The Economist

Special report:
Brazil

Grounded

Having come tantalisingly close to taking off, Brazil has stalled. Helen Joyce explains what it must do to get airborne again

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IN JUNE THIS year Brazil was struck by an outbreak of mass protests as sudden as a tropical storm. Brutal policing of demonstrations against a rise in bus fares elicited a wave of solidarity and brought more than a million marchers to the streets on subsequent nights. It also gave vent to previously unsuspected public fury over rising inflation, high taxes, poor public services and political corruption. Even football, a Brazilian passion, became a target of the protesters' ire. Many carried placards contrasting their government's lavish spending on stadiums for next year's World Cup with the dire state of the rest of the country's infrastructure.

The change in political weather came after almost two decades of brightening skies. Since 1994, when hyperinflation was tamed with a new currency, the real, successive governments have pursued generally sound economic policies and adopted anti-poverty programmes. The economy grew rapidly and inequality declined. The global commodity boom helped by sucking in Brazilian iron ore and agricultural produce, and in 2007 Brazil struck vast deposits of deep-sea oil. Being chosen to host both the 2014 World Cup and the 2016 Olympics seemed due recognition that its days as a chronic underachiever were behind it.

But Brazil's economy did not play ball. Having grown by 7.5% in 2010, the fastest rate for a quarter-century, it slowed to 2.7% in 2011 and a mere 0.9% in 2012. This year will see a tepid recovery at best. Inflation is sticking at around 6%. Pessimists recall that the one period of impressive growth within living memory, in the 1970s, ended in chaos and hyperinflation. In recent years Brazil has been seen as one of the leading emerging-market economies that would help drive global growth in the next half-century. But many now wonder whether it has managed nothing more than a *vôo de galinha* (chicken flight), a brief, unsustainable growth spurt followed by a rapid return to earth.

During Brazil's "economic miracle" of the 1970s it was the rich who captured most of the gains. At the time Edmar Bacha, an economist, invented a new label for it, "Belíndia"—a combination of a small, rich country, like Belgium, and a large, poor one, like India. Public education, health care and roads were provided for the Belgian part. Those living in India did without and expected nothing better.

Brazil is still one of the world's most unequal countries. Its murder rate rivals Mexico's. Public health care is a lottery. Fewer than half its pupils leave school fully literate. But it is no longer Belíndia. In the past quarter-century a better labour market and a basic social safety net have cut poverty by two-thirds. In the past decade the income of the poorest 10% of Brazilians has almost doubled in real terms, whereas that of the richest 10% has grown by less than a fifth. Brazil's Gini coefficient, a measure that expresses income inequality, is at a 50-year low. But "there is a sense in which Brazil is still Belíndia," says Marcelo Neri, the president of IPEA, a government-funded think-tank: "A rich country that's growing like Belgium—that is, slowly—and a poor one that's growing fast, like India."

More than half Brazil's population of 200m now belongs to a new lower-middle class, living in households with a monthly income per person between 291 and 1,019 reais ($127-446). Most of these gains in income have come from earnings, though government transfers have made an important contribution, especially in the poor north-east. Tens of millions of Brazilians now live in more solid houses equipped with cookers, fridges and washing machines. Many own cars. Children of illiterate domestic servants have jobs in the formal economy and study for degrees at night.

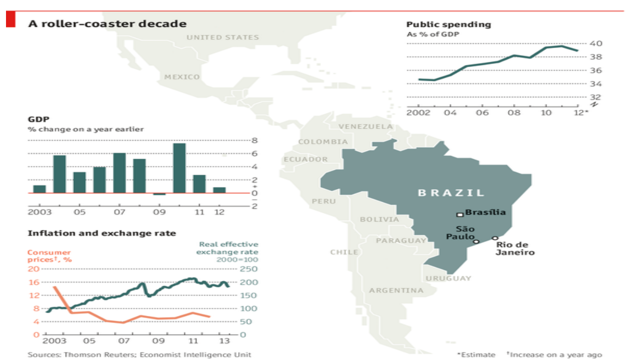
But when the new middle classes step outside their doors, traces of 1970s Belíndia are still all around. The number of cars in circulation has more than doubled in a decade, but most roads are still unpaved and few new ones have been built. Public transport consists mainly of packed, decrepit buses. Air traffic has also more than doubled in the past ten years, but airports have barely been touched. Children attend school in two, sometimes three shifts a day. Two-fifths of Brazilians are not covered by local primary health care. When life was a struggle for survival, the economy and jobs were the main concerns. Now that people are a little better off, the parlous state of infrastructure and public services is at the front of their minds.

The government has tried but largely failed to respond to growing demand for public goods. Many of the big infrastructure projects included in its Growth Acceleration Programme announced in 2007 are running years behind schedule and way above budget. Dilma Rousseff, the president, appears at last to have accepted that Brazil will need private-sector involvement to get the roads, railways, ports and airports it needs, but her conversion has been late and grudging. Concessions to run three airports were auctioned at the beginning of 2012, but auctions for more airports, as well as ports, roads and railways, were delayed while the government quibbled over the terms.

The dangers of complacency

Many Brazilian politicians seem to believe that the protests were simply growing pains, but they are being unduly complacent. They should have realised that the new middle classes would want decent public services, commutes without epic traffic jams and elected representatives who were visibly working towards these ends. Several parties have proposed electoral reforms to make politicians more responsive to voters, but they all want different things, so reaching consensus will be difficult.

A less favourable economic climate is now making it even harder to meet the voters' increasingly vocal demands. The slowdown in growth has caused a downturn in investment, which last year was just 18.4% of GDP, not enough to lead a recovery or to build the infrastructure Brazil needs. Ms Rousseff has been hectoring businessmen to invest more, ignoring the fact that it is mainly government obstructionism and heavy-handedness that hold them back. And commodity prices seem unlikely to bail out Brazil's economy with another growth spurt.



The country has also blown its chance to cash in on its demographic bonus. Its birth rate has declined steeply over the past few decades but it still has a young population, with many people currently of working age, and a relatively small number of dependants at either end of the age scale. Unfortunately most of this bonus is going on a crazily generous pension system. That will soon put an even bigger strain on public finances as large numbers of workers start to retire.

Despite all these caveats, this special report will argue that, given the will, there is scope for the social and economic advances of the past two decades to continue. Brazil's agribusiness has made huge productivity gains and offers opportunities for further growth. Innovative consumer firms are catering to the new middle classes and are starting to expand abroad. Brazil's politicians have been put on notice that today's young adults, better educated than the previous generation, will be less willing to accept corrupt, venal politics and more insistent on getting decent public services in return for the high taxes they pay.

The way to fund such services is not to increase public spending, which at 38.5% of GDP is already far higher than in comparable countries, but to get growth going again. To achieve that, the government will have to resume the reforms it dropped during the good times: trimming pension benefits, cutting red tape, lowering and simplifying taxes and updating labour laws. Successful infrastructure auctions, too, would help get investment back on track, and abandoning anti-profit rhetoric would improve business sentiment. But the most urgent problem that Brazil needs to tackle is a sharp loss of competitiveness.

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