

Structural reform priorities for Brazil

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Wilson Center - November 13th, 2018

How to prioritize structural reforms

- ▶ Like other EMs, Brazil faces a long list of possible structural reforms
- ▶ Doing **all reforms at once is unviable**
 - ▶ Risk of widespread political backlash
 - ▶ Better not to overburden public administration
- ▶ So how to identify reform priorities?
 - ▶ Common answer is to look at economic impact
 - ▶ But this approach is somewhat naïve since it fails to consider political obstacles

Prioritizing with two-step approach

- ▶ To identify reform priorities, we suggest two-step approach
 1. Choose reforms with **strongest economic impact**
 2. and **highest public support**
- ▶ Choice of which reform to prioritize can also be influenced by
 - ▶ legislative considerations
 - ▶ fiscal implications
- ▶ In this presentation, we apply this methodology to Brazil

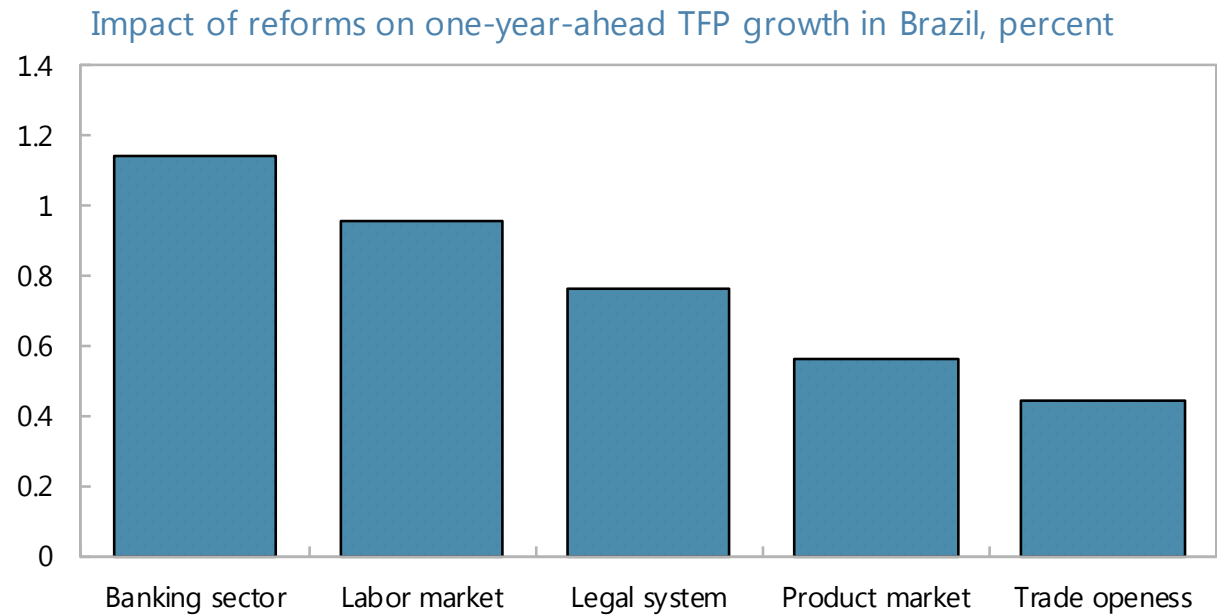
I. Economic impact of reforms



Assessing economic impact of reforms

- ▶ We follow empirical literature on the effects of structural reforms
 - ▶ Ostry et al. (2009), Bouis and Duval (2011), Prati et al. (2013), IMF (2015)
- 1. **Estimate impact** of reforms on TFP growth using panel regressions
- 2. **Measure structural reform gaps** in Brazil relative to advanced economies
- 3. Multiply estimated impacts by reform gaps to obtain overall effects in Brazil

Economic impact of structural reforms



II. Public support for reforms

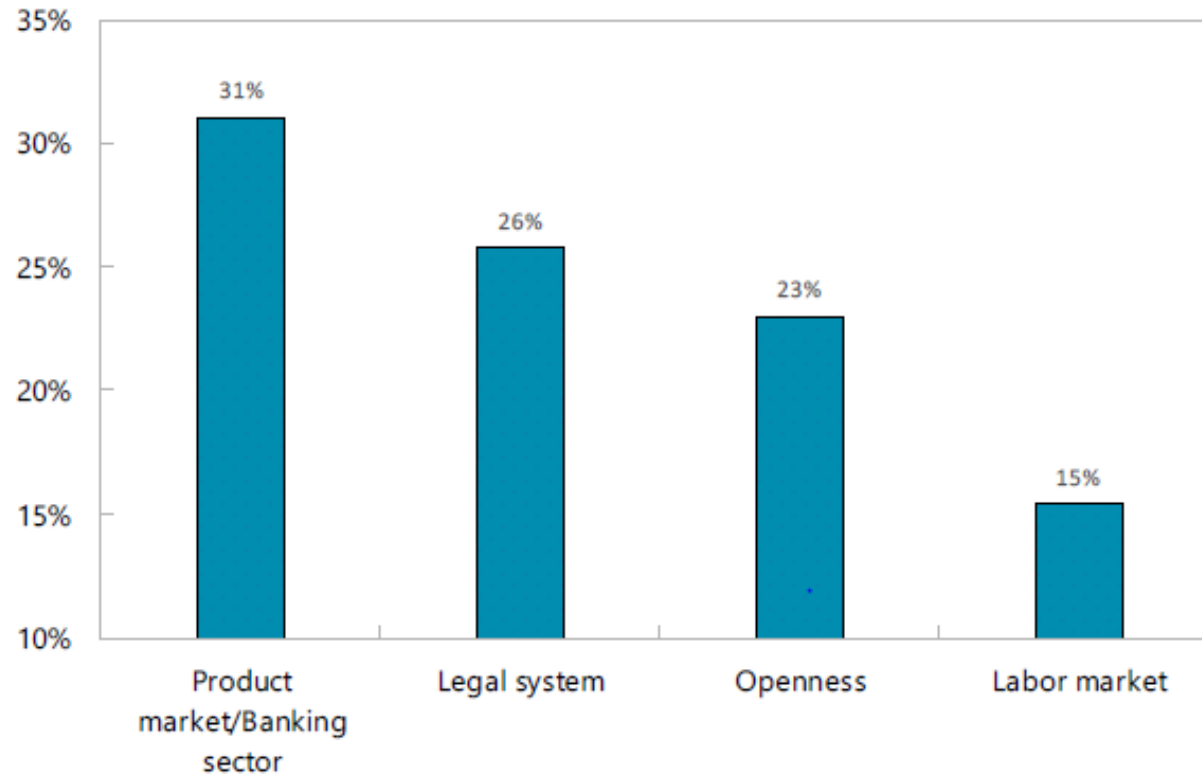
How to assess public support for reforms?

- ▶ To assess public support, we use survey data from Latin Barometer
- ▶ One question asks about people's support for free-market economy
 - ▶ Across Latam, **support for reforms increases with economic growth**
 - ▶ Be proactive, don't delay reforms until crisis strikes
- ▶ Another question asks about the **key issues for economic development**
- ▶ Some answers can be easily matched to structural reforms
 - ▶ "Integration to the world" as support for trade reforms
 - ▶ "Rule of law" and "Quality of public institutions" as support for legal reforms

Matching with structural reforms

- ▶ In other cases, the matching with structural reform is less straightforward
 - ▶ “Productivity” and “Innovation” as support for banking and product-market reforms
 - ▶ “Equity of opportunity” as support for labor market reforms
- ▶ Two exercises to **validate our matching procedure**
 1. Call for “innovation/productivity” stronger in countries lagging in banking/product reforms
 2. Call for “equity of opportunity” stronger by winners from labor reforms, e.g. unemployed

Public support for reforms in Brazil

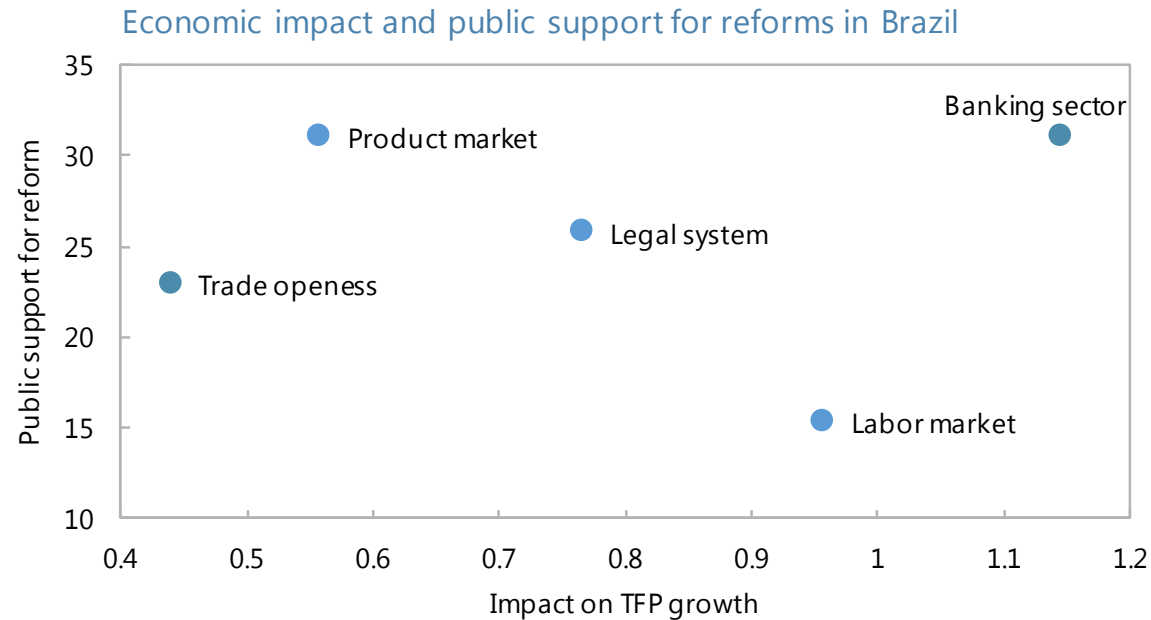


III. Identifying reform priorities



The impact-support frontier

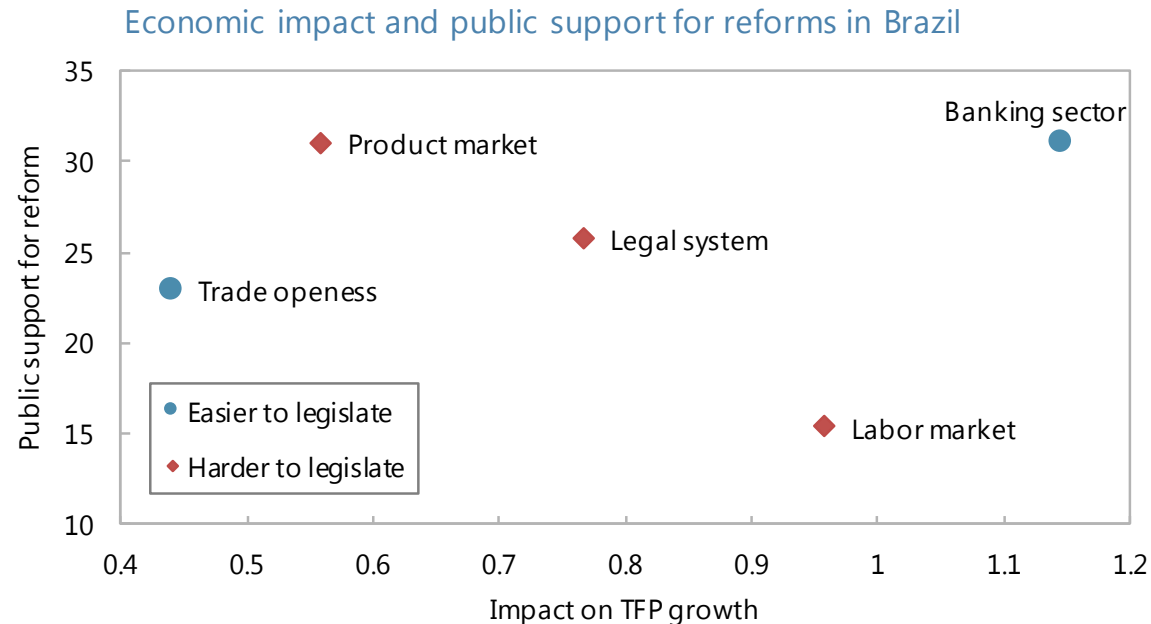
- ▶ Using our two-step approach, we can draw impact-support frontier



- ▶ Banking sector reforms have **strongest economic impact** and **highest public support**

The impact-support frontier

- ▶ Using our two-step approach, we can draw impact-support frontier



- ▶ Banking sector reforms have **strongest economic impact** and **highest public support**
- ▶ They are also **simple to legislative** without congressional approval
- ▶ By reducing credit subsidies, they also generate **fiscal gains**

Conclusion

- ▶ To select reform priorities, we propose two-step approach considering
 1. **economic impact** estimated with conventional empirical techniques
 2. **public support** based on the analysis of survey data
 - ▶ Priorities can also be influenced by legislative considerations and fiscal impacts
- ▶ To maximize public support, **do reforms when economy is growing**
- ▶ **Banking reforms** can generate highest economic gains at the lowest political cost
 - ▶ They are also simple to legislate and deliver fiscal savings