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1. Introduction

As with most countries in Latin America, the greatest challenge facing the Brazilian economy is to find and follow a sustainable path towards equitable growth. To be clear, the challenge is not only to achieve good economic performance, as measured by GDP or the pace of economic growth: it is to do so whilst taming a rampant level of economic and social inequality typical of those that threaten the solidity and depth of democracies in the region (Figure 1).

The historically high levels of inequality in Latin America must have something to do with the legacies of the colonial past, as well as with the fact that the young independent nations in the 19th century generally did not seek social change in any significant way. For example, in Brazil the institution of slavery persisted until 1888, well after independence from Portugal was promulgated in 1822; and the social exclusion of those formerly enslaved persisted during the newly proclaimed Republic. However, whatever the weight of the past, it is now generally accepted that Latin America missed the so-called Great Levelling that was observed in the advanced economies of the Global North in the 20th century (Williamson, 2015, 2010). The latter, ravaged by great wars, were able to rebuild themselves based on all-encompassing social contracts, which included the construction of robust welfare states. What Latin America seems to have missed was the opportunity to build good economic performance concomitantly with achieving a substantial level of social balance. Aiming at this dual objective increasingly appears to be a condition for effective and lasting economic progress. (Cingano, 2014; IMF 2017; Wilkinson and Pickett, 2019) (Figure 2).

In failing to achieve these two objectives, Brazil is a typical Latin American country. Its management of its economy has accommodated high levels of economic and social inequality. In fact, according to Census data, at the height of the country's economic growth, in the 1960s and 70s, when GDP roughly doubled in each decade, it witnessed

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the highest levels of economic inequality on record until then. The most intense concentration occurred through the 1960s, when the Gini seems to have varied from .50 to .57.³ This conjunction sparked a ‘nature versus nurture’ debate among economists in the country in the 1970s: Was inequality a natural outcome of progress (e.g., higher demand for skilled workers meeting with insufficient supply); or was it a deliberate, policy-driven outcome?⁴ And while some scholars still insist that growing inequalities were the aches that inevitably accompanied sudden economic spurts, and were destined to vanish in time, there is a mounting consensus that policy choices were the key driver. Accordingly, inequalities were driven by the suppression of democracy during those decades: political opposition was muted, and unions, both urban and rural, were closed down and their leaders incarcerated; and a policy of wage repression particularly affected lower-skilled urban and industrial workers, ruling out any possibility of sharing economic prosperity (Hoffmann, 1973; Bacha and Taylor, 1978; Souza, 2018).⁵ Also, social investment in education and health care was largely neglected; and social protection was largely seen as irrelevant. In the end, the development project concocted by the ruling military, which expressed their peculiar understanding of ‘development as growth with structural change’, boiled down to state-led import substitution industrialization (ISI). This experiment, besides failing to show sustained results when compared to similar experiments elsewhere, was undertaken under the auspices of political repression of labor’s collective action, and there was no attempt to incorporate ample strata of urban and rural workers into the mainstream economy.

With the debt crises of the 1980s, practically the entire region plunged into economic stagnation. In the case of Brazil, this predicament translated into two decades of low growth (56 percent in the 1980s and 23 percent in the 1990s) and a still increasing level of inequality (reaching a Gini of .61 in 2000). The country restored democracy in the mid-80s and in 1988 it implemented a new constitution with the stated aim of fighting poverty and inequality. However, making good this promise on social rights had to be postponed. The problem was an elevated external debt, and high and growing inflation rates, to which Washington Consensus-like politico-economic decisions undertaken in the 1990s continued to add the negative impacts of open trade and capital flows, privatizations, and deceleration of public spending, even after the ghost of explosive inflation rates had finally been scared away in 1994 with the Real Plan. While the decades of high growth following an ISI policy, roughly from the 1930s to the 1980, were over, the experiments of the following decades, especially the 1990s, concentrated

³ This is Carlos Langoni’s (1972) estimation for the earnings of the labor force, excluding from the computation those declaring zero income.

⁴ For reference, see Tolipan and Tinelli 1975.

⁵ Hoffman synthesizes this policy as wage compression (in Portuguese, “arrocho salarial”). It combined repressive measures against the unions with devaluation of the minimum wage (for example, a loss of 25 percentage points between 1959-1961 and 1968-1970) and an increased flexibility for employers to fire low-wage workers. It was thus possible to avoid the obligation to concede inflation-related adjustments (which were mandated by the labor law for those who were already employed). The latter measure enabled employers to pay higher wages to higher-skilled workers, for whom there was no cap set in law. So, wage concentration increased, because of compression at the lowest level and no limitation at the top.

on price stabilization and stagnation of (non-financial) state expenditure. The latter resulted in economic stagnation, a deteriorating industrial output, and an increasingly precarious labor market.

It should be noted that neither state-led ISI, roughly from 1930 to 1980, nor the government-driven market-led experiments of the 1990s made confronting the obscene social question their main commitment. Of course, it has always been part of the industrialization rhetoric of latecomers on the periphery that social progress will inevitably follow the economic progress brought about by manufacturing. But lacking democracy, i.e., effective political competition and free and legally recognized collective action by workers, makes social progress an aspiration hard to fulfill, as the Brazilian wage repression policy testified. On the other hand, the rhetoric of less state and more market tries to sell a similar bargain. Unfettered markets will deliver economic efficiency, higher competitiveness, more and better jobs. In the end, relatively successful Brazilian industrial firms, those previously backed by now defunct industrial policies, were the target of foreign acquisitions,⁶ or simply failed. And many of those that were able to survive substantially shifted their workforce to informal contracts, that is, contracts outside the reach of the labor law and social protection.

What was not the subject of any sustained experimentation was something akin to the 20th century trajectory of the Global North's Great Levelling,⁷ the simultaneous seeking of growth and income redistribution. This, to some extent, is the great novelty of the 2000s in the region.

2. The Great Levelling in the Global South (2004-2014)?

In 2002, Brazil elected as president a candidate from the center-left (incidentally, a trade union leader) for the first time since the start of military rule in 1964. It is not without interest that, contrary to widespread fears, Lula da Silva and the Workers' Party (PT) shared with ousted president João Goulart and his early 1960s left-of-center coalition the ambition of regulating capitalism in the country. This included regulation of the labor market (legalized unions and a minimum wage), as well as land reform for a country with a Guinness Book of Records level of land ownership concentration. Back in the 1960s, this agenda had been seen, through the lens of Cold War paranoia, as a communist plot.⁸ Now, in 2003, in a country suffering from adherence to Washington

⁶ This is notoriously the case for one of the biggest Brazilian autoparts companies, the Metal Leve S.A., which ended up being acquired by the German company, Mahle GmbH, thanks to the abrupt introduction of trade openness by the Brazilian government back then - a dramatic episode narrated in Jaques Kerstenetzky (2018).

⁷ It should be noted that even after the ending of the "trente glorieuses" (after the 1970s) and the resurgence of some inequality in the Global North, especially, though not exclusively, in European countries, welfare states continued to grow and continued to reduce labor market income inequality substantially (by almost half). (See Kerstenetzky and Guedes, 2021).

⁸ Incidentally, the same Cold War that stimulated the development of welfare states in the former WWII allies in the West was a justification for countries such as the US to support dictatorships and smother social progress in Latin America.

Consensus recipes that had brought about increases in inflation, external debt, rates of unemployment, and informal work, along with meagre economic growth, a progressist agenda seemed to be all that was left to experiment with. But not immediately. First, in early 2003, speculative reaction to a left-wing government caused the Brazilian real to depreciate and increased the sovereign risk premium to unprecedented heights. So, the first year of Lula's mandate was, to some extent, a continuation of the orthodox macroeconomic tenets and policies of the previous government, especially the pursuance of high fiscal surpluses.

It was the decade between 2004 and 2014 that saw the kernel of a new progressive agenda. This was a period of sustained economic growth (lower than under the military, but higher than all the periods thereafter) and a reduction of economic inequalities, a combination not previously registered in the country. A raft of economic and social policies was drafted to deliver a growth style that I myself have called redistributive (Kerstenetzky, 2011, 2012, 2016) and other colleagues have called distribution-led (Carvalho and Rugitsky, 2015) to open a dialogue with the growth models literature. For the first time in 40 years, the social question was faced as a challenge to be confronted whilst implementing a growth strategy.

Domestic consumption, mass consumption in particular, was the main driver of growth in those years, rather than exports. Nevertheless, exports also grew substantially in the wake of the global commodity boom of the first decade of the 21st century, which itself was driven by the rise of China. The period of the 'economic miracle' of the 1970s had seen a rise in the appetite for consumer durables of the upper middle classes and the rich, a group whose highly concentrated hold on income distribution and consumption patterns were seen as the engine of industrialization. Now, consumption by the lower middle classes and the poor boosted the tertiary sector, thus helping to explain the latter's sudden growth and new structural changes, this time towards the service sector. Unsurprisingly, the barrage of jobs generated to respond to increased consumption levels by low-income families was mainly located in the service sector, especially in its personal and distributive (wholesale and retail) subsectors. That expansion contributed to a further increase in consumption and growth, in a process of circular causation (Kerstenetzky and Machado, 2018).

It should be noted that the increase in mass consumption was to an important extent policy-driven (this justifies the labels redistributive growth or distribution-led growth). It was not caused only by the substantial increase in targeted-to-the-poor social assistance benefits, such as the Bolsa Familia and others, important as these were. The policy of valorization of the minimum wage negotiated with the unions, which had been interrupted by the military back in 1964, was responsible for a substantial elevation of the much-depreciated minimum wage and was critical for the success of the experiment. This reverberated importantly in the labor market, affecting not only registered workers receiving the minimum wage but also others without formal contracts, who nonetheless had their salaries informally indexed to the statutory minimum. In any case, it should be

noted that informal employment decreased substantially,⁹ due, in addition to economic growth, to the higher oversight and incentives provided by new labor market policies. These included tax simplification for small businesses employing significant workforces and the regulation of domestic work (the law of the domestic worker), as well as expanded social protection. But besides its effect on the labor market, another important impact of the minimum wage policy was on those households which had someone receiving the basic pension, whose value was pegged to the statutory minimum wage. Indeed, the same was true of all social benefits that were guaranteed in the constitution, such as unemployment benefit and a non-contributory basic pension for rural workers and the very poor (elderly or disabled). Retirees receiving the basic pension represented around 60 percent of all retired persons in the public pension system in Brazil (Brito et al., 2017). In sum, and in practice, the minimum wage stood for a guaranteed minimum income for a large swathe of the Brazilian population, in or outside the labor market, and had a huge distributive impact.

In fact, it almost goes without saying that, beyond its impact on the pace of economic growth, this huge income influx substantially altered Brazilian income distribution, delivering the highest sustained decline in (household income) inequality on record in the country, to a Gini of .52 in 2014 down from .59 in 2002 (Kerstenetzky, 2017). The situation had reverted to that of the early 1960s, before military rule drove up income inequality. And, again, a minimum wage valorization policy had been key for that result (Brito, Foguel and Kerstenetzky, 2017).¹⁰ The results in terms of poverty reduction were also substantial: even higher than those obtained during the Real Plan, which controlled hyperinflation, and certainly more sustainable. The decline of 18 percentage points during the 2002-2014 period, to 10 percent of the population, was even more spectacular than the one-off 7 percentage points decrease that had taken place between 1993 and 1995 and had been followed by stabilization at the very high level of around 30 percent of the population (Kerstenetzky, 2017) (Figure 3). We know of similar outcomes in many countries in Latin America; and, thanks to recent data analysis, we also know that the depth of the redistributive experiment was greater in countries run by center left coalitions. The latter took advantage of the commodity boom to add to or strengthen redistributive policies (Lustig et al., 2023). Brazil remains the country whose distributive results were among the highest in the region.

Both functional and personal income distribution showed improvement in that decade. While the wage share effectively increased, on some estimations from 46 percent to 51 percent, between 2002 and 2014,¹¹ empirical research has also shown that it was the higher share of lower wages within the wage bill (both more jobs and higher wage rates)

⁹ Considering informal employment as that which is not covered by social security benefits, this dropped from 53 percent to 36 percent of the labor force between 2002 and 2014. For details, refer to Kerstenetzky and Machado, 2018.

¹⁰ Brito et al. (2017) also calculated that basic pensions were the main channel through which minimum wage valorization impacted on household income distribution between 1995, when the valorization started, and 2014.

¹¹ Miebach and Marquetti (2022).

that was the main driver of the expansion of consumption and hence of growth. This was due to a higher marginal propensity to consume in this stratum of the income distribution (see Carvalho and Rugitsky, 2015).¹² Of course, this is also true of families and individuals receiving increased social benefits. In the case of the Bolsa Familia program, this covered around 25 percent of the Brazilian population; but social security pegged to the minimum wage (e.g., the basic pension and other constitutional social benefits) plus minimum-wage earners covered even more, at about 40 percent.¹³

In addition to this classic Keynesian move, whereby effective demand was aided by a barrage of public transfers and a social indexer, redistributive growth also relied on what Colin Crouch has famously called ‘privatized Keynesianism’, as noted in Carvalho and Rugitsky (op.cit.). In fact, access to credit (both public *and* private) was amplified, including for low-income families and individuals. The upshot was a sustained growth process with distribution, in fact, led by the latter and their increasing employment, especially formal employment (i.e., conforming to labor law as well as covered by social security). This was not only a unique outcome in the country’s history but also unique when compared to those of other emergent regions of the world over the same time period. These regions included countries such as China, India, Russia, and South Africa, some known for their ‘jobless-growth’ (India¹⁴ and China,¹⁵ for example, with elasticity of employment in relation to growth well below one, while in Brazil that elasticity exceeded one, especially for registered workers¹⁶), or for mainly creating low-paying or precarious jobs (South Africa) and generally enhancing inequality.¹⁷ However, it was certainly not unique in human experience, considering the history of advanced economies in the Global North in the 20th century.

But the experiment also had its fallouts. The list should include an increased level of deindustrialization, even of re-primarization, of the Brazilian economy, thanks to a substantial growth in the import of capital goods and high-value inputs (importantly) from China and increasing reliance on commodity exports (mainly) to China of unprocessed materials such as soy, meat, and oil. Also, most of the new opportunities for job creation were in the low-end service sector: government consumption, such as

¹² According to Carvalho and Rugitsky (2015, p.9), “[d]ata of the latest consumer expenditure survey in Brazil (Pesquisa de Orçamento Familiar, 2009) reveals that the propensity to consume over total income of top income earners is 56 percent, relative to more than 100 percent in the lower income category and 84 percent on average.”

¹³ Castro (2012) estimated that there were 12.4 million Bolsa Familia benefits, covering around 50 million people, as well as 30 million direct receivers of the minimum wage, either as social benefits or public sector wages (21.9 million) or even private sector wages (8.8 million) in 2009 - in a total population of 191.5 million Brazilians. Since some of the MW receivers lived in the same household as other receivers, we cannot just multiply the number of benefits by a factor of 3.8 (the average size of a Brazilian family then) to calculate MW coverage, as we did with the Bolsa Familia benefit. But according to Castro’s estimates, that coverage should reach at least 40 percent of the population.

¹⁴ Jobless growth is defined in the literature as GDP growth which is not accompanied by an equivalent growth in jobs; in other words, a one percent increase in the GDP generates a less than one percent increase in employment. The data for India is in Rizwanul (2015).

¹⁵ Zhou (2020).

¹⁶ Amitrano (2013) found an elasticity of 1.57, in 2010.

¹⁷ For reference, see OECD, 2015.

that needed to provide public education and health services, though increasing, was not engaged with significantly as part of a necessary and more ambitious structural change; and increasing household debt signaled not only higher financial vulnerability among low-income families but also regressive transfers to financial wealth owners. Finally, the redistributive experiment left unscathed the income of the tax-privileged richest 10 percent of the population, who could still take home as much as 58 percent of national income and up to 79 percent of national wealth.¹⁸ Most of the redistribution happened among the poorer 90 percent portion of the population.

So, something of a Great Levelling, but not a great one.

3. The Backlash (2016-2022)

However accommodating of the interests of economic elites (especially bankers, agribusiness, and big business as a whole) the redistributive experiment was, when the occasion presented itself, in 2016, these elites swiftly grabbed it to back a parliamentary coup that ousted President Dilma Rousseff (PT) and to execute an electoral fraud that would advance their preferred policy agenda.

True, the Rousseff mandates (2010-2014 and 2015-2016) had been jeopardized by the commodity bust of 2012, as well as by unforced missteps. These, initially, included running an increase in the fiscal surplus and allowing stagnation of public investment; and later, when the economy started to decelerate, several cuts were made in payroll taxes, which did not result in more private investment but contributed to fiscal deterioration and a rise in the public debt (Carvalho and Rugitsky op.cit.). The years 2015 and 2016 saw the country plunging into deep recession (negative growth of 3.6 and 3.8 percent respectively) and high unemployment (9.8, in 2015, a rise of 38 percent in relation to 2014, and a peak of 12 percent, in 2016) as a result, and the political factor was important, both for deepening the recession and for bringing a complete change in the policy course thereafter.

In fact, as early as 2016, the new president, Michel Temer (then Dilma Rousseff's vice president), succeeded in having the Congress approve the starkest fiscal rule on earth, the expenditure ceiling rule, which halted the growth of real primary public spending in the country for 20 years. According to some projections this would shrink the Brazilian central government to the point where it would account for around 13 percent of GDP by the end of the period, starting from a 20 percent high (Dweck 2020). That this was the intention was never hidden from the public by policy makers drawing up the fiscal rule. Also, a labor law reform was hastily approved, nominally to curb unemployment by deregulating the labor market but actually aimed at eliminating unions and labor rights (the full plan, conceived by the subsequent Jair Bolsonaro government, was to be even more abstruse, including the complete elimination of social contributions from employers). That this program had not been submitted to the electorate, who instead had

¹⁸ See WID, 2023

voted for an agenda of social programs and public investments when electing Rousseff, was already shocking enough. Even more shocking, perhaps, was the conformist attitude of the Congress when confronted with an unpopular reform and a fiscal rule that tied their hands. (What congress members' political calculation was will become clearer when we get to the self-serving financial strategies devised by Brazilian legislators, in the next section.) But the backlash did not finish there. A far-right populist non-mainstream politician, who openly defended military dictatorship and the practice of torture, was democratically elected in Brazil when Temer's mandate (that is, Rousseff's) ended in 2018.

Intellectual elites still struggle to understand how this was possible. It certainly offered those who took advantage of it a unique window of opportunity. Lula was imprisoned following the Lava Jato judicial investigation (a Brazilian version of the Italian *Mani Pulite*) and was prevented by the Supreme Court from running for the presidency despite (some say because of) the fact that all polls showed he would have won against Jair Bolsonaro. The Lava Jato had deeply damaged the public image of the Workers' Party and, to a great extent, that of the entire political system, to which Bolsonaro claimed to be an outsider. Then, Bolsonaro suffered a failed murder attempt whilst campaigning in the province of Minas Gerais. The mainstream press amplified all this daily: Lula and the PT were corrupt; the Lava Jato was redemptive; Bolsonaro, after the attempted murder, was a victim. Add to that the military, the social conservatives, former middle-class PT voters' resentment, and the right-wing electorate proper, now out of the closet. That election was certainly not run according to the classic class struggle script.

Bolsonaro's rule, from 2019, followed a script of unending campaigns against the left, the judiciary, liberal democratic governance, the state itself. The economics of government was left in the hands of a Chicago graduate ultra-liberal economist, and the mission was 'to shrink the state', dismantling its capacities, weakening, or altogether eliminating public policies. The scene was further complicated by Bolsonaro's management of the pandemic in Brazil. When he had to do something, he still maintained an adversarial attitude. By denying the gravity of the health crisis, delegitimizing scientific and medical discourse, as well as civil society and subnational governments' protective initiatives, he contributed to increasing the number of victims,¹⁹ which in Brazil was well above what might have been expected.²⁰ When he did govern, Bolsonaro ruled for *his* people, his constituency: agribusiness (against environmental protections, indigenous land demarcation, landless peasants' movements), the military (almost 5,000 took up positions of power in the executive, and there was an expansion of civic-military schools); and religious and non-religious social

¹⁹ According to some estimates, by rejecting the offers of two vaccine producers, Bolsonaro may have been responsible for the deaths of at least one hundred thousand Brazilians between January and June 2021 (see Barros, 2023). Castilho et al. showed that in 2020-2021 there were more deaths in municipalities that had chosen Bolsonaro, instead of the PT's candidate, in the 2018 poll.

²⁰ With 2.7 percent of world population, Brazil nonetheless had over 12 percent of the global death toll.

conservatives who despised gender, racial, and sexual orientation issues. There is not much to tell with respect to the economy, except that the rosy promises of the neoliberal agenda, whose fundamental tenets were established during Temer's administration, were unfulfilled. Inequality started to climb again as early as 2015 and the economy stagnated.²¹

4. The pendulum swings yet again (2023-?)

An underlying theme in the political economic plot of recent years in Brazil is the nature and functioning of the political system, its 'coalition presidentialism' which is, incidentally, not a Brazilian invention.

After redemocratization, the number of parties in Brazil increased almost non-stop, culminating in over thirty during the PT years in government, up from 6 in 1980 (when bipartidism was abolished by the military with the aim of dividing the opposition and winning the 1982 subnational elections). A stimulus for the multiplication of parties was provided in the form of easy access to public financing and publicly financed time for campaigning on television and in other mainstream media.

With dozens of competing parties in Congress, no incumbent president had the parliamentary muscle to achieve approval of their projects; so, coalitions had to be mounted. In turn, having this number of parties meant it was not their programs that distinguished one from the other, but rather the likelihood (based on potential number of votes in Congress) of their obtaining participation in government or access to resources for attending to their local constituencies. Many of them came together in a huge informal bloc called the Centrão (the Big Center)²². Centrão, proved to stand for 'critical mass', rather than for an ideological middle ground of sorts, as the bloc was ruthlessly self-serving and conservative.

Governments resorted to different strategies to form coalitions and attract the Centrão or members of it. These ranged from sharing power directly to offering positions in, or linked to, the executive (ministries, high-profile positions in state companies) or even outright cash payments to representatives, payments disguised, for example, as part of the publicity expenditure of state companies. The shadow of corruption loomed large

²¹ My colleague, Ricardo Bielshowsky, recalls that Bolsonaro's finance minister, Paulo Guedes, and the central banker appointed by him, Roberto Campos Neto, kept the basic interest rate near to zero at a time when capital was already flowing out of Brazil (2020 and 2021) due to the pandemic. This contributed strongly to the devaluation of the real and an increase in inflation which hit the poor the hardest. He also considers whether higher inflation might have been the most important factor in the electoral demise of Bolsonaro in 2022.

²² The origins of the Centrão go back to the constituent assembly of 1987. The bloc ended up exercising an important power of veto against the progressist agenda when mobilized by politicians espousing right wing policies.

over these stratagems and has tainted all presidencies since 1989, when the first presidential election after redemocratization took place.²³

In any case, until Bolsonaro's presidency, the upper hand in the bargaining was with the executive; but after him, parties, especially party leaders, started to seize greater autonomy by directly accessing, with presidential connivance, huge amounts of discretionary resources (beyond the already sizeable public financing of parties and campaigns they had already voted for). The level of these resources quadrupled under Bolsonaro (from 10 to 46 billion of reais, around 34 percent of the discretionary resources at the disposal of the executive which must be passed on to members of Congress). But the big novelty was the so-called 'secret budget', i.e., budgetary resources received and allocated by MPs in states or municipalities without any transparency, and without any regard to the executive power's publicly proclaimed priorities and policies (see Folha, 2023). All this further increased the costs of coalition formation and weakened the ability of any president to advance their projects.

This was the political scene facing Lula at the beginning of his third mandate in 2023. In 2022, he had been absolved by the Supreme Court of the corruption charges raised against him, because the Lava Jato investigation was deemed to have been vitiated, with Judge Sergio Moro being shown to have been politically biased in convicting the former president (incidentally, in 2019, Bolsonaro appointed Moro as his minister of justice). Hence, he was able to run for president in the 2022 election and ended up defeating Bolsonaro by a small margin. Most of the votes for Lula came from the poor and marginalized: blacks, women, Catholics, and those living in the poor Northeast, as well as in big cities such as São Paulo. However, the mandate was not only his, but belonged to a widely encompassing political coalition forged for fear that a second far-right mandate would deal a fatal blow to Brazilian democracy. It gathered the center left and the center right around the defense of democratic institutions seen as under immediate threat.

As well as finding common ground within such a heterogeneous group, Lula has before him the task of reconstructing institutions, policies, practices, and state capacities that were left wrecked, and of 'picking up where he left off', i.e., resuming the interrupted project of redistributive growth. In other words, he must glue together his new center-right allies and his traditional constituency, the poor.

Ironically, the pandemic helped to set the agenda by throwing into dramatic focus the manifold - now dramatically increased - social needs in the country: the need to strengthen the public health system, the school system, and social protection. The pandemic also highlighted the inadequacy of Brazil's tax system, which exempts the very rich from paying taxes despite their ownership of a huge proportion of the

²³ In pre-democratic Brazil, private companies on public contracts, especially the big ones in the construction sector, usually operated in association with public agents to deplete the public purse and enlarge their private profits by overpricing. After democratization, this corruption stratagem was kept in place, this time to finance political campaigns, which in Brazil tend to be exceedingly expensive. (See Barros, 2023)

country's income and wealth. A tax reform was needed. Also requiring urgent attention was the climate crisis, in particular the threat to the rain forest and the heating of the planet brought about by wildfires. The incidence of these fires had intensified, as under Bolsonaro they were neglected, and even indirectly stimulated.

Lula also inherited from Bolsonaro a public deficit disguised as a surplus. To make possible belated attempts by Bolsonaro to buy votes (by spreading money among the poor in his final year in office, including just months before the runoff presidential election in October 2022), his government defaulted on judicial liabilities amounting to dozens of billions of reais. This (Congress-approved) default was designed as a postponement which would simply transfer the debt to the next administration. Finally, to keep spending within the 'expenditure ceiling' rule, Bolsonaro passed in November 2022 a budget for 2023 that included an enormous cut: in it, there was no room for social programs such as the Bolsa Familia, for the program to increase the number of medical doctors, for investment in education or indeed for public investment in general, for the valorization of the minimum wage, or for the adjustment of the income tax schedule, which would have benefitted the lower middle class – all initiatives which Lula had promised to undertake and had been elected to undertake in the October poll.

Lula and his winning coalition were able to pass a replacement budget in Congress in December 2022, even before his inauguration on 1 January 2023. That budget supplemented the previous one with resources sufficient to make good on Lula's campaign promises. Moreover, Lula's budget was approved by a supermajority as a constitutional amendment that altogether eliminated the expenditure ceiling rule (which had been included in the Constitution). The budget also committed the new government to presenting a new fiscal rule before Congress by August 2023, this time as an ordinary legal rule.

Few would have predicted that the same Congress that was generally so submissive to Bolsonaro (the management of the pandemic provoking an exception) would so swiftly and massively support Lula. This could be seen as simply giving him a year's breathing space; but it was still astonishing. The negotiating season had reopened, and earlier than anyone would have guessed.

The additional primary expenditure included in the 2023 budget amounted to 1.5 percent of 2022 GDP. Another commitment, this time to reduce the primary deficit to just 1 percent (a more stringent target than the Congress-approved 2.2 percent), added a fiscal demand of 1.2 percent of GDP. So, an increase in expenditure and a lower fiscal deficit would require more revenue: a predicted 2.7 percent of GDP. To achieve this, the government intended to close loopholes in the tax system, of which there were many. According to conservative estimates these might amount to US\$ 100 billion (e.g., a little more than the entire budget of the public health system, or 4.5 percent of 2022 GDP). Loopholes, also called 'tax expenditure' (or 'renunciation of revenue'), do not add much to growth or employment and tend to increase income concentration.

A second key measure was approved in July 2023, when Lula succeeded in getting Congress to pass a new fiscal rule requiring the generation of a fiscal surplus within two years and the relating of real growth of public expenditure to that of revenue. The surplus was proposed to shrink a public debt that now amounted to 74 percent of GDP and absorbed 7 percent of GDP as debt service. The debt was generally perceived to need stabilization. This was particularly important given the extremely high real basic interest rate (around 8 percent), the management of which was in the hands of an ‘independent’ Central Bank (whose president was a former Bolsonaro ally). But budget surpluses were expected to appear only in 2025. As for tying the expansion of non-financial expenditure to that of revenue, the rhythms of expansion were set to be unequal. Given the need to generate surpluses, expenditure was to grow less than revenue – up to 70 percent of the growth of the latter; but the floor was the population’s growth rate (0.6 percent), so that per capita real expenditure would not decline. There was also a guaranteed minimum growth of public investment, at 0.6 percent of yearly GDP. And there was a cap on the growth of expenditure, given by the hypothesized (low, at 2.5 percent) yearly growth rate of the economy over the next 4 years.

The final touch as far as macroeconomic policy was concerned was tax reform. Congress took partial action by having a vote on indirect taxes, and created a VAT that would both enhance tax efficiency, by eliminating cumulativeness, and create equity, by setting different rates according to whether goods and services were essential or non-essential. At the same time, a second round of reform was planned, this time to increase the progressivity of the tax system by taxing wealth, a move that would meet more resistance in Congress,²⁴ with its overrepresentation of the interests of higher income groups. But taxing the rich would become increasingly difficult to avoid if the plan was to expand public expenditure and investment and service the country’s domestic debt, especially in view of an increasingly difficult international context (slower growth in China and the fallout from the Russo-Ukrainian war), and the country’s recent past of low or no growth.

This fiscal architecture was devised to finance both short-term expenditure, such as on social programs, social services, and minimum wage valorization, and public investment and publicly financed private investment. In the case of investment, the plan included an extension of the role of the BNDES (National Bank of Development), still the financial mainstay for private investment in Brazil. This time around, the BNDES would go beyond drawing on public money, and would access international financial sources such as the Interamerican Development Bank, the Bank of China, the Bank of the BRICS, and would issue BNDES bonds.

Critics of these plans might ask for a more ambitious and innovative agenda – one that would directly tackle the issue of equitable and sustainable development. To this end, a decision was taken to create a new edition of the PAC (Program of acceleration of growth, in the Portuguese acronym) which had been inaugurated in Rousseff’s term and

²⁴ The tax system is generally considered regressive for relying largely on consumption taxes and displaying very low progressivity when it comes to direct taxes.

which envisaged a package of investment in physical, social, and environmental infrastructure. Environmental investment was to include a myriad of mitigation and adaptation measures in various areas, configuring what the government called the Plan for Ecological Transformation.

The investments planned in the new PAC amounted to 1.4 trillion reais over four years,²⁵ i.e., around 3.5 percent of GDP, of which a quarter was direct public investment (including that of state companies, the main one being Petrobras). The rest would come from publicly financed private investment (via the BNDES) or direct private investment. So, public-private partnerships and concessions to the private sector would be key components of the fiscal stimulus.

Planned investments (public and private) in the new PAC,
in billions of reais – Brazil, 2023

	2023-2026	2027	Total
Efficient and sustainable transport	220,9	128,2	349,1
Inclusive social infrastructure	2,1	0,3	2,4
Water for all	26,1	4,9	31
Digital inclusion and connectivity	20,3	7,6	27,9
Energy transition and safety	449,4	90,9	540,3
Innovation in the defense industry	27,8	25	52,8
Education, science and technology	36,7	8,3	45
Health	29,3	1,2	30,5
Total	1,4 tri	0,3 tri	1,7 tri

Source: Casa Civil website, Brazilian government <https://www.gov.br/casacivil/novopac/conheca-o-plano>. Accessed on 29 September 2023.

To sum up, several of the short-term measures described above (i.e., in the approved 2023 budget²⁶) paid off very quickly as the rate of GDP growth reached 3.1 percent in the first semester of 2023. This was driven not only by an agribusiness export boom but also by a fiscal impulse which encouraged consumption. Unemployment finally dropped to a little over pre-recession levels (8.0 percent in the second quarter of 2023 and dropping – down from 9.3 percent in the second quarter of 2022), and the real wage

²⁵ These included investments planned for 2027, though Lula's mandate would end in 2026.

²⁶ Others, such as the recently approved program to reduce or even eliminate the financial debt of low-income families, were still to play out.

bill climbed, reflecting an additional 1 million formal jobs. Also helpful were rises in the minimum wage, plus a relatively modest and declining inflation rate (around 3.2 percent). The initial strong resistance of the Central Bank to reducing the prime tax rate, probably the main brake on the country's economic growth, finally began to yield somewhat, with three consecutive .5 percent reductions in the second semester of 2023. True, the level of private investments did not react; but neither did it fall; and there was a general perception, stimulated by the new fiscal rule, that public accounts were moving in the right direction, which would show in falls in the future interest rates in September 2023. The package of publicly coordinated investments showed promise to the extent that it might act as a 'big push' with green deal features, and from the start seemed likely to propel industry and quality services within an eco-social sustainability paradigm. But of course, there was also resistance, and the battlefield, unsurprisingly, was fiscal policy.

5. Perspectives

Difficult as it always is to foresee the future whatever the circumstances, we might try here to envisage possible directions in terms of what now appear to be the opportunities and challenges.

The short-term impediments to Brazilian socioeconomic progress seem to have been taken seriously and addressed by the economic policies and initiatives of the new government. The most serious of them all has already been overcome, namely the expenditure ceiling of the Temer administration which, if thoroughly in place, would simply eliminate the fiscal and social state altogether. The new initiatives have opened up space for fiscally stimulated economic and equity advances. It is to be hoped that these initiatives will be financed by more progressive taxation.²⁷ Labor law reform, the second blow delivered by the Temer administration, has yet to be changed, and this is no small task, as precarious forms of employment and a weakening of collective bargaining are now set in law. In terms of a more distant horizon, the coordinated investments proposed under PAC3 seem ambitious in the kinds of investment that are contemplated, including social and ecological projects; but they reflect the current view that socioecological policies and investments offer, in addition to sustainable well-being, potential economic returns.

There is a chance that this agenda will succeed. The economic, social, and ecological prospects are really promising. And the short-term measures are already paying off as there are signs of improvement in the 2023 (six-month) growth rate, some progress in the labor market, and some reduction in deforestation of the Amazon region. If this

²⁷ By contrast with the former fiscal rule, the expenditure ceiling, which was added to the Brazilian constitution and needed a supermajority to be removed therefrom, the new rule was approved as an ordinary law, which should facilitate later changes.

trend continues, now enhanced by the PAC investments, this will be a green deal à la Brazilian.

This arrangement reflects the support of the center-left and the center-right, and of heterodox and orthodox economists to the government program proposed by Lula. However, despite a widely shared feeling among these groups that democracy needs substantial financial commitment, especially in countries with huge (pandemic-aggravated) social debts, such as those in Latin America, the actual commitment may be modest.

For example, the estimated growth rate embodied in the new fiscal rule, 2.5 percent (also the cap for increasing expenditures), was soon outdated (the cumulative rate for the year 2023 in July was 3.1 percent). In any case, it is not clear why there is a need to keep to an upper limit, provided that a portion of the increase in revenue goes to reducing the public debt. A compromise might seriously affect urgent spending needs. For example, if the country were to make good on commitments to education and health care included in the 1988 Constitution, it would need to more than double current public investments. Using an alternative measurement, Brazilian expenditure per student on basic education as a proportion of per capita GDP would have to increase 3 percentage points to reach the OECD average (23 percent versus 26 percent), and per capita health expenditure would have to almost double (4.2 percent versus 7.2 percent). The positive macroeconomic impacts of expenditure on health care and education cannot be overestimated, including the impact on GDP²⁸ and (equitable and green) jobs creation (Kerstenetzky et al., 2023). In that sense, capping the growth of expenditure at 2.5 percent per year does not seem to take seriously enough the huge gap, no matter the parameter adopted, and the extraordinary opportunity to promote sustainable wellbeing that shrinking it represents.²⁹

The other problem is the underlying political system and the dynamics that have resulted in congress members' substantial budgetary autonomy from the executive power. The president has been able to approve a great number of measures that are central to his progressive agenda; but the price being paid needs to be factored in. Special treatment for legislative amendments (which are excluded from the limits imposed on primary expenditure, and now amount to one quarter of the free resources at the disposal of the executive branch),³⁰ as well as huge resources thrown at the military ('defense industry') in PAC3, equivalent to the planned investment in health care, both give an idea of the political cost. It is pork-barrel and 'fourth power' politics through the back door.

For example, representatives have free rein when it comes to deciding where to put money coming in from guaranteed billionaire legislative amendments. This has recently been shown to have resulted in people from some of the poorest and driest Northeastern

²⁸ Castro et al. (2011) calculated a fiscal multiplier of 1.85 for education and 1.7 for health care.

²⁹ Thus far, there are aspects of the new fiscal rule that are unclear, including the reconciliation of its targets with constitutional minima that apply to education and health care.

³⁰ Folha 2023.

towns being provided with no water reservoirs at all, while other towns in the same region have access to more reservoirs than they need, and some reservoirs have deteriorated for lack of use. The state company that controls water distribution in the Northeast is led by a member of the Centrão and he holds his position thanks to negotiations to approve Lula's progressive agenda.³¹

New tax loopholes have undermined progressive legislative initiatives from the executive as a result of the same kind of bargaining.

As for the military, not only are they an increasingly protected corporation, with special pensions and discretionary resources of their own, but they also continue to see themselves as an overarching power in the Republic and act upon that distorted view.

Last, but certainly not least, progressive taxation, viz. of offshore money and 'exclusive funds' owned by the very rich (tax-exempt individual funds with values of over 5 million reais each), is meeting with resistance from the same Congressmen from the Centrão who compose the legislative basis which has thus far been loyal to Lula.

In the end, what the balance will be is hard to guess; but if the result is an increasingly frustrated electorate, and resources in the wrong hands, there will be a serious chance of a far-right comeback.

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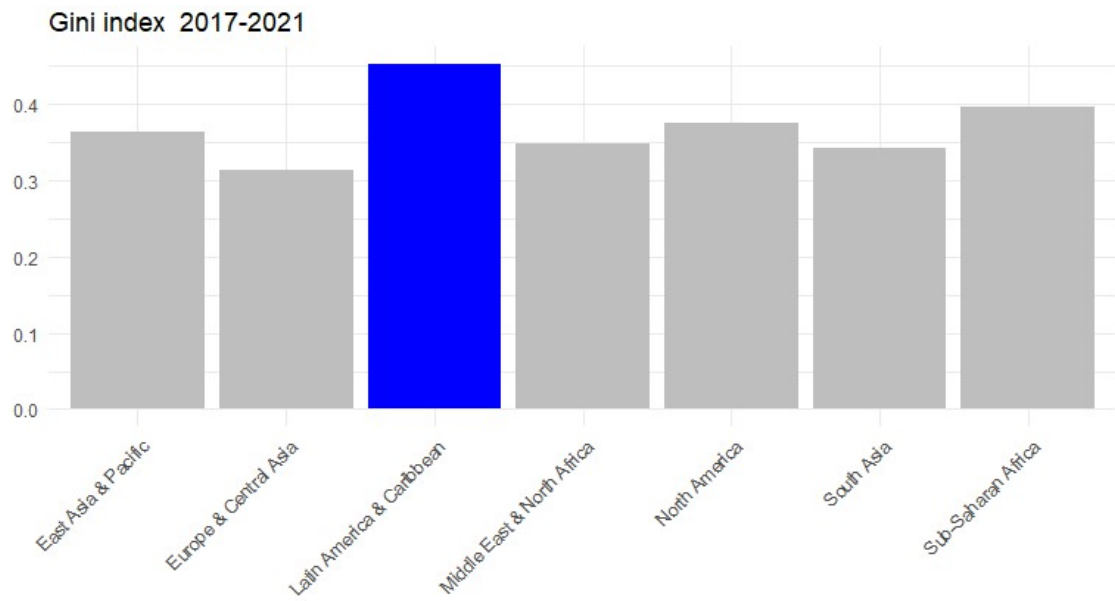
³¹ Folha 2023.

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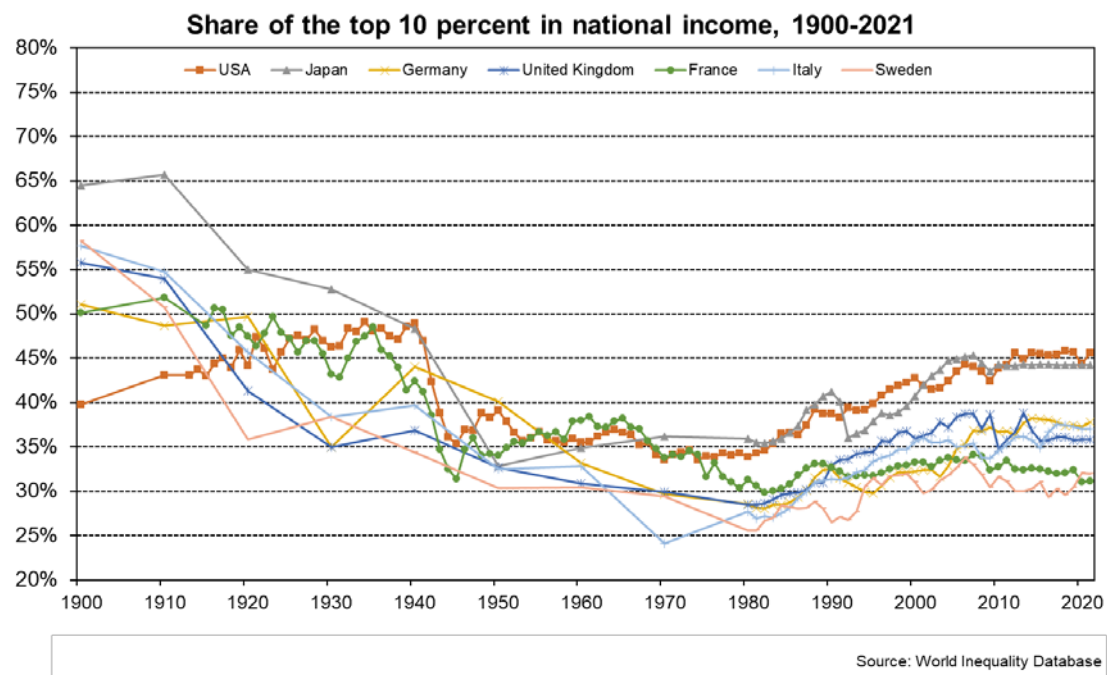
Annex

Figure 1:



Source: World Bank database

Figure 2:



Source: World Inequality Database

Figure 3:

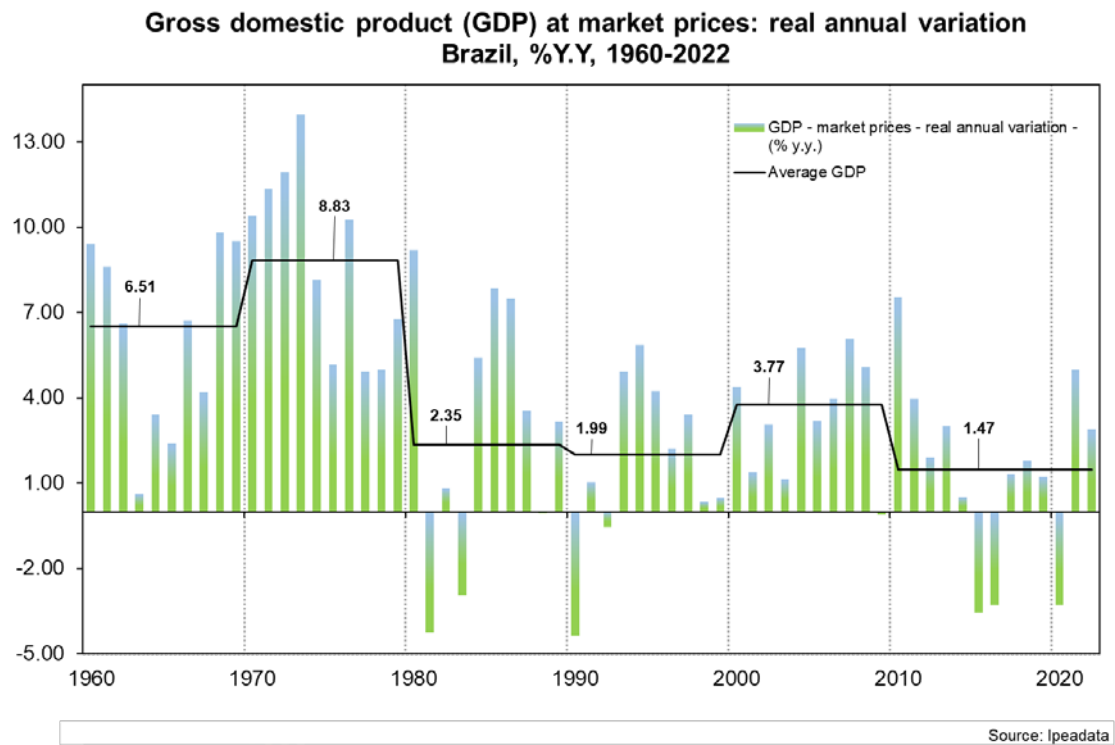


Figure 4:

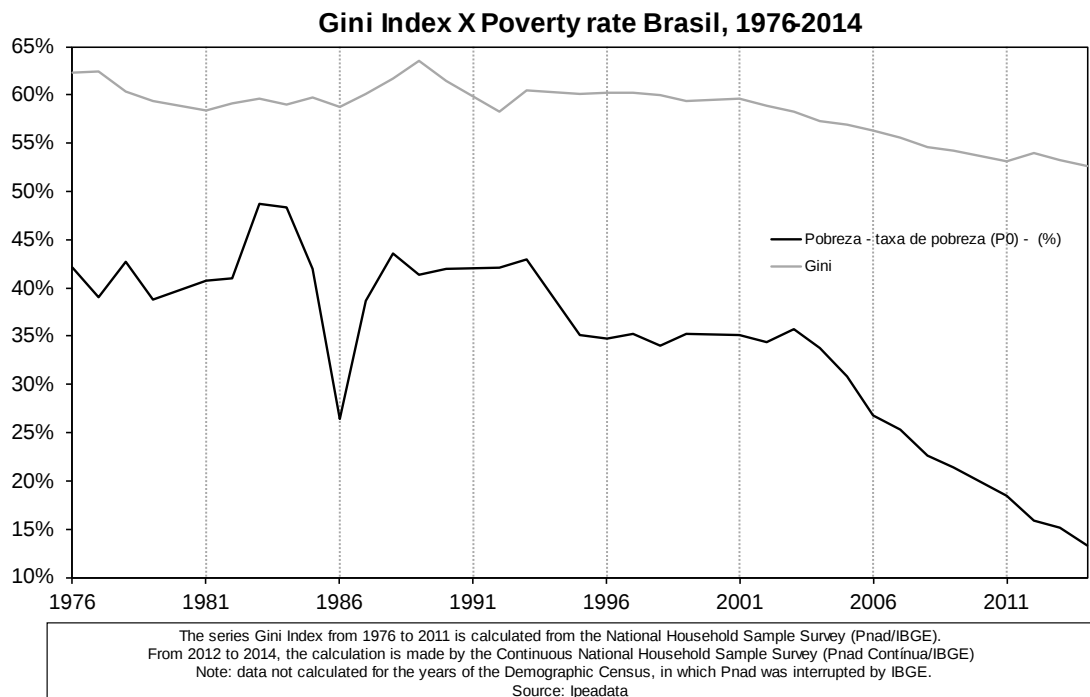
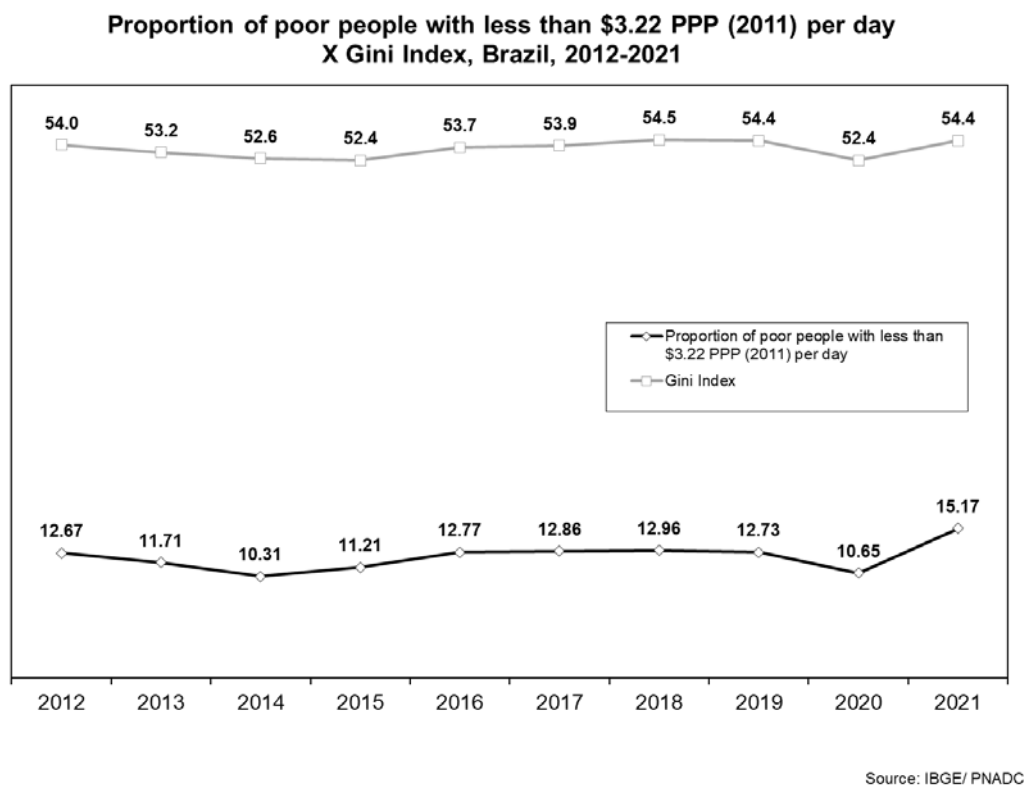


Figure 5:



Figure 6:



Note: Both the poverty rate and the Gini index declined in 2020 due to cash transfers (the “auxílio emergencial”) to a large proportion of the Brazilian population following the Covid-19 pandemic, proposed and approved by the Brazilian Congress.