

THINKING BRAZIL

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A Newsletter of BRAZIL @ THE WILSON CENTER

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75 Days of Luis Inácio Lula da Silva

Progress and Prospects

Brazil is moving forward under the new presidential administration of Luiz Inacio "Lula" da Silva. Despite initial concerns regarding his sensitivity to Brazil's delicate economic situation, so far Lula has made all the right moves. Initial measures taken to calm international markets prior to his inauguration were extended on February 7th when Finance Minister Antonio Palocci announced the elevation of the primary fiscal surplus target to 4.25% of GDP (previously 3.75%).

In an effort to align the budget with the implications of this decision, the administration announced on February 10th that it would hold back the equivalent of U.S. \$4 billion already earmarked for the 2003 federal budget. Although these decisions ignited negative reactions from radicals within Lula's PT (Workers' Party) they also mollified international markets in addition to the most stridently pessimistic analysts of the Brazilian economy.

By mid-March, the profile of Lula's Administration has been clearly sketched out, which presented an excellent opportunity for a careful assessment of the challenges that lie ahead. How have efforts to calm investors and guide Latin America's largest economy out of crisis fared thus far? What lies ahead for Brazil's domestic and foreign policy? What trends, challenges and opportunities will Brazil experience under Lula?



Alexandre Barros

On March 19th, political scientist and risk analysis expert Alexandre Barros discussed Brazilian President Luis Inácio Lula da Silva's first 75 days in office. Barros's presentation satiated a thirst among international observers for insight on current risks in the economic and political framework of Brazil after one of the most closely followed elections in history.

Facing grim prospects for a quick global economic recovery, Barros noted that Brazil is also forced to cope with overwhelming social demands on the domestic front. He noted that the central challenge for Lula's administration will be to transmit confidence to foreign financial markets by demonstrating respect for existing contracts while simultaneously addressing social needs, trimming public expenditures, fighting corruption, reducing the debt burden, and promoting economic growth. Consequently, during the first days of his administration, Lula has adopted a very orthodox set of economic poli-

cies not dissimilar to those already being implemented by the previous administration.

According to Barros, "there is nothing more similar to a conservative than a liberal in power."

In this context, Lula has been pursuing a responsible economic policy based on maintenance of fiscal prudence while pushing for reforms of the tax (revenue sharing) and social security systems as well as securing the autonomy of the Central Bank.

Although not unexpected in a new and inexperienced administration, some flaws have begun to appear in the form of details overlooked in major policies, prompting critics to question the efficiency of Lula's administration. Barros felt that these criticisms, in addition to what he referred to as "ego disputes" and the possible radicalization of some factions of Lula's political party (the PT) could raise red flags in any analysis or predictions regarding this administration. He also raised concerns about dual stan-



Public Policy Scholar Competition 2003

We are pleased to announce continuation of the Brazilian Ministry of Culture's Public Policy Scholars for 2003. The topic of the current competition is *The Influence of Race and Social Inequality on Brazilian and American Culture*. Application instructions and additional information can be found at www.wilsoncenter.org/brazil. Completed applications, including all supporting material, must arrive at the Wilson Center, or be emailed as attachments to parlini-aj@wwic.si.edu by April 18th, 2003.



dards for the administration's appointments - economic positions were filled with individuals based on technical merit, while appointees in other sectors were designated for political reasons.

Barros emphasized the importance of addressing the debt burden (67% of GDP in 2002) and for the Central Bank to achieve its targets, reducing its vulnerability in dollars. In order to achieve these goals Brazil needs to increase its exports which places enormous importance on bilateral trade with the United States (which accounts for 23% of Brazil's imports and 24% of its exports).

Mr. Barros categorized several issues as "big if's" deeming them too underdeveloped to make reliable predictions. Those areas include privatization, deregulation, social expenditures, growth and debt, and friction in Brazil-US trade relations. Barros felt that Brazil's overall outlook could be sunny or bleak hinging on the administration's

effectiveness in managing these variables.

The deterioration of global political and economic conditions as well as the emergence of serious domestic challenges are concerning trends. Barros, however, remains optimistic for Brazil's future - he believes Lula's election and the first steps of his administration have been surefooted.



Moreover, he believes that the entire process represents a true revolution in Brazilian politics, forcing observers in Brazil and around the world to view today's government in a new light.



FROM THE DIRECTOR

Strategic Survey 2002/2003

On April 10, 2003, Luis Inácio Lula da Silva had plenty of reasons to celebrate the first 100 days of his administration. During this period he thwarted dreadful domestic and international forecasts, maintained high approval ratings (75%), and garnered important victories in both the economic and political realms. Of course, many suspicions persist regarding the competency of Lula's team, but these suspicions are not anymore based on ideological determinism or prejudices but on practical concerns. Consequently, the bastion of doubt regarding Lula's effectiveness has fallen and the growing degree of confidence in Brazil is reflective of these changes.

During early April, "Brazil's Country Risk," (average yield spread over US Treasuries) which was almost 2,500 points in September 2002, had fallen below 1000 (991) for the first time since May of 2002. After having fell 35% against the dollar last year, the Brazilian Real has rebounded 8% in 2003 and was traded at R\$ 3.27 to the dollar in April 2, the best rate in three months. The trade balance registered a US\$ 3.76 billion surplus, prompting Brazilian authorities to forecast a surplus of US\$16 billion by the end of 2003. The C Bond, Brazil's most traded international bond, gained 3.16%. During the first two months of 2003, the government was able to secure a primary surplus of R\$ 16.1 billion, or 6.6% of GDP, which outpaced the targeted rate of

4.25%.

Although the trade balance was somewhat influenced by rising inflation, all other results were effected by important decisions made by the administration including: resistance to the pressure from state governors to renegotiate their respective debts with the federal government, the establishing of a high nominal interest rate (26.5%), the unilateral raise of the primary surplus target at 4.25%, and cuts in the budgeted expenses (R\$ 14 billion).

In the political realm, Lula scored an extraordinary goal by passing his first ambitious reform in the lower House. On April 2, 2003, the House approved in first round (442 in favor, 13 against and 17 abstentions) legislation, which will lead to autonomy for the Central Bank. An important accomplishment in itself, facilitating this legislation was also a political demonstration of Lula's capability of gathering support for future reforms. Indeed, his success portends the possibility of passing critical reforms to the tax system and public sector pension regime.



Seminar Announcement

MEET THE LULA GOVERNMENT

May 12 – 14, 2003, Brasilia

Organized by Forum Empresarial Brasil and the Brazilian Amercian Chamber of Commerce of Florida, this important seminar will connect investors and business executives with cabinet members and important representatives of the new government of Brazil. Participants will discuss government policies and investment perspectives which may be mutually beneficial for Brazil and for companies with Brazil-based/related operations.

[Click Here to register!](#)

Thinking Brazil is a publication of **Brazil @ the Wilson Center**.

This project is founded on the conviction that Brazil and the U.S.-Brazilian relationship deserve to receive better attention in Washington. Brazil's population, size, and economy, as well as its unique position as a regional leader and global player fully justify this interest. In response, and in keeping with the Center's mission to bridge scholarly research and public action, **Brazil @ the Wilson Center** sponsor activities designed to create a "presence" for Brazil in Washington that captures the attention of the policymaking community. **Brazil @ the Wilson Center** is grateful for the support of the Ministry of Culture of Brazil, ADM, Cargill, Chevron-Texaco, FMC, and GE Fund.

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