP on average between 2000 and 2008 (Figure 4.2). As a result, Brazil's social security expenditures are higher than most other developing countries and approach the average of OECD countries where spending has remained relatively stable over the past decade. Interestingly, Lindert (2004) points out that for a given age and income-level distribution, Latin America is spending more on social security than did Europe at a similar point in development.

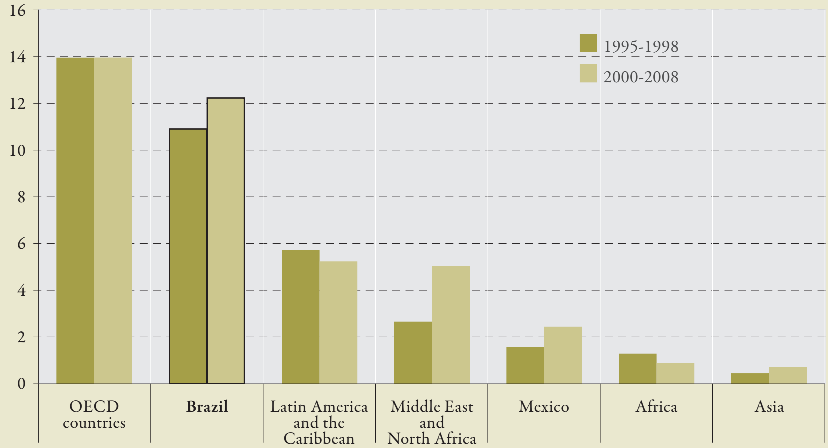
Figure 4.1 Social security and social spending, Brazil and other selected countries, 2008
(percentage of GDP)



Note: Social spending regroups spending in social security, education, health, and housing. Latin American countries include Argentina, Bolivia, Chile, Colombia, Costa Rica, Cuba, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Panama, Paraguay, Peru, Dominican Republic, Trinidad and Tobago, Uruguay and the Bolivarian Republic of Venezuela.
Sources: Economic Commission for Latin America & the Caribbean (ECLAC), CEPALSTAT (2010); Asian Development Bank (ADB), *Key Indicators 2010* for China, Malaysia and India; Health spending for China and India from WHO, *World Health Statistics 2010*.

[43] See ECLAC: CEPALSTAT, at http://www.eclac.org/estadisticas.

Figure 4.2 Trends in spending on social security by region, 1995–1998 and 2000–2008
(percentage of GDP)



Note: IILS estimates are based on IMF, *Government Finance Statistics* (2010) and IMF, Global Development Network Growth Database; GDP from World Bank (2008); OECDStat for OECD countries; ADB, *Key Indicators* for Asian countries; and ECLAC.

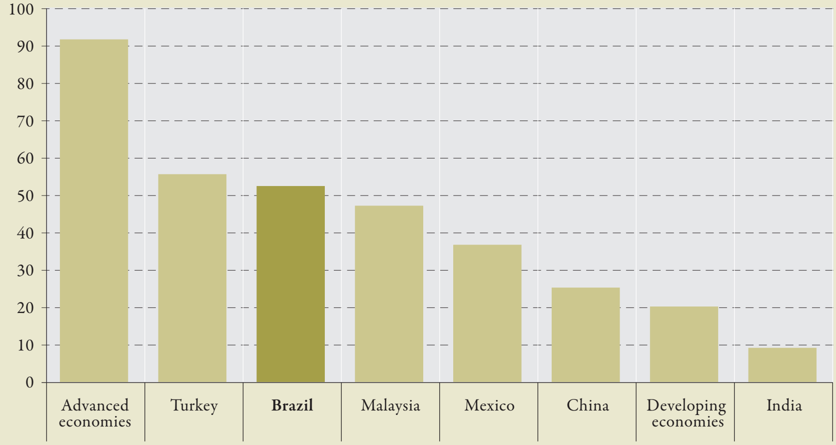
Source: Economic Commission for Latin America & the Caribbean (ECLAC) (2010).

...including a comprehensive pension scheme and social assistance programme for retirees.

Pension schemes – which constitute over 90 per cent of total social security expenditures – play an important role in Brazil's overall welfare system (see Box 4.1). As a result, pension coverage is relatively high with over 50 per cent of the labour force covered (Figure 4.3). In major emerging economies such as China, India and Mexico, the rate is well below 50 per cent and for developing economies it is only 20 per cent (the figure is over 90 per cent for advanced economies).

The comprehensiveness of the social protection system lies in two important factors. First, while the system was originally designed to cater to workers with a formal labour contract, the social pension scheme has been reformed to include self-employed and domestic workers, substantially increasing the coverage. The second is due to the existence of two important programmes that provide benefits to the elderly poor – the rural pension (Fundo de Assistência ao Trabalhador Rural) and the Continued Benefit Provision (Beneficio de Prestação Continuada, BPC):

Figure 4.3 **Pension coverage in selected countries and regions**
(percentage of labour force)



Source: World Bank (2010).

- Rural pension: To be eligible, rural workers need only provide evidence of 15 years of rural activity.[44] The bulk of the scheme is financed by the State (tax financed), though a tax of 2.1 per cent tax on agricultural products is designed to cover some cost. The programme has expanded significantly since the early 1990s. The number of beneficiaries has doubled in the past two decades rising from 4.1 million in 1992 to 8.2 million in the first half of 2010 (Ministry of Social Security, (MPS)).[45] It is estimated that for 2010, spending will total R$50 billion (US$28 billion, 1.6 per cent of GDP).

- Continued Benefit Provision (BPC): Although not strictly part of the pension system, the BPC is a social assistance programme that provides benefits equivalent to the monthly minimum wage either to persons aged 65 or older, or to persons of any age who are unable to work due to disability, with per capita household income less than one-fourth of the minimum wage (the extreme poverty line). In 2009, 1.54 million elderly and 1.63 million disabled households received benefits through the BPC. Total spending amounted to R$16.9 billion (US$8.5 billion), equivalent to 0.05 per cent of GDP. The average benefit in 2009 was

[44] Rural agriculture workers who migrate to urban areas and contribute to the pension system via their urban job can, upon demonstrating proof of agricultural work, have their time working in agriculture credited toward their pension.
[45] Ministério da Previdência Social (MPS): http://www.previdenciasocial.gov.br.

R$444 (US$223) per month (due to the increase in the minimum wage from R$415 (US$209) to R$465 (US$234) in February 2009).

These programmes have helped to provide much-needed income support to individuals and households during the crisis. There are also a number of key labour market and social policies, notably the unemployment insurance scheme, the Bolsa Familia programme and minimum wage practices, that have played a critical role in Brazil's response to the crisis.

Box 4.1 Brazil's retirement income system

The Brazilian pension system is now divided into three regimes. The first is the General Regime of Social Security (Regime Geral de Previdência Social, RGPS), which is a public and mandatory scheme for all private-sector workers, including domestic and self-employed workers. The second is the Pension Regime for Government Workers (Regimes Próprios de Previdência Social, RPPS) where public-sector employees are covered under specific pension provision. The last scheme is the Complementary Pension Regime (Regime de Previdência Complementar, RPC). In addition to these three regimes, there are non-contributory social pensions to provide poverty relief to the elderly (see table).

Main characteristics of the pension system in Brazil

Scheme	Contribution rate	Qualifying conditions	Level of benefit
RGPS	**Employees:** 8 per cent of minimum wage up to 11 per cent of the ceiling. **Employers:** 20 per cent of covered payroll plus an additional rate based on the firm's record of workers' injuries. **Self-employed:** 11 per cent of declared covered earnings. Special rules for rural workers and arduous work.	**Contributory pension:** 35 years (men) or 30 years (women). For arduous work, between 15 and 25 years. **Age pension:** Age 65 (men) or age 60 (women) for employees and the urban self-employed, age 60 (men) or age 55 (women) for rural workers. At least 168 or 180 months of contributions depending on first insured period.	**Contributory pension:** 80 per cent of the insured's average earnings. **Age pension:** 70 per cent of the insured's average earnings plus 1 per cent of average earnings for each year of contributions, up to 100 per cent. The minimum monthly age pension is equal to the legal minimum wage.
RPPS	11 per cent of entire wages without ceiling.	Same as urban employees in RGPS.	80 per cent of highest monthly wage.
RPC	Defined-contribution, private voluntary	Variable	Defined-benefit
Social assistance	Non-contributory	Either older than 65 or disabled with average household income lower than 25 per cent of the minimum wage.	Same amount as the minimum wage. Eligibility is reviewed every two years.

Source: ISSA (2010); M. Caetano (2009); J. Savoia (2007)

B RESPONDING TO THE CRISIS AND IMPACT OF POLICIES ON RECOVERY

During times of crisis and economic downturn, social protection measures can help support aggregate demand and spur recovery through a number of channels. First, measures to help individuals and families maintain their income, including those who have lost their job, will protect and smooth consumption against shocks. Such measures can mitigate the impact on aggregate demand and can serve to avert unnecessary short-term strategies with long-term adverse consequences – such as taking children out of school. Second, if properly designed, income support measures can also have significant positive effects on the incidence of poverty – which is often exacerbated during downturns and can adversely affect long-term growth as it is often difficult to reverse. Third, such measures, which are targeted directly to job losers, i.e. via unemployment assistance or benefit programmes, can facilitate the transition between unemployment and employment. Moreover, if combined with active support such as job-search assistance or training, they can have positive effects on job-search with potential long-term benefits in human capital acquisition.

As noted in Chapter 2, Brazil's fiscal stimulus package amounted to around 1.2 per cent of its GDP, of which only a small fraction was devoted to social protection measures. However, this masks the role that some of the existing programmes have played in supporting individuals and households. In fact, the strength of the existing social protection scheme has provided much-needed income support – with positive ancillary effects on aggregate demand and overall confidence – throughout the crisis period and beyond. A number of key programmes were strengthened as part of the stimulus package introduced during the crisis; in particular, the Government (i) extended unemployment insurance; (ii) expanded the Bolsa Familia CCT programme; and (iii) maintained an increase in the real minimum wage. This section discusses these measures and examines their impacts.

Brazil is also one of the few Latin American countries with an unemployment insurance scheme in place...

The most immediate impact of a downturn is often felt by those who lose their job. In the first instance, support is provided through unemployment insurance to maintain (and replace) a certain level of income until workers can be reemployed. In periods of crisis, unemployment income-support programmes play a crucial role in protecting and empowering people and serving as a macroeconomic stabilizer.[46]

In Latin America, Brazil is one of the few countries (there are six in total) to have an unemployment insurance programme (Box 4.2). The scheme is based on five different groups: formal workers (the largest group), small-scale fishermen, domestic workers (the smallest group), rescued workers (from forced labour) and workers in the Bolsa Qualificação (Training Scholarship) programme (see Chapter 3).

Although foreseen under the Constitution of 1946, the unemployment insurance system was not introduced in Brazil until 1986. However, it was not until 1990 that the Government set up a specific source of funds and more accessible criteria for granting benefits, based on the establishment of the Worker's Protection Fund (FAT). The FAT funded an unemployment insurance programme designed to link financial aid and the pursuit of employment by means of labour market intermediation services, professional training programmes, and investments. The Fund is managed by a tripartite council (CODEFAT or FAT Deliberative Council) composed of representatives of government, workers' organizations and employers' organizations, whose aim is to define, finance, approve, and monitor the Fund's work plans. The FAT finances not only unemployment insurance but also several labour intermediation and professional training programmes, together with a number of other programmes, for example a wage subsidy for low-income workers (Abono Salarial). In addition, 40 per cent of FAT

[46] Scholz et al. (2010).

Box 4.2 Brazil's unemployment insurance programme, 2010

The details of Brazil's unemployment insurance, based on the year 2010, are as follows:

- **Coverage:** limited to waged workers. Domestic employees with a signed labour contract are eligible if their employer has registered them in the FGTS.
- **Source of financing:** managed by the FAT, which is financed via a business sales tax of 0.65 per cent.
- **Qualifying conditions:** recipients must have been employed for at least six months in some stipulated period of recent employment. Unemployment must not be due to misconduct or resignation.
- **Level of benefit:** depends on the average earnings of the previous three months of employment. In general, the formula for calculation of the benefit is as follows: 80 per cent of average benefit is paid based on the average earnings, up to R$841.88. The minimum monthly benefit is equal to the legal monthly minimum wage (R$510), and the maximum monthly benefit is R$954.21.*
- **Benefit duration:** three to five months, depending on the length of employment (six to 11 months, 12 to 23 months, or 24 months or more of employment). Under special conditions, the benefit may be extended for an additional two months.

* Benefits are adjusted annually according to changes in the minimum wage. The minimum wage for 2010 is R$510.

Source: www.mte.gov.br/seg_desemp/beneficio.asp#; ISSA (2010); Y. Zhang et al. (2010); M. Vodopivec (2009).

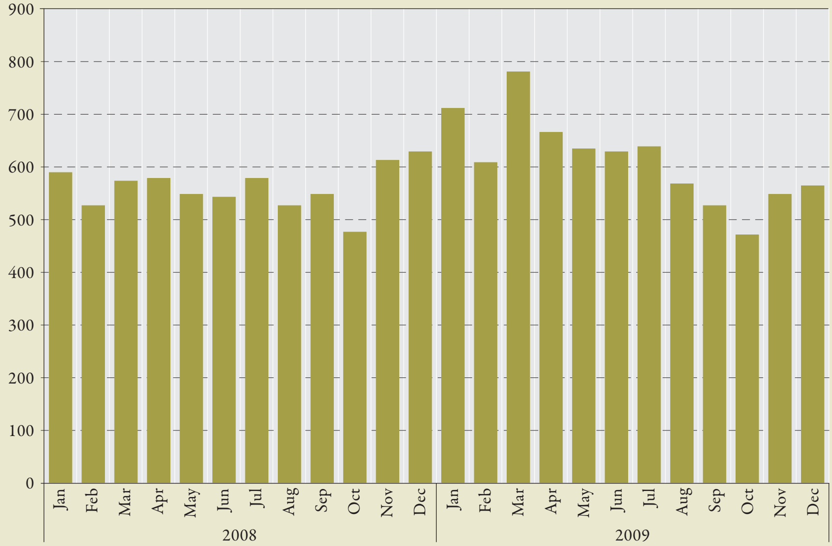
funds are loaned to the National Social and Economic Development Bank (BNDES) to support the financing of new investment projects, with the aim of stimulating job creation and thus reducing the need for unemployment insurance.

... and benefits were extended to workers most hit by the crisis.

As a result of the crisis, the Ministry of Labour extended the duration of unemployment insurance by two months for workers whose sector of economic activity was severely affected by the recession. On 24 March 2009 the extension was granted to workers who were laid off in November and December 2008. And in May 2009, the extension was further granted to workers who were laid off in January 2009 and February 2009. This measure was as a result of the social dialogue between the government, enterprises and labour unions. The extended duration was thus granted to the bulk of job losers, as these months – as illustrated in Chapter 1 – constituted a significant share of employment losses. As a result, unemployment insurance claims among formal workers rose from a low of nearly 477,193 in October 2008 to a peak of 780,125 in March 2009 (Figure 4.4). As the labour market recovered, the total number of unemployment insurance beneficiaries declined throughout 2009 to below 500,000 in November 2009 as the unemployment rate fell and the two-month extension expired.

This expanded duration and eligibility constituted a significant response to the crisis. With average monthly benefits ranging from R$465 (US$204) to R$870 (US$383) and the number of recipients nearly doubling, spending on unemployment benefits rose dramatically – in fact, it increased by nearly 50 per cent from R$14 billion (US$7.6 billion) in 2008 to over R$20 billion (US$11 billion) in 2010.

Figure 4.4 Unemployment insurance beneficiaries, 2008–2009
(thousands)



Source: Ministry of Labour and Employment (MTE).

The conditional cash transfer programme Bolsa Familia provides support to low-income households...

Cash transfers provide non-contributory payments in the form of cash to the poor or to those who risk falling into poverty. Programmes of this nature are generally state-run and often form part of the Government's broader social safety net. They are often conditional – known as "conditional cash transfers" (CCTs) – and thus the disbursements are subject to certain conditions linked to, for example, education, health or nutrition.[47] The most common conditions are children's attendance at school, health-care check-ups and the provision of nutritional needs. The objective of these programmes is to increase real household income and thus guarantee to recipients a minimum level of consumption with the aim of reducing poverty and hunger and improving social development, by means of a direct income transfer to poor and extremely poor families. They also aim to break the cycle of intergenerational poverty by improving the well-being and skills of children so they can overcome the social and economic barriers faced by their parents. CCTs started in Brazil in the federal district and a few municipalities, and in Mexico in the mid-1990s (focusing on school attendance and health care) and have since been widely adopted in other countries, especially in Latin America and often in response to a crisis.[48] Recent studies show that a third of developing countries have implemented some kind of cash transfer programme.[49]

The main features of Bolsa Familia, present in all of Brazil's 5,564 municipalities, are: decentralization (management is shared between the Federal Government, states and municipalities); assistance to the whole family, not to any of its members separately; conditionalities fulfilled by the families and the Government in the areas of health, education and social assistance; direct payment to the family, without any intermediary; use of the banking network for payment; and freedom of the family to make consumption choices.

[47] Conditionality is often difficult to enforce and administer.
[48] Similar initiatives have been adopted in Argentina, Chile, Colombia, Dominican Republic, Ecuador, Honduras and Jamaica, as well as in other parts of the world such as Bangladesh, Burkina Faso, Cambodia, Ethiopia, Lesotho, Pakistan and Turkey.
[49] Lustig (2008).

With respect to the conditionalities, the programme requires maintaining school-age children in school, having children vaccinated and, for women who are pregnant or breast-feeding, accepting pre-natal and post-natal care. In 2009, around 90 per cent of the beneficiaries were females and 30 per cent were single mothers. The programme has thus been important for empowering women by strengthening their positions in the household, thereby increasing their influence within the family and raising their self-esteem.[50]

The value of the benefit varies according to the number of children in the family, including teenagers up to 17 years old and pregnant women, and could be between R$20–184 per month (equivalent to US$12–111). The monthly benefits paid are calculated at approximately R$20 (US$11) per child up to 15 years old, while for pregnant women and teenagers (16–17 years old) the benefit is approximately R$30 (US$17) per month. Families can enrol a maximum of three children up to age 15 and two children aged 16 and 17 in the programme. An additional monthly benefit equivalent to approximately R$60 (US$33) per month is available to extremely poor households – those with per capita monthly income below R$65 (US$33) – regardless of family composition.

... and Brazil acted quickly to expand eligibility and improve benefits under the programme...

In early 2009, in an effort to mitigate the effects of the economic crisis, the Brazilian Government reiterated its commitment to the Bolsa Familia programme and announced an expansion that comprised two main measures: (i) an update of the poverty and extreme poverty lines and of the benefit value; and (ii) an expansion of the coverage of the programme. The cost of these measures was estimated at R$410 million (US$206 million), or approximately 0.014 per cent of GDP, bringing the total cost to R$11.8

[50] Suarez and Libardoni (2007).

billion (US$5.9 billion) or 0.4 per cent of GDP in 2009. The expansion took place in three principal stages:

- Stage 1: inclusion of 300,000 families in May 2009; expansion in large municipalities with smaller coverage under the programme and a high number of registered families within the Bolsa Familia profile;
- Stage 2: inclusion of 500,000 families in August 2009; expansion in municipalities with a high number of registered families within the Bolsa Familia profile and a greater number of updated registers;
- Stage 3: inclusion of 500,000 families in October 2009; expansion in other municipalities with smaller coverage.

It is worth mentioning that these measures – albeit planned before the onset of the crisis in September 2008 – were implemented more quickly than previously planned, in an effort to expand the social safety net during the crisis. In 2008, as a result of an increase in food prices, the Brazilian Government had decided to update the poverty and extreme poverty lines to reflect increases in the National Consumer Price Index (Índice Nacional de Preços ao Consumidor, INPC). Thus, in 2009 the poverty line was updated from R$119 (US$60) to R$135 (US$68) and the extreme poverty line from R$59.70 (US$30.00) to R$68.70 (US$34.50). As a result, the eligibility for benefits was increased from a monthly income of R$120 (US$60) to R$140 (US$70) and benefits were increased by close to 10 per cent, with the average benefit reaching R$95 (US$48) per month. This was done in order to take into account inflation and the higher cost of living in the country.

The extended eligibility helped 1.4 million additional families to benefit from the programme. As a result, the number of household beneficiaries rose significantly from 11 million in 2008 to 12.4 million in 2009 and it is estimated that 14 million people will be reached by the end of 2010. Consequently, the number of individuals receiving support from Bolsa Familia is around 50 million, or 25 per cent of Brazil's population. The

Table 4.1 Regional distribution of beneficiary families and of the poor, February 2009
(percentages)

Regions	Distribution of beneficiary families in February 2009	Distribution of the poor
North	10.2	9.9
Northeast	51.2	47.0
Southeast	25.2	27.4
South	8.3	9.7
Midwest	5.2	6.0

Source: Ministry of Social Development (MDS).

extension of Bolsa Familia also provided an important source of support to households in poorer rural areas. Most of the poor (75 per cent) are found in the northeast and southeast regions, and this is reflected in the regional distribution of Bolsa Familia beneficiaries, as shown in Table 4.1.

... which had important social and economic benefits.

A number of studies illustrate that the Bolsa Familia programme has produced immediate and significant improvements in the living conditions of the poor population:[51]

- Given that low-income households have a high propensity to consume, a large portion of the money is spent on goods and basic necessities. An IPEA study states that the income multiplier is greatest when public transfers are directed to low-income families: for example, an increase of 1 per cent of GDP in Bolsa Familia results in a positive change of 1.44 per cent in GDP and of 2.25 per cent in household income, while the same increase in interest payment raises GDP by only 0.71 per cent and household income by 1.34 per cent.[52] Bolsa Familia enhances the dynamism of local economies since the money is spent on domestic products that are sold in the local markets. As a result, it generates demand for domestic goods and services, which in many instances favours the small and micro-enterprises important in rural areas. The programme thus plays an important role in boosting job creation.[53]

[51] See Soares et al. (2007); ILO (2010a); ILO (2010b); ILO Note on Crisis.
[52] IPEA (forthcoming).
[53] Cardoso (2007).

- Food and nutritional security are improved – families eat better and more frequently, and child malnutrition has declined since the receipt of money is conditional on health check-ups;
- Poverty and income inequality are reduced – 21 per cent of the Gini decrease between 2003 and 2006 is attributed to the Bolsa Familia programme. The regularity of the benefit allows families to plan their budget better; it is also estimated that extreme poverty is reduced by 16 per cent through the various social assistance programmes.[54]
- There is some empirical evidence that demonstrates the programme does not create a disincentive towards work.[55]

The minimum wage in Brazil is an important benchmark for labour market and social policy...

The Brazilian minimum wage defines the level of remuneration for formal wage employment in both the private and the public sectors and serves as a benchmark for a number of social security policies, including pensions, disability and unemployment benefits. The minimum wage is also used to measure poverty lines. It also influences informal worker earnings as employees and employers often negotiate wages using the minimum wage as a benchmark (the so-called lighthouse effect).[56] According to data from the 2008 National Household Survey (PNAD), 12 per cent of Brazilian workers earned the minimum wage. Among private-sector formal waged employees and informal workers, 16 per cent earned the minimum wage in 2008 (Table 4.2).

In terms of distributional consequences, the minimum wage in Brazil has important implications for a number of disadvantaged groups. In 2008, for example, 13.8 per cent of women earned the minimum wage, compared with only 5.9 per cent of men. For domestic workers – almost 95 per cent of whom are women – the minimum wage was the reference value for close to half of registered workers (i.e. formal workers with a registered employment contract) and for around 5 per cent of unregistered workers.

[54] Lindert et al. (2007).
[55] Ministry of Social Security (Ministério da Previdência Social, MPS) (2009).
[56] Neri and Moura (2006).

Table 4.2 Workers earning the minimum wage, by occupational category and gender, 2008 (percentages)

	Women	Men	Total
Public servants	12.3	3.4	10.6
Formal waged employees	18.7	8.8	15.5
Informal waged employees	19.1	9.5	16.1
Domestic workers with a signed labour contract	47.6	3.7	46.4
Domestic workers without a signed labour contract	14.6	1.5	15.3
Total employed	13.8	5.9	11.8

Note: Total employed includes military personnel, self-employed, employers and unremunerated workers. When the survey was undertaken in September 2008, the minimum wage was R$415.

Source: ILO Country Office for Brazil based on National Household Survey (PNAD) of the Instituto Brasileiro de Geografia e Estatística (IBGE).

The level of minimum wages – if properly set so as not to discourage hiring or informality – can have particular importance during an economic crisis since they can serve as a social floor for wage adjustments and also as a tool to fight against wage deflation.[57] At the same time, minimum wage increases can act as a fiscal stimulus, by boosting consumer spending.[58] This is particularly relevant in the case of Brazil given that a number of benefits are linked to increases in the minimum wage.

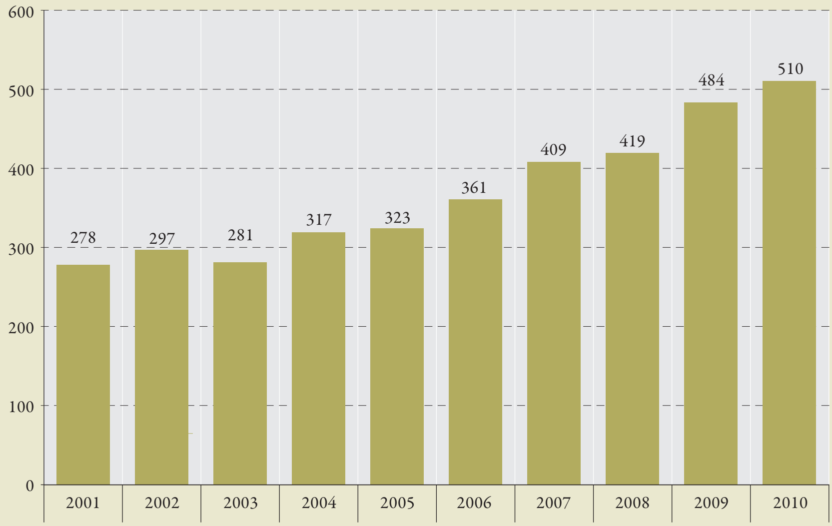
... and during the crisis, the Government maintained scheduled increases in the minimum wage.

In 2006 the Brazilian Government, following consultation with representatives from workers' and employers' organizations as well as representatives of retirees, set out the terms of yearly minimum wage increases through 2011. In February 2009 the scheduled 12 per cent nominal increase from R$415 (US$209) to R$465 (US$234) (or 6 per cent real increase), took effect, and in January 2010 the minimum wage was further increased by 9.7 per cent (5.7 per cent in real terms) to R$510 (US$256) per month (Figure 4.5). This 2009 increase resulted in a significant boost to the economy, injecting R$21 billion (US$42 billion), equivalent to 0.7 per cent of GDP.

[57] H. Herr (2008).

[58] A recent study by the Federal Reserve Bank of Chicago showed that minimum wage increases boost consumer spending substantially after a hike, even more than tax cuts: Aaronson, Agarwal and French (2008).

Figure 4.5 Real value of the minimum wage, 2001–2010
(R$, February 2010)



Note: Measured in R$ as of February 2010 for the City of São Paolo.
Source: Departamento Intersindical de Estadísticas y Estudios Socioeconómicos (DIEESE), 2010.

The decision to maintain the scheduled increases in the monthly minimum wage in February 2009 and again in January 2010 had a number of important consequences. First, it increased the incomes of wage-earners at the bottom of the pay scale – close to 12 per cent of formal wage workers earn the minimum wage. Second, increases in the minimum wage help support overall household income given that it is tied to a number of social protection schemes. In particular, benefit amounts of the RGPS (General Regime of Social Security), BPC (Continued Benefit Provision – a social assistance programme for elderly and disabled poor), and unemployment insurance are tied to the minimum wage.[59] The February 2009 increase alone injected an additional R$12.3 billion (US$6.2 billion) in 2009; overall, it is estimated that some 20 per cent of the population benefited from the increase.

[59] Pensioners who receive benefits that are above the minimum wage also benefited from the increase, although at a lower rate. See Jaccoud (2009a).

The programmes which are tied to the minimum wage also have important multiplier effects:

- IPEA estimates that each additional R$1 spent on the RGPS has a multiplier effect of 2.1 on family income and of 1.2 on GDP.
- The BPC programme has a multiplier effect of 2.2 on family income and 1.4 on GDP.[60]
- It is estimated that 22.5 million people, equivalent to 12.3 per cent of the population, were taken out of poverty as a result of the increase in pensions and BPC benefits.[61]

In addition, preliminary research from IPEA shows that stimulus on GDP of the increase in spending on the social cash transfers (Bolsa Família, BPC, and the RGPS) were important for creating employment during 2009. The multipliers on output of the three streams of social transfers are estimated to have led to an injection of US$ 30 billion into the economy. Under the assumption that employment growth is linear to growth in output, the increase in spending in RGPS, BPF and BPC potentially created (or saved) 1.3 million jobs.[62]

[60] Analysis based on the 2006 Social Accounting Matrix (IPEA, 2010).

[61] The poverty line is defined as the per capita household income below half the value of the minimum wage, which in 2008 was R$415. Analysis based on information from the 2008 PNAD household survey of the Secretariat of Social Welfare Policies of the Ministry of Social Security (Ministério da Previdência Social, MPS).

[62] Mostafa, J., forthcoming.

C POLICY LESSONS AND CONSIDERATIONS

A number of key lessons emerge from Brazil's capacity to mitigate the effects of the crisis through social protection measures. First, at the onset of the crisis there were already a number of key social protection initiatives in place that could be easily be scaled up. In particular, Brazil reiterated its commitment to the Bolsa Familia programme by extending eligibility and improving benefits during the crisis. It also extended the duration of unemployment benefits for the bulk of formal job losers and maintained planned increases in the minimum wage with ancillary benefits to a number of other social protection schemes.

Second, such programmes are designed to address the needs of those most vulnerable to downturns. Programmes of this nature aid in the recovery process by providing an efficient mechanism for transfer payments and mitigating the social impact on those most in need by providing income support to cash-constrained households. In the case of Brazil these schemes have helped address longer-term issues, such as poverty reduction (e.g. through pensions) or development (e.g. through school attendance via Bolsa Familia).

Finally, these programmes have been found to have important multiplier effects on overall economic activity and employment creation. Indeed, preliminary estimates from IPEA illustrates that spending on social transfers for the 3 key social programmes, i.e. Bolsa Família, BPC, and the RGPS created (or saved) 1.3 million jobs in 2009. Moreover, the design of these programmes is often consistent with labour market and economic objectives. For example, Bolsa Familia is found to improve the economic dynamism of local economies by increasing demand for local products and services given the high marginal propensity to consume among lower income households. Similarly, the BPC is estimated to have a multiplier effect of 2.2 on family income and 1.4 on GDP (similar to Bolsa Familia).

In sum, the experience of Brazil illustrates that well-designed social policies and programmes can serve to meet important social objectives such as poverty reduction while having important spillover effects on economic growth and job creation. Moreover, programmes of this nature need not be expensive to be effective.

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CHAPTER 5
LESSONS LEARNED AND REMAINING CHALLENGES

INTRODUCTION

As of late 2010, many countries continued to struggle with the consequences of the global financial and economic crisis. In a number of countries, such as the United States, job growth has not yet returned in a sustainable manner. In other countries, there are concerns about the quality of jobs being created and the extent of structural changes in the labour market.[63] Brazil, on the other hand, by early 2010 had already attained or surpassed pre-crisis highs in both growth and employment. The approach taken by Brazil also effectively addressed the acute challenges faced by the most vulnerable groups. In this respect, Brazil's experience offers a number of valuable lessons, notably how labour market and social policies – if well designed – can support an economic recovery. And alternately, how macroeconomic policies can lead to an inclusive and job-rich growth. In addition, the time is now ripe, given that the recovery in Brazil is well under way and growth in 2010 exceeded 7 per cent, to examine in closer detail a number of underlying challenges for the country.

With that in mind, section A highlights a number of potential lessons that other countries could draw on. It also examines any deficiencies or areas for improvement that could be considered within the context of Brazil's response to the crisis. Section B discusses a number of persistent challenges confronting Brazil, while section C assesses key areas for improvement.

[63] See for example ILO (2010a).

A LESSONS LEARNED

Brazil's success in handling and mitigating the crisis stems from a number of factors. First, following the currency crisis of 1999, Brazil was well-placed to address future external shocks. In this respect, the pre-crisis experience and starting conditions were important elements. Following the 1999 crisis, Brazil adopted a new macroeconomic regime that was characterized by inflation targeting, a floating (dirty) exchange-rate policy and the pursuit of primary surplus. Fiscal conservatism coupled with a commodity boom led to an overall strengthening of the macroeconomic fundamentals, in particular a build-up of external reserves and a sizeable primary surplus in the country's fiscal accounts. During the 1990s, the country also adopted a number of reforms that strengthened the financial sector, making it less vulnerable to crises of this nature.

As a result, the improved position permitted the country to take action to address the origins of the crisis, notably the credit crunch and stimulate domestic demand in employment-intensive sectors and provide support to the already dynamic private sector. At the same time, prior to the onset of the current crisis, Brazil had introduced and expanded a number of social protection schemes that, with the improved fiscal position, could be bolstered in support of the most vulnerable groups. However, many countries – both advanced and developing – introduced countercyclical policies to varying degrees. What sets Brazil apart, however, is that the design of policies has taken into consideration the mutually-reinforcing benefits of various courses of actions.

Brazil was able to effectively address the origins of the crisis in short order by maximizing the employment benefits of macroeconomic policy…

Although not directly affected by the mortgage-backed security crisis in the United States, the Government introduced several monetary and exchange-rate policies to improve liquidity through interest rate reductions (five in total) and a series of initiatives to alleviate short-terms pressures on the exchange rate. In addition, to increase the flow of credit to individuals, business and households the government also enacted a series of measures, but the approach was more targeted in nature. A number of tax reductions were also introduced to stimulate domestic demand. With respect to both sets of initiatives, macroeconomic policies were leveraged to maximize microeconomic benefits, notably job creation (Box 5.1).

Box 5.1 Maximizing microeconomic benefits of macroeconomic policy

Under the new macroeconomic regime over the past decade, Brazil managed to accumulate external reserves and a sizeable primary surplus that the country was able to leverage in order to restore liquidity to the market and the real economy. The improved fiscal position also meant there was room to enact a series of tax cuts.

The success of these initiatives lies in the fact that the measures, notably the tax reductions and targeted credit to SMEs, were concentrated in areas with large spillover effects on job creation.

Credit expansion – addressing the origins of the crisis: The public banks, Banco de Brasil and Caixa Econômica Federal, were given the authority to seek ownership interest in private and public financial institutions to improve the supply of credit, especially to the inter-bank market. In addition, the public development bank, BNDES, was capitalized with funds from the Treasury and the long-term interest rate on BNDES loans was subsidized. The existence and strength of the public banking system provided the Government with an exceptional tool for countering the private contraction of credit.

SMEs – credit lines to job-rich enterprises: Special measures were introduced to boost the credit operations of micro, small and medium-sized companies. The support to micro enterprise and SMEs was important for employment creation, given that micro and small enterprises constitute more than a third of formal employment. During 2009 employment in micro and small enterprises grew by 4.5 and 4.6 per cent respectively, compared to only 3.5 per cent among medium-sized enterprises.

Tax cuts focused on highly integrated sectors: The largest component of the tax reductions – which accounted for over one-third of the stimulus package – was the reduction in the tax on industrial products. In particular, in December 2008 the industrial production tax (IPI) was cut for motorcycles, trucks and automobiles to 0 per cent from 7 per cent (for vehicles up to 1,000cc) and to 6.5 per cent from 13 per cent (for vehicles up to 2,000 cc). These cuts had important multiplier effects. First, the reduction of the IPI tax on automobiles accounted for 13.4 per cent of car sales in the first half of 2009. Second, the increase in vehicles sales stimulated economic activity and jobs in other areas due to the forward and backward linkages with the automotive industry – an estimated 25 million jobs, direct and indirect, are reliant on car manufacturing. In fact, IPEA estimates that each R$1.00 spent on cars has a multiplier effect of R$3.76 on output.

…and targeted support to employment-intensive sectors to stimulate job creation…

A number of initiatives were undertaken to support employment creation more directly. In particular, the Growth Acceleration Programme (PAC) and Minha Casa, Minha Vida programme supported job growth in the construction industry, which had been hit by the crisis. In this regard, the private sector played a fundamental role in helping the economy recover and providing much needed support to job creation and maintenance. In addition, measures were adopted to support rural family farmers (Box 5.2).

While recognizing that the reductions to promote sale, production and use of automobiles and similar goods through the IPI cuts comes with some trade-offs in terms of the environment, the Brazilian fiscal stimulus package also included a number of measures to promote the growth of green jobs while fostering environmentally sustainable development. For example, in March 2009 the Government extended the reduction in the IPI on cars but restricted it to flexible-fuel vehicles that can run on either ethanol or gasoline. In addition, as part of Minha Casa, Minha Vida, the Government adopted the use of solar-power water heaters and developed – in cooperation with the ILO – a training programme to support their installation and maintenance.

…and well-designed social protection measures that provided support to the most vulnerable while reinforcing economic objectives.

Over the past decade, Brazil has developed a comprehensive social protection system that, with the onset of the crisis, could be enhanced and expanded. In particular, the Government (i) expanded the conditional cash transfer programme Bolsa Familia; (ii) extended protection and support of unemployed workers; and (iii) maintained the scheduled increase in the minimum wage. All three programmes have design features that are characteristic of effective, mutually-reinforcing policy levers (Box 5.3).

Box 5.2 Direct support to employment

Employment-intensive infrastructure: Two important measures were adopted as part of the stimulus package that constituted over 40 per cent of total stimulus spending. First, the Growth Acceleration Programme (PAC) was expanded, with around 75 per cent of the disbursements benefiting construction projects in the areas of transport and public utilities. Second, the Minha Casa, Minha Vida programme, unveiled in response to the crisis, aimed at building one million new homes in 2009 and 2010. As a result, the two initiatives boosted the construction sector: in August 2010, employment in the construction sector grew by over 15 per cent (compared to August 2009), far exceeding the growth realized in other sectors.

Support to rural farming – representing 16 per cent of the labour force: To bolster activity in the agricultural sector, the Government announced the Plan Safra 2009/2010 that granted R$107.5 billion (US$59.4 billion) to 4.1 million rural units, among which R$15 billion (US$8.3 billion) was allocated to family farms. The aim of the funding was to address credit constraints, enhance diversification and strengthen insurance against price declines.

Box 5.3 Well-designed social protection measures

Targeted: Programmes that are targeted to address specific needs or challenges – as opposed to certain groups – are more likely to be successful in meeting their objectives.

- *Bolsa Familia*: benefits were targeted to poor households with children and extremely poor households – those with per capita monthly income below R$65 (US$33) – regardless of family composition.
- *Unemployment insurance*: benefits were extended by two months during the current crisis but only for severely affected workers, such as such those active in mining and steelmaking (see also section B of this chapter).
- *Minimum wage*: the prevailing minimum wage serves as a benchmark for a number of social security policies, including pensions, disability and unemployment benefits as well as the poverty line.

Conditionality: In many cases, mutual obligations act as motivators for benefit recipients and can lead to better outcomes and improvements in the desired effect.

- *Bolsa Familia*: recipients must comply with a number of requirements in the area of education and health, e.g. ensuring that school-age children remain in school and are vaccinated.
- *Unemployment insurance*: Recipients must have been employed for at least six months and job loss must not be due to misconduct or resignation.

Box 5.3 Well-designed social protection measures

Regular updating in line with market incomes: Ensuring that benefits are updated in a systematic manner, and consistent with prevailing wage and income developments, increases their relevance and effectiveness.

- *Bolsa Familia*: eligibility criteria are a function of the poverty and extreme poverty lines with regular updating to reflect increases in inflation and higher costs of living.
- *Unemployment insurance*: 80 per cent of the average benefit is paid based on the average earnings up to a maximum (R$ 954), with the minimum monthly benefit equal to the monthly minimum wage.
- *Minimum wage*: Scheduled annual increases with the previous two increases in the minimum wage (February 2009 and January 2010) represented a real increase (above inflation) of 6 per cent and 5.7 per cent, respectively. The newly elected Government has reiterated its commitment to raising the minimum wage again in January 2011.

Non-distortionary in terms of work incentives: Social protection measures must be aligned with work incentives – when appropriately designed, social protection measures and work incentives can have mutually reinforcing benefits rather than working at cross-purposes.

- *Bolsa Familia*: some empirical evidence that suggests it does not create a disincentive towards work.
- *Unemployment insurance*: benefits are of a limited duration (3-5 months) and therefore unlikely to distort the work–leisure function.
- *Minimum wage*: There is no evidence that the presence of a minimum wage (or increases to it) have a negative effect on employment.

Consistent with economic objectives: If properly designed, social protection measures can not only support individuals but they can have multiplier effects throughout the broader economy.

- *Bolsa Familia*: While the programme seeks to reduce poverty and hunger and improve social development, it has been found to have important positive effects on income growth and business activity:
  - Income multiplier is greatest when public transfers are directed to low-income families ;
  - Spending by recipients enhances the dynamism of local economies since the money is spent on domestic products that are sold in the local markets. As such, the programme plays an important role in boosting job creation and enterprise (SME) development.
- *Unemployment insurance*: benefits can help individuals avoid steep declines in well-being, maintain contact with the formal labour market and improve job matching, all of which can contribute to productivity gains in the long run.
- *Minimum wage*: The case of Brazil demonstrates that minimum wage increases can have important positive effects on aggregate demand. They can also – if properly set – help reduce the incidence of informality which in turn can positively affect competitiveness.

Social dialogue is at the heart of good policy design.

The engagement of social partners, and more generally tripartism, played a critical role in the context of the crisis. To begin, the decision in 2006 that laid out the terms for minimum wage increases during 2007–2011 was the result of consultation with the social partners. In addition, the extension of unemployment insurance to workers most hit by the crisis was also a by product of tripartite engagement. Social dialogue also resulted in a programme that offered temporarily laid-off workers the possibility of receiving unemployment insurance while undergoing training courses. Indeed, there is increasing recognition in Brazil of the importance of social dialogue in shaping the policy debate. For example, since 2003 the Economic and Social Development Council (CDES) – a multipartite council – exists with the aim of providing advice on longer-term strategic objectives regarding social and economic development. The Council members, at the discretion of the President of the Republic, has representation from Government, employers, trade unions and civil society and has made insightful recommendations to the Government regarding crisis mitigation strategies and post-crisis policies.

Together, these initiatives have helped to mitigate the consequences of those most affected by crisis. But, importantly, these programmes have also been shown to spur local economic dynamism while contributing to the longer-term development of Brazil in the areas of environmental sustainability, education, health, nutrition and enhanced labour productivity.

B CHALLENGES AHEAD AND AREAS FOR IMPROVEMENT

More attention should be given to the role of labour market policies…

By most metrics, Brazil response to the crisis was a success – one which was built partially on previous experiences. In this respect, the current crisis offers an opportunity for Brazil to learn from its policy practices. The impact – though short-lived – was borne principally by the labour market through job losses; moving forward, the Government should consider devoting more attention and resources to existing labour market policies (Box 5.4).

The Global Jobs Pact calls on countries to help jobseekers through well-targeted active labour market policies including increasing resources, improving the effectiveness of public employment services and investing in skills upgrading through training. The Pact also recommends limiting or avoiding job losses through practices such as extending unemployment benefits or work-sharing.[64] In fact, according to The Global Economic Linkages (GEL) model – a theoretical macroeconomic model of a closed economy designed to analyze the impact of policy shocks on a range of economic variables – well designed public investments in the area of labour market policies, e.g. unemployment insurance, employment retention, labour market intermediation or public employment services has important positive effects on output, employment and wages (Figure 5.1, panels A, B and C). In fact, public spending in the form active labour market policies has a positive fiscal multiplier of 0.31 on impact and 0.43 after a year. The effect is principally achieved through improved labour market efficiency, e.g. investments in public employment services and training improve labour market intermediation and improve the match between demand and supply of labour. In addition, the multiplier effects is larger when spending takes place in period of under-employment of resources – the improved economic outlook as a result of job creation also leads to higher wages and employment which reinforces growth prospects. This is especially in contrast to the baseline scenario and although such an intervention requires expenditure outlays in the short-term, the model demonstrates that debt

[64] ILO (2009a).

Box 5.4 **A snapshot of labour market policies in Brazil**

Public employment services: The Brazilian Public Employment Service (Sistema Nacional de Emprego, SINE), was created in 1975 to provide guidance to unemployed workers, improve information on the labour market, and aid in the design and development of labour market policies. The sharp increase in unemployment in the 1990s led to the creation of additional training and certification programmes and an increase in the number of branches. The number of workers registered at SINE has surpassed five million annually since 2002.

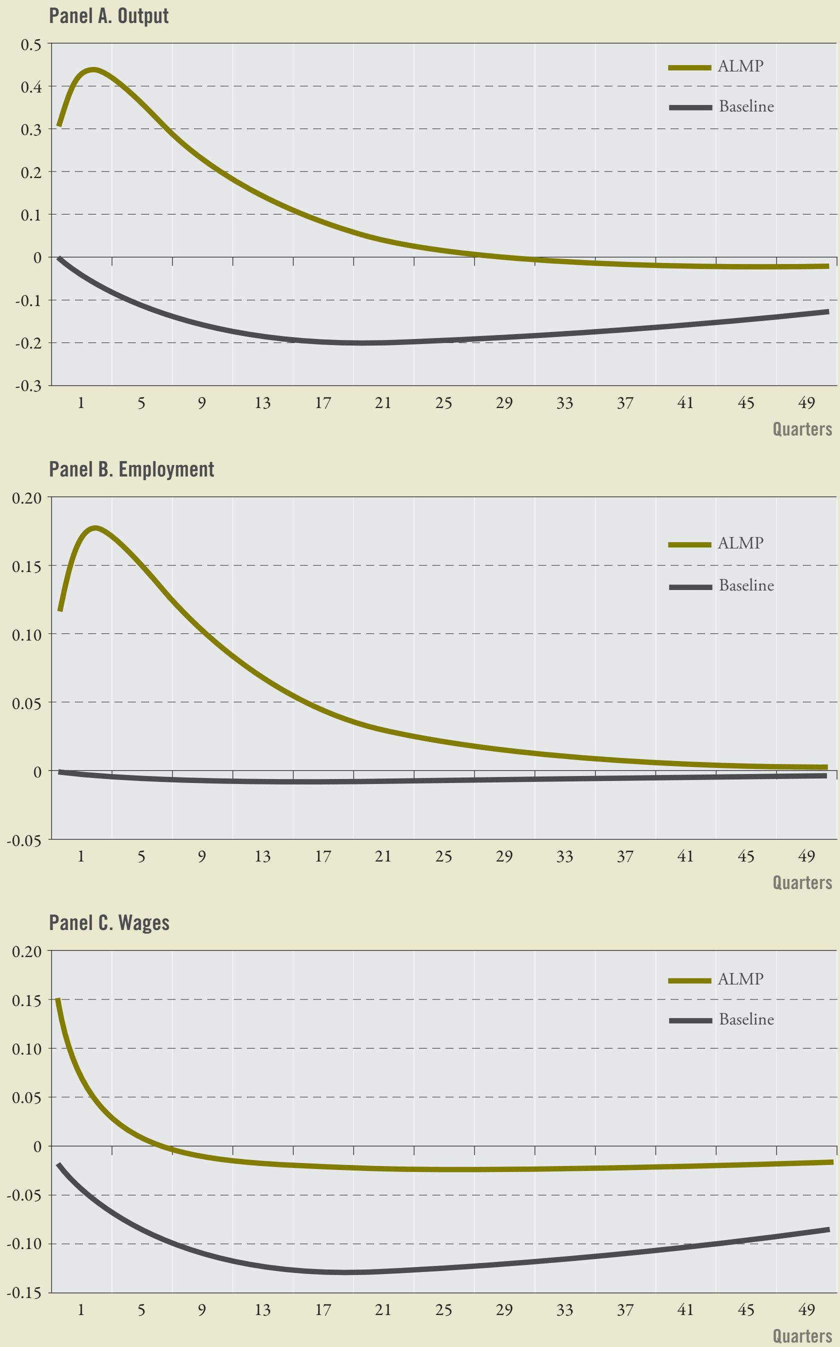
Training programmes: The 1995 the National Plan for Training and Vocational Qualification (Plano Nacional de Formação e Qualificação, PLANFOR) sought to increase labour productivity and set the goal of training 20 per cent of the country's economically active population. The programme was implemented through state governments and social entities without the involvement of SINE. Eleven million workers were trained between 1990 and 2001; however, many courses did not meet programme guidelines. In 2003, PLANFOR was replaced by the National Professional Qualification Plan (National Professional Training Plan (Plano Nacional de Qualificação Profissional, PNQ), which established specific pedagogic content and increased the hours of training.

Microcredit programmes: The Programa de Geração de Emprego e Renda Rural (Programme for the Creation of Employment and Income, PROGER) was established in 1994 for the purpose of extending credit to microenterprises, small enterprises, cooperatives, and production initiatives in the informal sector. The goal was to generate employment and income by making loans available to entities that otherwise would have little access to credit. Credit is offered through various public financial institutions. The programme initially focused on urban workers in metropolitan regions with the highest unemployment levels. In 1995 credit was also made available in the rural sector, first through the Rural PROGER and later through the National Programme to Strengthen Family Agriculture (known as PRONAF). In 2008, nearly 1.8 million loans were offered through PROGER with an average credit of R$9,500.

Source: ILO Country Office for Brazil.

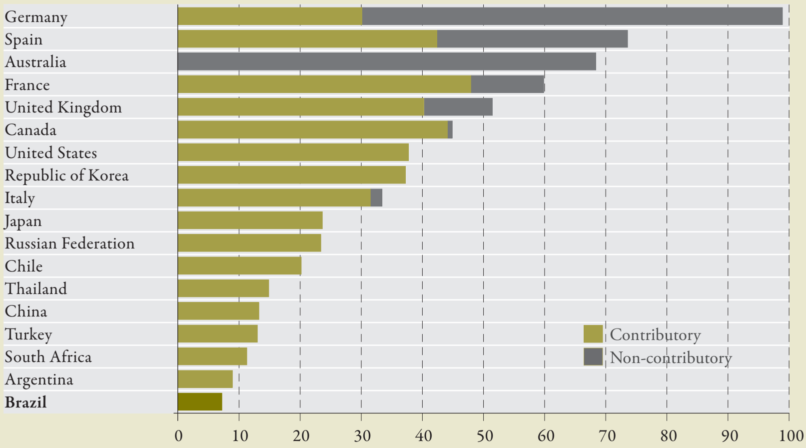
levels recover to similar values as the baseline scenario over the medium term. Indeed, over time the fiscal position improves due to overall improvement in employment and wages (improved tax base and fewer expenditures on benefits, e.g. unemployment assistance).

Figure 5.1 Impact of active labour market spending



Source: Bridji S. and Charpe M., (2010).

Figure 5.2 Unemployed receiving unemployment benefits in selected countries, latest available year (percentage of total unemployed)



Source: ILO (2010b).

... in the first instance by improving coverage of unemployment insurance...

As discussed above, Brazil extended benefits by two months and expanded eligibility for certain workers, so that by March 2009 over 780,000 job-seekers were receiving benefits. And while Brazil is only one of six Latin American countries with an unemployment insurance scheme in place, coverage is limited. By design, the programme only covers wage workers in the formal sector or about 35 per cent of workers. Effective coverage – due to eligibility requirements – is even lower (Figure 5.2); in fact, only 7 per cent of Brazil's unemployed are covered by unemployment benefits.[65] In most other emerging countries – and in the few Latin American countries with schemes in place – effective coverage is much higher, for instance 20 per cent in Chile and 13 per cent in China and Turkey.

[65] Calculated based on the number of unemployed workers in the labour force, including those whom are entering the labour market, who were employed informally, or who did not have sufficient tenure to qualify for benefits. Also includes those unemployed who have exhausted their benefits and are therefore no longer covered by the unemployment insurance programme.

During times of crisis, Brazil – and other countries – should consider extending benefits to a wider group of displaced workers, for example by allowing workers with shorter tenure to be eligible for benefits or by expanding eligibility criteria beyond the sector of employment. In the case of Brazil, in 2007 only 11,800 domestic workers received unemployment insurance benefits out of a total of 6.7 million employed as domestic workers. Consideration could have been given to improving access for domestic workers: current regulations stipulate that they may qualify for benefits only if their employer chooses to voluntarily enrol them in the Fundo de Garantia por Tempo de Serviço (FGTS).[66] In addition, extended eligibility criteria during downturns could be based on factors other than sector-specific. Although in many instances employment losses were initially concentrated in automobile manufacturing – and thus the expanded eligibility criteria was merited – firms whose demand stems either directly or indirectly from manufacturing were also severely impacted. For example, in the municipality of Betim, in the state of Minas Gerais, between November 2008 and March 2009 there was a net loss of over 7,000 formal manufacturing jobs, but service-related employment also fell by close to 2,000 during the same months.

... and strengthening linkages to other labour market programmes, for example by introducing mutual obligations related to training.

Policy-makers in Brazil could have leveraged the crisis as an opportunity to strengthen other labour market policies such as labour market intermediation and job training, and could also have improved the integration of these programmes into the unemployment insurance system. For example, there is little or no conditionality for receiving unemployment insurance, and recipients could benefit from job-related training or related labour market programmes. Although Brazil has an array of labour market policies, some of which have been in existence for various decades, neither labour market intermediation nor job training were included as part of the policy response to the crisis.

[66] Fundo de Garantia por Tempo de Serviço (Guarantee Fund for Time of Service) is an employer-financed severance system whereby 8 per cent of the worker's salary is deposited into an individual account every month. The worker can access the fund upon dismissal, retirement, or for the purchase of a house. In the case of unjust dismissal the employer pays a penalty equivalent to 40 per cent of the value of the fund.

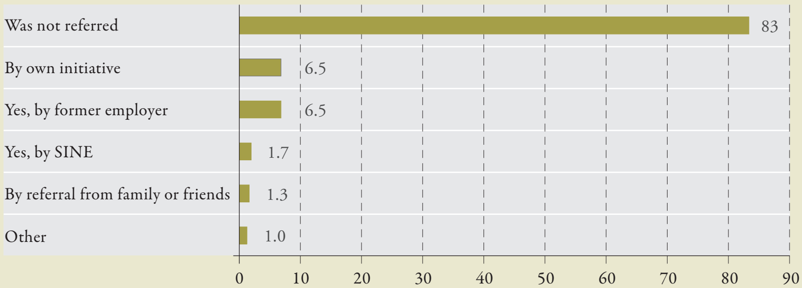
But for labour market policies and programmes to be effective, a competent public employment service (PES) is essential. Yet a recent evaluation of Brazil´s public employment system revealed some significant deficiencies that needed to be addressed (DATAUnB, 2010). One notable problem is the low percentage of referrals to the labour market intermediation system among workers who receive unemployment insurance benefits. In 2009, only 2.1 per cent of unemployed workers received support from the SINE during their job search. Moreover, even if referred, the placement rates from SINE are low, at around 18 per cent of the nearly six million workers registered during 2007–2009.

The low placement rate is partly attributable to the different profiles among workers registered at the SINE and the demands of the market. On the whole, employers were seeking workers with secondary education and who were under 40 years of age, whereas jobseekers tended to be less educated and older, or young people, who were more educated, but had limited work experience.

Job training is also not well integrated into the public employment system. A mere 1.7 per cent of unemployment insurance beneficiaries were referred to a professional job-training course (See Figure 5.2). Indeed, the evaluation of the public employment system revealed that it is better-educated youths, with access to information via the Internet, who tend to be registered in the courses offered through the National Professional Training Plan (PNQ). Of the 124 thousand persons who participated in a PNQ course during 2007, only 16 per cent were 40 years or older and 51 per cent were 24 years or younger. Moreover, among youths the courses were often not successful in leading them to job placement, as there was little on-the-job training and few opportunities to conduct internships after finishing the course.[67] Although job training cannot solve the problem of a lack of job offerings during a crisis, job-training courses, if well-designed, can improve employment prospects and support a productive recovery.

[67] Universidade de Brasília, DATAUnB (2010).

Figure 5.3 Referral of unemployment insurance beneficiaries to a training course, Brazil, 2009 (percentage)



Source: Universidade de Brasília, DATAUnB.

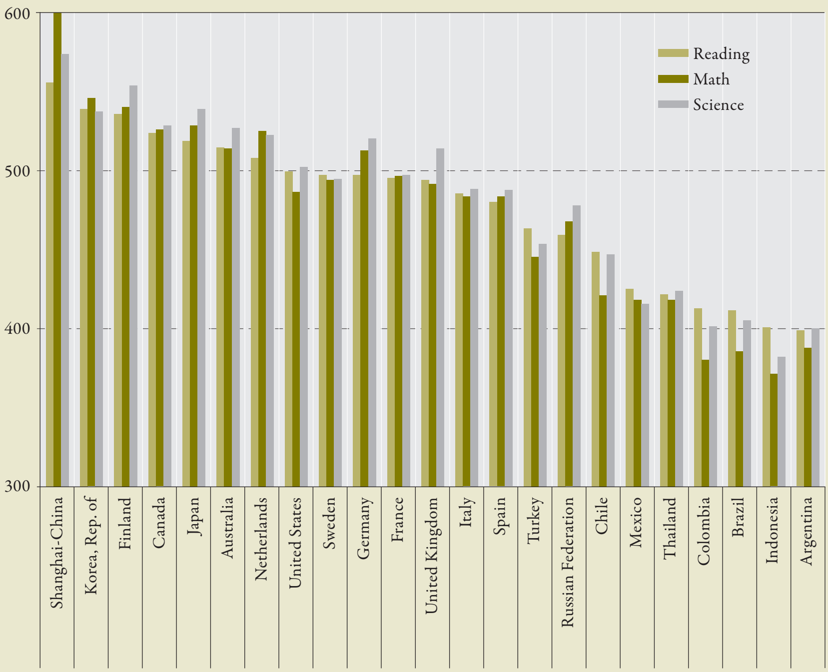
At the same time, educational outcomes need to be enhanced.

In the past two decades, Brazil has made considerable progress in terms of primary and secondary school enrolment. For example, the combined gross enrolment ratio in education (both sexes) has risen from just about 67 per cent in 1990 to over 87 per cent in 2005. As a result, there have also been some important improvements in literacy rates. However, overall skill levels of young students remains an important issue. For example, in the OECD's ranking of reading, science and math skills, Brazil trails most of the industrialized countries (Figure 5.4). Unless efforts are made to improve basic skills, this will compromise future labour market prospects of a large proportion of the labour force and have important negative consequences on overall competitiveness.

Consideration could be given to placing greater emphasis on employment retention schemes.

Because the crisis was short-lived, companies might have been better off had they taken steps to limit dismissals. Job loss can have significant and persistent repercussion on morale and productivity when – and if – hired back. There were some attempts to limit dismissals in Brazil, principally through the Bolsa Qualificação (Training Scholarship) programme, whereby workers participate in a training course and receive unemployment benefits for a few months and then return to their place of work. In 2008,

Figure 5.4 International PISA scores in math, reading and science, 2009



Source: OECD PISA 2009 database.

7,700 workers participated in this programme, but during the crisis year of 2009 the number jumped to approximately 20,100.[68] There were also some collective agreements signed – as discussed above – whereby workers agreed to collective holidays and reduced working hours with reduced pay. But given the short-term nature of the employment losses and related GDP decline in Brazil, policies such as work-sharing whereby workers accept to work reduced hours – in some cases with the Government compensating the wage reduction – could have been effective in lessening the number of dismissals, as was the case in Germany (Box 5.5).[69] Indeed, although Germany's GDP fell sharply during the crisis, the unemployment rate only increased from an average of 7.2 per cent for 2008 to 7.6 per cent for 2009 (in the same period, the average unemployment rate of the European Union

[68] Giubertti (2010).
[69] For more information on the German work-sharing programme, see Dietz et al. (forthcoming); Crimman et al. (2010).

Box 5.5 Germany's short-time work programme

In response to the economic crisis, short-time working arrangements (*Kurzarbeit*) were extended in 2008 from six to 18 months. In May 2009, the maximum length was extended again to 24 months. Under the programme, employers can apply for temporary state assistance to top up the wages of employees who are working reduced hours. The assistance is available to establishments which are facing a temporary, unavoidable loss of employment due to economic factors. The Federal Employment Agency covers 67 per cent of the net wage loss suffered by the wage earner (60 per cent for childless workers), and employers are reimbursed 50 per cent of the social security contributions they make on behalf of workers. This can rise to 100 per cent if the downtime (i.e. reduced working hours) is used for training. The state also pays for employees' contributions towards social benefits, pension, health care, long-time care, unemployment, and so on.

During the crisis, an average of 1.1 million people were on short-time working arrangements compared to fewer than 150,000 pre-crisis. In 2009 alone, an estimated 340,000 jobs were saved through reductions in weekly working hours, paid overtime, short-time work and working time accounts. As such, the *Kurzarbeit* programme has proved to be a highly effective and affordable approach towards minimizing unemployment and related costs.

Source: Dietz et al. (forthcoming); ILO (2009b).

rose by 1.9 percentage points). Alternatively, more sectoral agreements could have been made, as was the case in the 1990s with the sectoral chambers in the ABC region of São Paulo or the industrial pole of the Amazonas during the present crisis. In these instances, government tax concessions played a catalysing role in bringing employers into the negotiations and in guaranteeing worker retention.

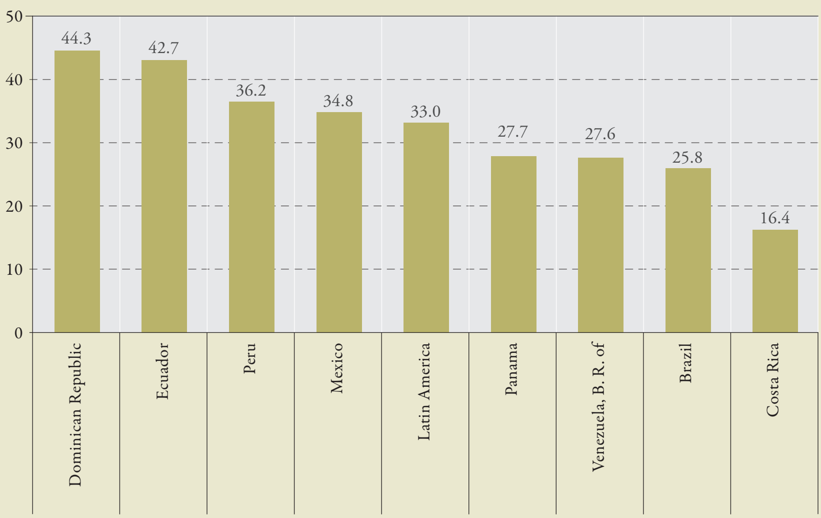
Efforts to reduce poverty, income inequality and informal employment must continue…

There are also a number of structural challenges that need to be addressed. Over the past couple of decades Brazil has made substantial progress in reducing poverty, income inequality and informal employment. For the most part, this trend was sustained through the crisis – aided in great part by the targeted social policies implemented. However, poverty and inequality – and to a lesser degree informal employment – remain high by international standards and in some cases substantially higher than many other countries in Latin America.

In terms of the share of the population living below the poverty line, in a comparison of recent data within Latin America, Brazil is doing rather well. In fact, among the nine countries in the region with available information, Brazil has the second lowest poverty rate at just over 25 per cent (Figure 5.5, panel A). Nevertheless, it is of concern when one-quarter of the population is living under the poverty line. And while on the one hand many Brazilians can benefit from the array of programmes available (e.g. one-quarter of the population benefits from Bolsa Familia), the mere fact that so many households are eligible merits some consideration of how best to ensure that, over time, individuals and households progress and become less reliant on such programmes. Similarly, a significant number of Brazilians – nearly 13 per cent – are living on less than US$2 per day, which is high in comparison with other major emerging economies and a number of Latin American countries such as Argentina, Chile, Malaysia, Mexico, Thailand and Uruguay (Figure 5.5, panel B).

Figure 5.5 Poverty rates in selected countries, latest year available, 2004–2008
(percentage of population)

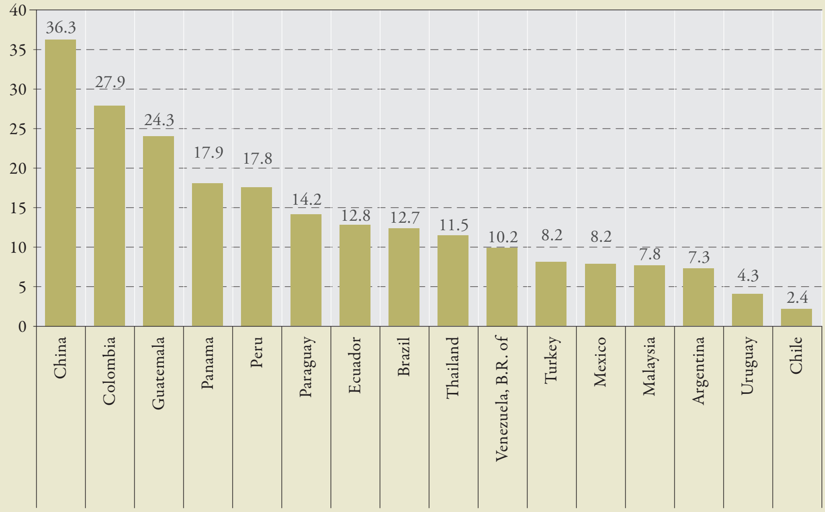
Panel A. Poverty rate in selected Latin American countries based on national definitions



Sources: United Nations Economic Commission for Latin America and the Caribbean (ECLAC), Statistics and Economic Projections Division for Panel A; World Bank, World Development Indicators (WDI) for Panel B.

Figure 5.5 Poverty rates in selected countries, latest year available, 2004–2008
(percentage of population)

Panel B. Income poverty in selected countries



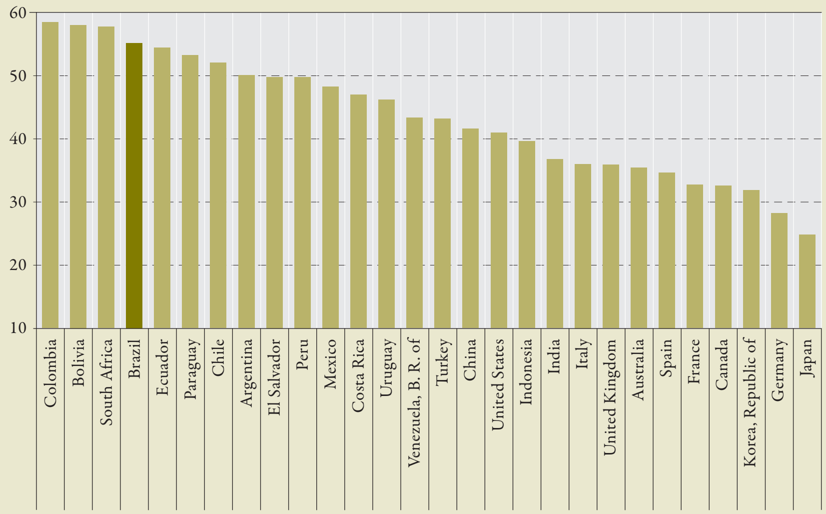
Note: Data for Panel B refer to the most recent year available during the period specified; income poverty refers to the share of the population living on less than US$2.00 a day at 2005 international prices.
Sources: United Nations Economic Commission for Latin America and the Caribbean (ECLAC), Statistics and Economic Projections Division for Panel A; World Bank, World Development Indicators (WDI) for Panel B.

Along the same lines, income inequality has been falling even during the crisis, as Chapter 1 illustrated. However, in spite of this progress, Brazil has one of the highest levels of income inequality – as measured by the Gini index – among G20 and selected Latin America countries (Figure 5.6). Only Bolivia, Colombia and South Africa have more unequal distributions of income. And while domestic demand is an important component of Brazil's growth, it is important to mindful of any adverse effects that income inequality can have on the accumulation of household debt. Indeed, household debt, excessive consumption and rising income inequalities played a fundamental role in the onset of the current crisis in many countries.

… and the minimum wage must continue to play a vital role.

Part of the challenge with respect to income inequality is the high rate of informal employment. Although the rate of informality in Brazil has fallen in recent years, so that as of August 2010 the share of salaried

Figure 5.6 Income inequality in G20 and selected Latin American countries, 2007
(Gini index)

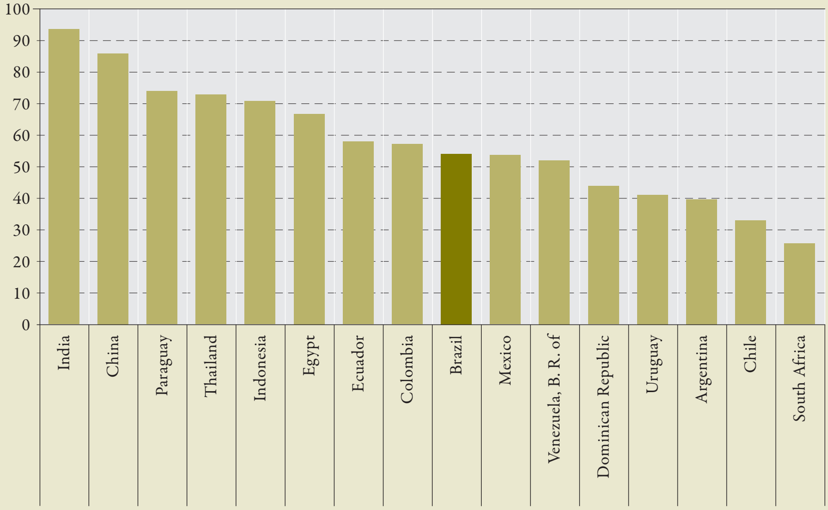


Note: The Gini index lies between 0 and 100. A value of 0 represents absolute equality and 100 absolute inequality.
Source: UNDP (2009).

workers without a signed labour card in the six metropolitan areas was just over one-quarter – compared to one-third prior to the crisis – informal employment in Brazil constitutes half the workforce, leaving many workers without adequate protection (Figure 5.7).[70] In many respects, efforts by Brazil to promote formal job creation have contributed positively to these efforts. At the same time, other labour market policies, notably the presence – and regular updating – of minimum wage, can play an important role in reducing the incidence of informality if properly set. While this may seem counterintuitive from a supply and demand framework, the increase in incomes of the workforce, especially those at the bottom of the wage pyramid, boosts consumption through the purchase of domestically produced goods and services. The additional aggregate demand brought about through the greater purchasing power, increases the demand for workers, especially in the areas of production, distribution and wholesale and retail trade, of which many occupations are formal.[71]

[70] Informal employment includes salaried workers, including domestics, without a signed labour card; self-employed workers and employers who do not contribute to the social security system; and unremunerated workers.
[71] Berg (2011).

Figure 5.7 Informal employment, 2001–2006



Note: Data refer to the most recent year available during the period specified
Source: Baccheta, Ernst and Bustamante (2009).

Finally, Brazil must continue to improve overall competitiveness.

To improve the country's competitiveness and its development prospects, policies are needed to bolster investment rates, reshape the tax system and ensure an exchange rate that aligned to improve the country's competitiveness and its development prospects. In the first instance, there is an over reliance on commodity exports for growth. In this regard, policies are needed to encourage investments, including physical and social infrastructure, in other areas in an attempt to diversify and develop other leading sectors – as has been the case with Brazil's aeronautics and biotechnology sectors for example. But overall investment levels – at about 17 per cent of GDP – is comparable low to other emerging countries, especially in developing Asia where investment levels are on average above 40 per cent of GDP. Moreover, investment in research and development, at 0.5 per cent, is a fraction of GDP.

Second, there are a number of taxes levied on production and consumption which hinders domestic demand and exacerbates income inequality. As such, more could be done to improve the progressivity of the current the tax system.[72] And finally, as the country recovers from the crisis, capital inflows have returned – boosted by the positive economic outlook and higher interest rates. This has lead to a significant appreciation of the R$, despite capital controls (2 per cent levy) put in place in October 2009. An over-appreciated currency could dampen export-oriented sectors and job creation. Brazil, as a member of the G20, could play a prominent role in advocating for the regulation of international capital flows, to the benefit not just of the Brazilian economy but the world economy as well.

[72] Santos and Silva (2010).

C CONCLUDING REMARKS AND WAY FORWARD

This chapter – and the report more broadly – highlight a number of valuable lessons stemming from Brazil's success in mitigating the labour market and social impacts of a financial and economic crisis. These lessons serve as good practices for countries that continue to be confronted by the challenges of the crisis.

More fundamentally, the experience of Brazil demonstrates that employment and social policies are not just residuals of economic growth but that they in fact help stimulate growth, productivity and economic dynamism – as well as providing much-needed support to the most vulnerable. These are lessons that go well beyond crisis mitigation, providing guidance on how to build productive, competitive, inclusive and sustainable societies.

In that respect, while Brazil has made remarkable progress – both recently and over the past decade – this chapter has drawn attention to a number of important challenges still facing the country. However, the current strength of the economic recovery under way represents an important opportunity to address and continue tackling some of these longer-standing issues.

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BRAZIL :
AN INNOVATIVE INCOME-LED STRATEGY

It is often argued that the cost of social equity is less economic growth, highlighting the supposed trade-off between these two goals. The crisis that erupted in 2008 – which was preceded by rising social inequalities – has shown that this is simply not the case. In fact, if properly designed, equity-enhancing policies can also promote prosperity and reduce the risk of future crises. The aim of the *Studies on Growth with Equity* is to show how such policy complementarities can be achieved.

Brazil provides a case in point. Over the past few years, the country launched a wide range of employment and social policies. Because the measures were carefully conceived and implemented in parallel with supporting macroeconomic policies, the country managed to reduce poverty and informality while achieving one of the most remarkable economic recoveries in the world.

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