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The Rise and Fall of Brazil's economic growth

Centre for Social and Economic Progress (CSEP)
CSEP Research Foundation

6, Dr Jose P Rizal Marg, Chanakyapuri, New Delhi 110021, India

Ph: 011 2415 7600

Speaker(s)

Roberto Zagha
Former Country Director for India, World Bank

Anoop Singh
Member of India's 15th Finance Commission & Distinguished Fellow, CSEP

Moderator(s)

Montek Singh Ahluwalia
Distinguished Fellow, CSEP

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Rakesh Mohan:

Montek Ahluwalia and Anoop Singh, the chair and the discussant. Let me just say a few words about Roberto Zagha. He doesn't know where he comes from. Because, he was born in Cairo. Then went somewhere else. Then went to Buenos Aires to school and so on. Then went to Brazil to school and college. Then made his way to the United States. And of course, to the World Bank. During his time at the World Bank, he was country director for India stationed here for four years. Then he actually found when he got here that he felt completely at home here. So, his conclusion was that he must have been Indian in his earlier life. But of course, he is Brazilian in terms of nationality as far as I know. And done a lot of work on the Brazilian economy. So, we took advantage of his brief visit to Delhi, to India this time for him to talk to us about the Brazilian economy because we hardly ever get a chance to hear about other economies. So, the only thing I would say since he is talking about the rise and fall of Brazil's economic growth, I would just say a couple of words on the rise that, in the 1950s and 60s until I think around 1980, the growth wasn't so high in the 70s after the oil crash. But it was still high. But certainly, in the 50s and 60s Japan was number one in terms of high growth. And Brazil was number two or about the same. So, people have forgotten that for almost 20 years at least, they were among the champion growers in the world in terms of economic growth. So, it is very useful to hear about what happened then. What happened later? Also, it gives you great warning for not to be complacent when you have had high growth. Things can really go wrong after that. Therefore, I think it is very interesting to hear Roberto and welcome Roberto to CSEP and I hope that… I think you have come after three years or so because of covid. So, we are hoping that covid is actually gone and so we hope we would welcome you here more often and spend more time here. We can give you a small desk to be with us. Because otherwise everything else is occupied. Montek, you are on.

Montek Singh Ahluwalia:

Thank you, Rakesh. I am just going to sort of go straight to ask you. I have known Roberto for a very, very long time. And if I got into that it would be very interesting and amusing. But it will take up too much time. So, let me just join Rakesh in welcoming you. Let me invite you to start your presentation.

Roberto Zagha:

Thank you very much. First of all, I would like to say that it is with great pleasure and honor and no little emotion that I find myself in Delhi once again among friends. And (audio break) very important in my professional life and many of whom have helped me grow not only as an economist, but also as a person. I am very grateful to be here with you and thank you very much for the invitation, Montek. Thank you very much, for the invitation Rakesh. (Inaudible talks from audience) Hello to the zoom. Nice to speak to the zoom too. I am going to keep this presentation to 35 to 45 minutes to leave time for questions and discussions which I think there will be a lot. The title of my talk is 'The rise and fall of Brazil economic growth'. For reasons which will become very evident in a few seconds. The presentation will look at the performance of Brazilian economy, some structural evolution of the economy and particularly important part will be the ideas dominating macroeconomic policies and the current events. Montek always insisted, when he was working on the growth commission that ideas drive policies and sometimes bad ideas drive policies. I think, as you will see this happens not only in India, but in other places as well. Brazil's external and to some extent internal image doesn't much correspond to reality. Yes, there have been lot of expectations about Brazil economic growth. Many of you may remember the Austrian writer, Stefan Zweig, who in the 1940s when he had left Austria to exile himself in Brazil in the city of Salvador Bahia. He had declared that Brazil was the country of the future and will always be. In some respect it is a very painful comment. For some time, Brazil seems to have escaped from this destiny. But as you will see, this is still haunting the country. In 2001, James O'Neill of Goldman Sachs painted a very opportunistic outlook for the BRICS. Of the BRICS, Brazil as you will see not really qualifies anymore, Russia well let us not talk about it because it will be opened to war. India and China and south Africa has not done very well. So, of the BRICS only India and China are two remaining countries. But in 2001there were good reasons to be optimistic about Brazil. The democratic transition from military regime to democracy had been very successful. Much more successful than in other places. There was an end to hyper inflation in 1994 which was done with very little shock to output. There was a very successful management of the fall out of the 1997 East Asian crisis. Lula took over, leftist took over Brazil in 2002 without the military intervening which was a first in Brazil. Last time this had happened was in 1964. When president Jоão Goulart had taken over the presidency and he was quickly pushed out by a military coup which stayed in Brazil for about 21 years after that. There was lot of maturation of institutions and policies of the economy also during the years preceding 2002. There was central bank autonomy, fiscal responsibility legislations, flexible exchange rate, redistribution programs that reached to 12 million people and very steady improvements in social indicators like life expectancy, education, nutrition and others. There were very dramatical improvements. So, I can understand in 2001 why one could feel optimistic about Brazil. But let us look at the record of the last 120 years, between 1900 and 1940 the per capita income doubled. Between 1940 and 1980 that was what Rakesh was referring to, there was a period of very high growth, the per capita income quintupled. 500%. Then between 1980 and 2020 the per capita income increased by 30% of which over 80% of this 30% happened during the Lula regime between 2003 and 2010. Finally, if you look at the recent past between 2014 and 2021 the per capita income declines by 7%. And even before covid there was already decline in the per capita income. So, if you divide the last 120 years into groups of 40 years, the first 40 years of the 1900s were very positive. It was a very meaningful achievement. The following 40 years were what Rakesh had described, the amazing growth. In the 1980-2020, it was the fall of Brazil's economic growth. There were reasons which led to the growth in the first 40 years, which have to do with the end of slavery, the investment in infrastructure, particularly railways, growth of coffee production and immigration from Japan and Europe which was a boost to the economy. In the following four decades there was import substitution, industrialization, large investments in state enterprises like steel, oil infrastructure, institutional modernization. But above all there was a fervor about growth. There was a governor of state of Minas Gerais who used to say 'to govern is to open roads' and he meant it both in physical sense of building roads and opening roads in terms of the economic perspective of the country. The president Juscelino Kubitschek who built Brasilia which was a bit of a disaster but nonetheless he was a very modernizing force in Brazil, wanted to achieve 50 years of progress in five. So that was the ambition. So, during this period the growth was the paramount objective. It was something governments talked about, wanted it to happen and would take any steps good and bad as we will see to make it happen. What we will focus today is mostly in the last 40 years which were very challenging. Economic instability, very adverse structural evolution of some structural features of the economy, very negative evolution in the ideas dominating policies in the economy and we will end up with some current debates. This is an illustration of what happened in Brazil's per capita income. You see a peak in 1980. Then a very slow… for15 years per capita goes up and down without much of an evolution. Then between 2011 and 2018 there is a growth of 30%. The peak that you see is in 2014 when the president Dilma was ousted for some very minor transgressions and since then the per capita income has fallen well before covid and actually under covid there was a bit of a recovery because of very expansionary fiscal policies and reduction in monetary interest rates. This will give you a comparison between Brazil, Korea, China and India. What is zooming ahead is Korea of course. Then you see Brazil which has been stagnating and China catching up and below is India. You don't see the acceleration of growth in India because of the scale of the graph. Should have done in logarithmic scale but anyway. You know more about it than is in this graph. Now, during the 40 years that we are focusing on Brazil had to face a number of macroeconomic challenges. Some were structural in nature or they were self-made and others were external shocks. The first structural one is Brazil is a dual economy. It has been a dual economy since the 1600s. The wood that gave its name to Brazil which is called Pau-brasil. And Brazil comes from grace which is red and which was a very valuable taint. So, it started with that. Then we had the extraction of gold and rubber, then sugar in the northeast, then coffee. Pretty much for a long time being an extractive agriculture and mining economy. Which meant that one sector was extremely productive and the rest of the economy much less so. Therefore, the exchange rate was determined by the advanced highly productive sector. And is something which has been a challenge in Brazil for throughout its history and particularly in the last four decades. Then the external debt crisis following the Volcker interest rates has been very damaging for Brazil. I know that many people think of Volcker as the savior of America. I think we can look at it very differently. It has sunk many developing countries and particularly Brazil. In Brazil it made sense to borrow externally to finance domestic investments when the interest rates in real terms were negative. As it went through the 60s and 70s. and then the rising interest rates in the late 70s was a tremendous shock which allied with the energy shock… the price of oil which increased dramatically… created an external debt crisis which Brazil handled poorly. Korea had to face the same situation, a public debt denominated in a foreign currency, energy shock. Brazil today is an exporter of oil. But at that time, it was an importer. But it managed the crisis much better than Brazil for reasons that you know. The result was, there was a very severe inflation under debt induced austerity. Inflation reached 70% per month. I know that in India newspapers, the media and policy makers become very nervous when inflation approaches 10%. Well, it was 70% per month. So, this gives you a sense of Brazil's external debt. What is in red is external debt in terms of GDP with a peak in 1985 and that is in blue I mean. What is in red is the servicing, the percent of exports to service that debt. Total debt. What you see in blue end which is interesting is that 2011 you have an increase in total debt. That is not public debt. It is mostly private debt. And the reason why you have private debt is that there is an interest rate differential which is very high as you will see. So, you have a lot of financial capital coming in to invest in government security or other securities. And some of it for reasons that perhaps Anoop will be able to explain the IMF has agreed to count as external direct investment. In particular into company loans in the IMF, they have now been accounted as indirect foreign investment. And when I asked…

Montek Singh Ahluwalia:

Both the graphs relate to the volume of external debt?

Roberto Zagha:

The blue is external debt as a share of GDP. And the red is the servicing of the external debt. Percent of exports. So, I asked Ranjit Teja who Anoop Singh knows extremely well, how was that IMF was allowing to count into company loans as their investments... they are like foreign investment. The answer he gave me was that nobody expected that company loans would have reached the volume that they have reached in Brazil. So, what you have in the case of Brazil is companies, state enterprises and private enterprises setting some shell company in the Bahamas, borrowing in dollars at 2 or 3 or 4% whatever the rate is and investing at 13 or 14 or 15% whatever the rate is in Brazil. And therefore, making an extraordinary profit on the way. We did some work on that and unfortunately the statistics are not very clear, but there is no question that the foreign direct investment figures that you see in Brazil are vastly inflated. Especially when you look at what happened in the real economy. It is not possible to have what is happening with the real economy with the figures that we have for a direct investment. Anyway, what this graph shows was that first of all in 1985 the crisis was public sector debt. 2011 we don't have a crisis. The foreign exchange situation is much better. But I would not feel very comfortable with the current evolution. This is the inflation rate I was telling you in 1990s the inflation rate reached extremely high levels. 2800% in 1989. And then again something like 2000% in 1994, which are extraordinarily high levels of inflation. At the same time throughout the four decades from 1980 to 2020 we see several structural weaknesses emerge in the economy. The first one is the industrialization. Manufacturing was 35% of the economy in 1980 and it is now barely 10.5%. The deglobalization, the export as a share of GDP have declined very significantly. Even though the increase is in nominal terms. When you look at the share of manufacturing in these exports the trend in deglobalization is even more serious. Decapitalization, there are some estimates showing that the current level of investment is not sufficient to cover depreciation. And the financial sector as a friend of mine would say, so much profit – so little credit. Then income inequality which has barely changed in 200 years. So, here what you have is some illustration of de-industrialization. For some reason I couldn't get from the World Bank the data until 2002 for China. But China would have started from a much higher point. But if you look at the evolution since 2000 what you see is a very sharp decline in the blue line which is Brazil share of manufacturing in GDP. The green line is Korea which has remained at a relatively high level. The purple line is India which has remained at an honorable level. I know India would like to see to have it higher. But at least, it hasn't declined. And then you have Brazil which is quite sharp and shocking reduction. Deglobalization here you have in blue. Brazil's share of exports in GDP. So, what is interesting here is that in the last few years the share of exports has increased. It has increased because with the number of crises, we will come back to it later. There has been a very significant evolution since 2017 and this has already shown its results on the level of exports. The green line is India, which was doing very well until 2012 which since then as share of exports have declined. And the red line is China, where exports as a share of GDP have been extremely high. But China has had explicit objective of redirecting its economy away from external markets towards domestic markets. So that this evolution is an objective of policy. (Inaudible question from audience) Goods and services total exports. So, this gives you the percentage of commodities in the case of Brazil in relation to total exports and what you see is a persistent increase in the level of commodity exports in the total share of exports. There were several factors that explain that. First of all, Brazil invested enormous amounts of resources in agricultural technology. There was a public enterprise called EMBRAPA. It was public resources which invested in research and development, not in diffusion of technology, but in generation of technology and vast parts of what was considered unsuitable agricultural land in Brazil all of a sudden, they became suited for soy, corn, even wheat which was unheard of in Brazil and so, Brazil had become one of the largest exporters of grain in the world. At the same time in mining that has continued an evolution of very rapid increases and then oil which was… Brazil used to be a very large importer of oil. But there were some discoveries and Brazil is now an exporter for oil. Not an insignificant one. So, the share of commodities on total exports has been increasing correspondingly the share of non-commodities manufacturing has been declining. And the problem with that picture is that agriculture and mining generate very little employment, less than 5% of the Brazil labor force works in the agriculture and mining. They are very productive because it is very intensive in capital. But the employment is very limited. Here you have a comparative view of the role of exports manufacturers in total exports. As you can see in China there is a persistent increase and now stabilization. In the case of Korea, more or less the same. A very sharp increase and then stabilization. In the case of India, it has peaked in June 2000 and now there is a slight decline. And in the case of Brazil, it is since 2000 and late 1900s there has been a persistent decline. This is a very worrisome structural trend. This gives you the figures about total investment, public and private. And it shows that in Brazil the level of investment, total investment has been declining very significantly from over 25% in 1980 to something like barely 15% a few years ago. Again, as I mentioned earlier some estimates show that this is not sufficient to cover depreciation of the stock of capital. You think that India has problem with infrastructure. This illustrates that it is a common problem in other places. This is a road that leads to the port of Paranaguά which is a big port in which exports of grain take place. This is the height harvesting season and which creates some problems as you can see. (Inaudible question) So financial sector, I think if there is one country besides US where there is financialization of the economy, that is Brazil. The financial sector accounts for 8% of GDP. The total credit that it delivers to the economy is 110% of GDP. Which is in the US you also have 8% of GDP resources absorbed by the financial sector, but the credit is 240%. Interest rates on government short term bills are the highest in the world. In the last financial sector assessment program there were some calculations, the spreads are the highest in the world. Six times higher than in the US. Nine times higher than in Europe. And also, much higher than in China and other countries like Latin America. That is reflecting the stock market. Between January 2005 and 2017, there is more recent data. But we only reached that year, the general index in the stock market went up by more than 250% whereas, the shares of financial institution went up by more than 800%. So, it is a very profitable sector which absorbs a lot of the economy but renders little services to the economy. So, these are the interest rates in real terms. The average for 2012 and 2016 and as you can see, they are simply the highest in the world. I don’t know if you can read but, Brazil is on the extreme left and then you have China, then you have New Zealand and so forth. (Inaudible question from audience) Real interest rates. This has some of the interest rates for working capital in February of this year charged by some of the major banks. You can see they vary between 6%. That is a fluke. Sometimes a bank has a very low interest rate for one reason or the other, it is only one week in February. But they go up from 14 to 34% which is very high to find investments which can have a rate of return which they can borrow. So, these are interest rates on government security. Securities you can see a peak in 1999 and then it has been slowly declining. But they remain above 10%.

Today the interest rate on government security is 13.5%. that is the central bank interest rate. The inflation rate is at 5% which means an interest rate in real terms is 8.5%. In terms of __ trends there is income inequality for the last 200 years. The data comes from the world equality indicators that PTT and others developed in the project in Luxemburg. It is 200 years and it shows the percentage of GDP for the top 10% of the income distribution. As you can see it is around 60% for the past 200 years. The blue is the bottom 50 and the green is the top 1%. So, the top 1% has more of the GDP and the bottom 50%. And that is a lot more. This is a comparison for the average for 1981 to 2021 for Brazil, China and India. The share of the top 10% is 45% in Brazil. These are the data from the World Bank which don't correspond exactly to those in the world inequality indicators. I couldn't find out exactly why. It deserves some more research. This is what the World Bank tell us. And just to illustrate the share of the 10% richest in the GDP according to the World Bank which is between 40 to 50%. That is something interesting which is, you see a decline in the last few years. This is partly due to a very significant expansion of public spending associated to covid to shore up the effects of covid on the low income groups. What you see in red is my own evaluation of… the five stars or four stars as we get very often in hotels to rate the services… of the quality of the policies. So, you have many more negative evaluations than positive evaluations. The first one is in the 1970s. the economy was still growing relatively rapidly but this was in response to what we call in Brazil the second phase of import substitution. So, in reaction to the energy crisis and Volcker monetary policy, Brazil decided to move its import substitution policies which until then had only protected consumer goods that had left pretty much open imports of capital goods, to include into capital equipment. So, there was a surge in the production of capital goods. And a loss of competitiveness, the exchange rate was over valued to protect the imports of goods and services and the result was shown in the following decades where Brazil economy had lost significant share in the exports. The second very bad idea that guided policy at that time was a pre-announced exchange rate in the 1980s. Early 1980s, from 1982 to 1985. The exchange rates were announced in nominal terms to bring down inflationary expectations. Inflation surpassed what was built in in the pre announced exchange rate. The result was a very significant appreciation of the exchange rate, currency crisis and so on. Then in 1990, there was new president. Fernando Collor De Mello who took over with the idea of stopping inflation at once. So, there was a very brilliant mathematical economist who happen to have been my professor at the university, he was a brilliant professor who was made governor of the central bank. He had a very simple program. He said inflation is a monetary phenomenon. If we freeze monetary assets inflation will stop. And therefore, he got the agreement of the president who was very concerned with his popularity and inflation. And in 1980 financial assets were frozen. So, your bank account you could withdraw a certain amount, but very minimal amount, shares in the stock market and a variety of other financial instruments were just frozen and could not be transacted. So, an interesting situation of having a truck with grains which could not pay for fuel to transport the grains from one city to the next. It just disorganized the economy completely. There was one moment of respite during a few weeks when the financial assets were frozen and therefore prices didn't go up. As soon as when this freeze was lifted the inflation restarted at even higher rates. But then, there was a very extraordinary creative plan which stopped inflation in 1994. It was a few economists, the main one being ___, who observed that there no aggregate demand imbalances. The public sector once adjusted for inflation, its surplus was relatively or the debt was relatively zero. There was no private investment to think about. And therefore, he had the idea of using the index of the CPI or the inflation index as a denominator of the __ account. And all prices in Brazil started to be denominated in both cruzeiro which was the currency at that time and this index. With that there was a certain stability introduced in this numerator which allowed transparency in prices which had been lost. And until inflationary expectations were reduced and in one day two currencies were huge and the new currency was created which is the Real which is the current currency. So, this was a very innovative and creative plan. The IMF didn't want to support it but Brazil went ahead anyway and it reduced inflation in a matter of a year. The inflation came down to very modest levels without any impact on the real economy. Because the economy was not growing very fast, but there was no negative adverse shock. Another idea that has __ macroeconomic policies is what in Brazil is called the Triad which is the combination of a primary surplus for the public sector as on objective of policy, inflation targeting together with the autonomy of central bank and flexible exchange rate with an open capital account. This was a policy which was very useful in the transition from the high inflation environment to the low inflation environment and also in the situation where Brazil didn't have very large reserves. It worked extremely well especially in flexible exchange rare. But as time went by the policy of having a primary surplus proved extremely damaging for public expenditure and public investment. Inflation target became over ambitious, the current target is 2.5% and is now 3.2 for the next year 2024 it is 3.25% and the independence of the central bank as we will discuss later is now being questioned by the new president himself. The last idea which has had a negative impact is that growth would result naturally out of small government and deregulation. It was sufficient to have a small… to reduce the size of government to deregulate the economy and growth will happen. Some of these have curbed the inflation but growth has not taken over. This is an illustration of what happened with flexible exchange rate. In blue you have Brazil, in red you have China, in grey you have India and in yellow you have Korea. In all cases you have relative stability. No big episodes of appreciation or depreciation. But in the case of Brazil, you have a very high instability. What you have is a monthly interest rate. Since January 1996, all the way to 2013, month per month inflation and so, you can imagine the life of an exporter how difficult it can be when the exchange rate is so unstable. There has been a lot of focus on fiscal adjustment in Brazil. Government in Brazil has become the source of __ and there have been very ambitious targets for a reduction of fiscal deficits without much attention being given to the role of growth. This shows you that evolution of public debt in relation to GDP in a growth scenario, with two growth scenarios. With relatively low growth, I think it was 2% and the primary deficit of 2%. One is growth, red is the growth of 2% and the green is the growth of 4% and in both cases the primary surplus of 2%. One thing which is very important for the fiscal situation in Brazil is the cost of interest rate which vary between 6 to 8% of GDP. So, this is the highest item of spending in the government accounts. But we will come back to these questions. Counterproductive ideas were several. Floating exchange rates, open capital account which has been part of the story behind the instability of the exchange rate. The country can dispense industrialization… (Question from audience unclear) Yes. Can do without industrialization. And that discussion took place also in India a few years ago. When there was a discussion whether India could grow on the basis of services alone. Another idea which has been counter productive is to have a central bank with one single objective. With the objective of low inflation without attention paid to employment and growth. One idea which has been a fiction which is the fiscal contraction can engender the expansion of the economy. Last but not least there was a constitutional amendment in 2015 which put a limit on public spending in real terms. Public spending could not grow above inflation levels. Year after years if was fixed in real terms for 20 years. Of course, it didn't work. And of course, it's been repealed. But it is another story that we will come back. An interesting development as well is when Bolsonaro our previous president was Trump on steroids. To cover one of his first decisions in January 2019 was to eliminate the ministry of planning. And one of the Lula's first decision now has been to restore the ministry of planning. Current debates which are very interesting and what I found more interesting is that we have a president who was illiterate until the age of 11, who has not gone to university and is now challenging the independence of the central bank and challenging its monetary policy. It has not always been like that way. In his first __ days he has appointed two very conservative presidents of the central bank and has never raised a question on inflation targeting. But at that time the economy was growing very fast, very rapidly and I guess he didn't pay much attention to that. But now he has been very vocal in his criticism of the high real interest rates. Questioning what the logic of inflation of 3%. Olivia Brown Shaw by the way has also been recommending targets, inflationary targets higher than the current ones. And how to contain the public debt. The 2016 constitutional amendment has been essentially diluted by number of laws and reforms and the question is what will set the fiscal angle in the future. Thank you.

Montek Singh Ahluwalia:

Thank you very much Roberto. I thought that was quite fascinating. (Break in audio) I was saying that I recommend to all the younger people to get hold of this presentation and look at all the stuff and see how much of it applies to India. Because some of the comparisons are already there. It would be very useful. Now, I think let us go to our formal discussant. That is Anoop.

Anoop Singh:

Well, I am going to be brief. Roberto possibly an old friend. We have worked on many countries together. He is given in mastery and __ could sell over the decades. I will focus only on one aspect of the situation. I am going to focus on the fiscal dilemma that Lula currently faces. And why any country whether you are the United Kingdom as you saw last year, India tomorrow or Brazil today, you can't avoid having a well designed fiscal architecture. And fiscal framework. Right now, Brazil does not have that. Brazil currently, Lula currently faces a complete dysfunctional fiscal framework. He is facing spending which is unconditional and unsustainable including on annuity subsidies. He is facing a myriad of fiscal mandates set previously or earmarks, it makes India's revenue expenditure problem look good. He faces all kinds of multiple limits on spending and rules, most of which have been periodically circumvented or changed by the last president or the parliament. That is the current situation. Lula needs to rebuild a fiscal framework. Now, before I talk on that, Lula had this problem in a different way in 2002. It is important to remember what he did then because that relates to the challenge he now faces again. In 2002 when he was becoming president markets did not believe he would be a conservative president. Especially on macro and fiscal policies. Brazil was seconds away from a debt crisis similar to Argentina only a few months after Argentina collapsed. They were literally seconds away. This was before he became president and after it became clear that he had won the election. So, he faced a challenge. How do I convince markets I do not need a debt restructuring as Argentina needs and still does today? How do I do that? The next seven years Lula then ran in my view an incredibly balanced fiscal policy especially the first five years. He essentially ran a well balanced budget, he followed primary surpluses, fiscal surpluses. He held inflation low. He kept the exchange rate under control mainly because of his fiscal framework. For the first time he bundled all the anti-poverty programs in fiscal spending he had inherited from a good government, but which he had inherited and he introduced I think for the first time Roberto conditional cash transfers into his Bolsa Familia program. Now a big comment in 2010 was by an important Brazilian, Brazil has now moved from being the 14th largest to the 7th largest economy in seven years on the Lula. The poverty rate has more than halved from 26 to 12%. The popular comment was, now that Brazil's future has arrived it will be short lived. That was the view. That is why interest rates in Brazil are so high. After Lula left and other governments took over the next president Dilma Rousseff she ended central bank independence, lowered interest rates abruptly in a way that would make even the last year's UK prime minister feel a bit envious and gave up on balancing the budget. You saw a historic economic contraction under Dilma Rousseff you have not seen before. Then came Bolsonaro. He did everything on the fiscal framework that one shouldn't do. Brazil has had multiple definitions of rules, spending limits and caps. Each time he either eroded them, exempted them or circumvented them. He also completely removed the conditional component of Bolsa Familia. He ignored the spending caps, circumvented this application. Lula now inherits a fiscal situation of spending arrears in spending what Bolsonaro committed, did not report nor they are built into the new budget. It is more than one and half percent of GDP. So, the issue now is how does Lula rebuild a fiscal framework. Now I am not trying to say Lula was the savior last time. The corruption that grew during Lula's presidency was proved to be large, but it ballooned after he left. And they allowed to develop in parliament something called a secret budget. A secret budget is something where either parliament or the government can use government spending to get legislation passed by greasing parliamentarians. This is an actual reality. So, my point is whatever else Brazil can do, whatever else Lula can do, number one for Brazil and number one for the UK now, if you rebuild a fiscal framework and how do you do that when much of Bolsonaro spending was apparently meant to be transfers to say certain sectors, lorry drivers I believe, energy subsidies, which kept inflation low, but they are unsustainable. Now they have to stop, inflation is going to rise. You need to build a new fiscal framework, how to do that. He today faces a much more difficult task because in 2002-03 he had to just convince markets he is going to be a conservative fiscal president. Now he has inherited a completely a fiscal framework and fiscal dynamics that is unsustainable. Whether or not he wants to deal with it, it is a question mark whether anyone can deal with it, without stoking public unrest. So, I would say Brazil today faces a very difficult situation on the fiscal side. My final message is whether you are UK, India or Brazil, if you develop an unsustainable fiscal framework, without sustainable fiscal rules, fiscal architecture that you follow and report transparently, your country is not able to grow then.

Montek Singh Ahluwalia:

Thank you very much. Would like a few questions from the audience and then you can respond to everything altogether? How would you like to proceed?

Roberto Zagha:

(Audio break) …requirements, some of which I fully agree with. And so, there is no point in commenting. But I think one of the main problems that Brazil has had in the last 20 years is that it became enamored with stability and it forgot about growth. So, we the ministry of planning has before being closed by Bolsonaro had lost all relevance. Because the ministry of planning was the ‘primus inter pares’ and it ceased to be that way. So, growth was a very important objective of policies and it cease to be that way. And stability was all the story. And fiscal policy became the beginning and the end of development policy. Otherwise, it didn’t matter. The fact that the country was de-industrializing, losing manufacturing exports, that the financial sector was growing at rates which were not very healthy, that credit was not expanding and so on and so forth some of the problems we saw. Didn’t attract much attention. The external investors were very happy. They were making a bundle. Even the IMF was happy. Before the crisis of 2014, I am sorry I didn’t bring the quote, but there was a quote in the article 4 of 2014, that Brazil has finally mastered its macroeconomic situation. It has created the middle class. It is poised for sustained growth and so on. I mean, I would blush had I written these words. But it was very… 2014, before which it was a peak if you remember, in the GDP graph it was a peak and then after that GDP started declining. It was entirely rosy assessment because the fiscal situation was seen as in control but as you pointed out it was built on a number of not very sound practices. I think if you have an economy where the real interest rate is above the growth rate of the economy, you can do whatever Yoga, gym flections and exercises you want, you will not be able to sustain the fiscal situation. Your fiscal architecture however cleverly designed will fail. I think what was missing in Brazil during all these years has been a strategy for growth. What it is we can debate and we can have disagreements, but the economy has not grown the last 40 years even under the best years of Lula. 30% in 10 years is much better than what had happened before. But it is not that great. 25% sorry. 30% is a total. So, we have to keep in mind that the fiscal policy is very important but that is not development. It is not sufficient for development. That is one point I wanted to make. The second point is, it is not quite like Argentina. Argentina, I am sorry to take …

Anoop Singh:

That was 2002.

Roberto Zagha:

The difference was that in 2002 Brazil didn’t have a public debt in foreign exchange whereas Argentina had committed the sin of being highly in public debt in the foreign exchange. So, that was a big difference. Otherwise, there was similarities and differences but what Brazil didn’t have was the fixed exchange rate that the fund and the government of Domingo Cavallo had implemented one to one which was… Stan Fischer had gone to Brazil and had long talks with the president at that time Henrique Cardoso, trying to persuade him to introduce… back to the dollar. And Brazil never accepted that. It was too inflexible, it was too rigid and the president at that time said we are not Hispanics, we don’t believe in rigid rules, we are Portuguese, we believe in plans. So, that is a second point. You raise a very interesting and very relevant comments, but I rather keep these two broad points.

Montek Singh Ahluwalia:

Just to stimulate the audience. I thought that was fascinating. And I just kind of inject some numbers that my friend Ayush Khare has been producing at my request while you spoke. That is going to be useful to share for the younger audience here. It is quite a dramatic picture of things going bad after 2014 which Roberto is painting. So, I thought I would throw some numbers at you which Ayush has calculated from the IMF. So, these are all IMF WAO numbers. If you look at the whole period before 2014 Brazil had an average growth rate of 4%.

And it wasn't fantastic, but its 4%. It was actually better than south Africa which was 3.4. So, I am comparing it with its other G20 developing country peers. After 2014 when all these good fiscal things were done according to both you and Anoop, the average growth rate in Brazil is a negative 0.2. Now you might say that the world also was slower and that is true. But you know, the other countries of comparison didn't have negative growth rates. Even South Africa went down to 0.6 but not negative. So, it is quite an amazing demonstration. Is Roberto right that all this fiscal rectitude that was injected into the system in 2014 was actually damaging or is he not right? This is just a set of numbers thrown at you to kind of reflect on. Now with those words let me invite you to make comments. It would be useful to make comments which seem to you to relate to issues that are relevant in India. I didn't realize by the way that Brazil had also abolished planning because you say that now they have brought I back again. Let us see if you do better. It is interesting. I am not aware of that. It was not covered in newspapers. I would have thought it quite relevant.

Roberto Zagha:

The planning function lost relevance in Brazil in terms of who was being appointed, resources, functions etc. So, when it was abolished, it was already more evolved. But now there is a very powerful, politically powerful minister, ambitious and interestingly Lula believes in planning.

Montek Singh Ahluwalia:

Now questions. Anyone who wants to ask questions raise their hands. I will call on the three people with preference given to the women. Gender equity. So big pressure on all the young ladies here to step in.

Audience: (Audio break)

This is from Divya Srinivasan. She has asked – between 2011 and 2016 based on your graph why are interest rates in Brazil so high. Shouldn't the central bank be cutting rates to incentivize investment and promote growth?

Montek Singh Ahluwalia:

That is kind of a very relevant debate going on right now. Because a lot of people say okay, so the FED has to raise interest rates, but do we have to follow suit?

Roberto Zagha:

Do we have to have other questions or…

Montek Singh Ahluwalia:

This is an interesting one. You may want to respond straight away.

Roberto Zagha:

I think whether the FED should raise interest rates or not I think has been controversial in the US and also been a controversy in Europe. it is also about what level should the inflation targets be set. There was recently in the Peterson institute a debate between Larry Summers and Olivia Brown Shaw. Larry Summers thought that if the central bank was going to loosen the inflation targets, it was a very dangerous slope whereas Olivia Brown Shaw thought it would be a very healthy slope. The arguments have to do with expectations. Now expectation is a big word because it is kind of the black box of macroeconomies. We don't always know how it is formed. We have a way of saying well their expectations have to be rational meaning that people have a model and they know the model that the economy follows. But it is not a very… it is a theoretical, elegant way of looking at rationalizing inflation targeting. But it is not entirely persuasive. So, it is the debate going on. One is inflation targets and the other is the current level of interest rates. The world economy has had a number of supply shocks. Whether it is covid related, value added chains disruption, whether it is the decline in __ in the US and Europe, a variety of shocks, the rise of energy prices and most recently the Ukraine war with its results on grain prices and energy prices. So, interest rate contain demand. And if inflation is caused by energy prices and all the supply side dimensions of the economy it is very hard to see how high interest rates will reduce the price of energy or price of grain or bring peace to Ukraine. Anyway. So, it is a debate that is going on and there are number of economists in the US that believe that there is currently a decline in inflation rates. But that is most likely due to the fact that the base is changing. And now the current inflation is being measured with prices which are higher 12 months ago than with the containment of demand. But there is a kind of religion about the terrifying effects of high interest rates. The same controversy has taken place in Brazil. It is very interesting that until Lula was elected there was no one questioning the central bank policy. Since Lula has been elected and he has very forcefully, very repeatedly said that the financial markets are very nervous nellies, as he describes them, that the same debate has taken place in Brazil. So, central bankers have a very difficult job to do in finding the neutral interest rates. This is a concept that has become very mentioned in the last few years, which is a __ rate of interest at which there are no inflationary pressures, there is high employment etc. But it is not something that you can determine empirically and you always try to find out where it is. Greenspan made its reputation on the fact that he didn't believe in macro models that the FED was doing at that time. He essentially ignored them and lowered interest rates when all the economies were recommending him to raise them. The same with Bernanke when he inundated the markets with liquidity when many economies were advising him not to do so. So, monetary policies more other than science, science can help, but Rakesh perhaps will be able to show a lot more light on this question given his experience. But we don't have a science in that. Should the central bank in Brazil reduce interest rate? Since Lula came to power a number of economists jumped to the other side of the fence where they were defending higher interest rates before December 31st and now defending low interest rates after January 1st, including the president of the central bank who is a very conservative economist.

Anoop Singh:

It is an important issue about real interest rates in countries like Brazil. What I learnt in my time working on Brazil I asked people around 2007-08 or 09, Lula has been here for four or five years. The fiscal situation is stable. Why are real interest rates so high? I was told, don't you know? I said no. They said, in countries that have had hyperinflation like Brazil has had, you will not bring real interest rates down until a generation of proper fiscal policy results. So, if you are seeing Brazil will have low real interest rates you have to wait for another 35 years and in those 35 years every year there must be sound fiscal policy. So, at that count you won't see really low real interest rates in Brazil for the next 20 years. That is my comment on that.

Audience:

(Audio not clear) … but rubber necking apart, to respond to just the two minutes that I have been here. Maybe you have covered this before in which case my apologies to you and the audience. Where are we now? I mean Brazilians have ingrained in their mind the need for primary surpluses, right? Because, all of the discussions in terms of primary surpluses unlike the discussion here which is all in terms of nominal deficits. So, is there any link between… the primary surpluses architecture presumably is debt driven or debt sustainability driven… particularly at a time when growth expectations are variable and uncertain. So, is it the case either by design or the way the economy works that chasing a particular primary surplus is a source of sustained high real interest rates? Which is not inconsistent with what I heard Anoop just say. But maybe a more structural driver of it?

Roberto Zagha:

First of all, the reason why in India the focus is on the nominal result of the fiscal accounts and Brazil is in the primary result is because the cost of interest payments on the government in India, I didn't do the recent numbers but they never surpassed two or three percent. I don't know where they are now. But a relatively modest amount. (Unclear audience comment) The point is that if you want to look at an indicator of this where the fiscal policy stands, if you look at the… when you have interest cost which amount to between 6 and 8% of GDP as they are in Brazil, the primary surplus becomes the indicator of your fiscal efforts. Real expenditures and revenue. Whereas in India, in the US when you have relatively small cost of interest rates on the government debt, the fiscal effort is already capturing the nominal accounts rather than primary surplus. So, that is why there is this pursuit of primary surplus. Which I don't think is a very healthy indicator because the pursuit of primary surplus in a situation where you have real interest rates which are… before you came, we were just talking about that… when real interest rates are significantly higher than the growth rate, you are never going to achieve that sustainability. Simple arithmetic.

Montek Singh Ahluwalia:

Any more questions.

Audience:

I think when you talk about India, India is particularly insular with its monetary policy indicators as compared to its neighboring countries. The inflation rates or the interest rates or the public debt is not really affected by the neighboring countries. But when we talk about Brazil and its proximity with its neighboring countries like Argentina and Colombia and Paraguay, because obviously when Argentina defaulted on its debt and a lot of its debt was held by foreign investors, it reduced the confidence of the investors in its sovereign bonds which had cross border spillover effects on Colombian sovereign bonds as well. So, I think that is kind of important to understand how the monetary policy indicators in Brazil are impacted by its neighboring countries. Also relevant for G20 negotiations which I think are going to be held in Brazil next year. Thank you.

Roberto Zagha:

I am no longer as familiar as the Indian economy or policy framework as I was before. So, I don't know exactly what is the degree of openness of the capital account. But in Brazil the capital account is extremely open. Private firms can borrow without authorization, without limit. At some point there were even mortgage finance being financed by external loans. So, it is a very open capital account both inflows and outflows which makes a monetary policy very… you know the impossible trilemma… very sensitive to what is happening in the US and the Europe. Whereas in India my impression is that there is a certain insulation of the capital account and therefore you don't have such impact. Which I think for a country at India's level of development is very healthy. I think all countries in the world, England, France, Italy, you name it, all European countries have opened the capital account very gradually and only in the 1980s, 1990s, whereas Brazil and Argentina opened through their capital account very early in the game which I think was very unsound.

Montek Singh Ahluwalia:

With the highest level of support from the intellectual community internationally and…

Rakesh Mohan:

I just want to comment on the last issue there. On this issue of the impossible trinity. I wrote the impossible article called – managing the impossible trinity in 2008 or so. I think the issue which you referred to as far as India is concerned is that the impossibility says you have to be at a corner of a triangle. What I was saying was you can be somewhere in the middle which is to say that your capital account is mostly open, but with certain degree of management, which IMF now calls the capital flow management. Second, the exchange rate is essentially market driven but again with a certain degree of management. If you have that you can have a relatively independent monetary policy. That is what I mean by managing the impossible trinity. I think that is to my mind countries in some sense of our level of marketisation or financial markets development etc. you need that while at the same time you want the exchange rate to be as market driven as possible but not fully. The reason for that is what you are referring to is the high volatility of capital flows so that even though our capital account is not fully open we have a large volatility to capital flows which you have seen all the time actually. So, that is sort just illustrating what you were saying.

Audience:

Thank you very much. I think I learnt a lot about Brazil and the monetary and fiscal issues accompanying. Jain, can we go to the last slide. I slipped it and I didn't go through the points. So, if we can… priorities for… current debates what should be the degree of… you see, one question that I was thinking about is when you said that the share of manufacturing has gone down in Brazil so, that takes me to Indian context where we have the share of manufacturing quite low at 16 or 17% in GDP and you also said that the mining and agricultural sectors are highly productive. So, is it that the rest of the share was taken away… I am talking about the real economy… by the services sector and the agriculture and mining? So, one of the priority areas like we have in India, would it be to take back the manufacturing share to a higher level so that it adds to growth as well as to jobs.

Roberto Zagha:

That is my conviction. Yes, I don't think Brazil can grow without having a more dynamic industrial sector and more export oriented manufacturing sector and probably a less protected manufacturing sector. There are all sorts of protection on the manufacturing sector which penalize export in particular, protection on steel, protection on very critical inputs. So, yes, absolutely I think… now how you do that is another question and whether it is technology policies, whether it is exchange rate, whether it is some strategic focus, it is another story.

Audience:

So, we in India have had a change of government in 2014 and since then we have had several landmark economic moments in the country, be it demonetization or the way we handled the covid crisis economically. What lessons or parallels do you think India can draw from Brazil's economic trajectory for its economics?

Roberto Zagha:

I would say three lessons. Number one, policy makers should not lose focus on growth. And it is essential, growth, growth, growth. The country needs a strategy for growth. And every country has to develop its own strategy. Number two, avoid the premature opening of the capital account. It is a very tempting game because there are lots of easy gains to be made in the short term but they can be very costly. And the third one, not to forget income distribution. Brazil has as you saw, income distribution has barely improved over the last 10 or 60 or 200 years. I think these are the three lessons I would draw and you can draw others, but I think that these three.

Audience:

I am an economics major student at JNU and I have a question to you sir, Anoop sir. You said that fiscal framework and architecture is important solution for the problems that Brazil had. So, can you please elaborate on that as to what are we talking about exactly given the fact that Montek sir said that the average growth rate of Brazil after 2014 was -0.2%. Given that they also had a fiscal framework. So, what exactly are we talking about?

Anoop Singh:

What I meant to say is that Lula currently faces a fiscal framework which is unsustainable, not only in terms of its spending, in terms of the architecture. So, even if government, even the new government sets targets for spending or deficits or a cap on total, on debt, it has shown the last 10 years or 15 years especially after the 2010 it can either find a way to circumvent them, redefine it. So, if you are a country where markets are not convinced that not only do you have a fiscal framework that looks good now, but will remain good 10 years from now, it is not going to work. That is the problem Lula faces now as he takes over the country.

Rakesh Mohan:

On the exchange rate actually Roberto very interesting what you are saying. That, in a sense we have a parallel problem again through the manufacturing sector. You are saying that in the case of Brazil there is mining and agriculture that is highly competitive and so you have a 'Dutch disease' equivalent. And so, the… I have not followed Brazil recently but I think your current account deficit is not too bad now, right?

Roberto Zagha:

It is not too bad, it is manageable and it is financed by "foreign direct investment" which is not that…

Rakesh Mohan:

That is not the current account. FDI won't be the current account. That will be in the capital account.

Roberto Zagha:

You are right. The current account is not bad.

Rakesh Mohan:

But similarly is the case. So, the point in some sense is, let us say in our case except for the 2013 'taper tantrum' period, 2012-13 when unprecedently the Indian current account deficit went to almost 5% or 4.5% or thereabouts, which we never had before or after historically as far as I can recall. Account deficits have been sort of around 1 or 1.5 or 2% or so and certainly, in the last 20 years except for those two or three years. So, the point in some sense is that because we also have a competitive IT sector and very roughly speaking, we have two flows on the current account which have been give or take a little bit basically 3% of GDP a year for the last 20 or 15 or so. The second is remittances from NRIs, nonresident Indians. So, you have 6% of GDP almost regular. It is amazing actually how regular this number is. Almost 6% of GDP net flows, not gross, net flows which means that you can have an 8% of GDP trade merchandise, trade deficits and still have only 2% of current account deficit. So, economy wide the exchange rate is probably ok, right? But as you are saying it is clearly biased against the manufacturing sector and the question is whether in Brazil vis-à-vis agriculture and mining, in our case services and remittances you can count that as labor services. What can one do? Because I agree with that, I am convinced in India that particularly the last 10 or 12 years that is what is really ailing our manufacturing sector which then gives rise to demands for protection from different sectors and of course in our cases currently for the production linked incentive schemes government is now giving subsidies to particular sectors. Again, I have done deep work on this which I hope you will do. My view is that that is what is leading to demand for these things for protection or subsidy. So, I don't know the answer to that. I was wondering what do we say for Brazil?

Montek Singh Ahluwalia:

Can I add a dimension to what he is saying? Has this led to a demand for what is now called industrial policy? And what is happening? What are they wanting? Because that is happening everywhere, we are seeing it, so I would like to know.

Roberto Zagha:

What I want is protection, protection, protection.

Rakesh Mohan:

What I am trying to say is that on the industrial policy at least in India, not other countries, to my mind is there isn't, because the exchange rate is structurally biased against manufacturing. Even though it may be United states economy wide.

(Unclear audience comments)

Roberto Zagha:

I think in the case of Brazil the answer is more simpler than in the case of India. I think India is more structurally complex situation and I really don't know to be honest what is the response. I see the problem, I don't see an obvious solution. In the case of Brazil, I think both mining and agriculture have huge rents. And I think it is a simple case for higher taxation which would provide in the case of agricultural products lower the domestic prices and highest consumption and less exports. You will lose exports. There is no question, in both cases. But I think that is a price to pay. It generates very little employment. It is highly productive and I don't think it will be useful to increase the levels of protection as a manufacturing associations of the north, south and the central as you want. Frankly it is very difficult when you have different sectors evolving with different levels of productivity over time. How you manage to integrate them into coherent growth framework. In the case of Brazil, I would not hesitate to have some sacrifice which I don't think it would be very serious in real terms because the profits are so enormous both in agriculture and mining that it would only have a marginal effect and certainly no effect on employment.

Audience:

To return to the earlier question about lessons for India. There are two dimensions of Brazil I knew and that is a long time ago which have stuck in my mind. One is that you seem to have at that time efficient public sector enterprises. I am talking particularly of Petrobras but there may be others as well. How are public enterprises insulated from political pressures in Brazil or is that a romantic view? Second and linked again with Petrobras is that we saw a great deal of courage from the judiciary in taking on the executive with the Jato Lavo and in what… was that a surprise to Brazilians or are there institutional protections that gave the federal courts the courage to take on the political establishment?

Roberto Zagha:

They are two very different questions. If Anoop wants to say a few words on the first one whether an efficient public enterprise... I don't know what you call efficient of public enterprises. But Petrobras has been making huge profits for the last two decades. Electrobras as well, the telecommunication companies. So, there are a number of efficient public enterprises some of which have been misused in terms of financing political parties and some corruption. So, can they be efficient? The answer is yes. They have always been efficient, I would say most of the time, yes. Have they been abused by the executive, certainly. That is one answer. The second answer… please feel free to contradict me, correct me, etc. On the strengths of the judicial institutions, I was amazed by how resilient they proved. It is a new development that both the election commission and the judiciary have been extremely firm in containing some of the abuses of the previous regime. The head of the electoral commission in my mind is a hero. He has just been extremely forceful, extremely clear and it is encouraging and at the same time I should not forget that Brazil was very close to a coup as the US was. It would have taken very little more organization and if Bolsonaro was a little bit smarter he would have engineered the coup. He was very close to doing it. Last but not least, the results of the elections, one can only be… I am very happy with Lula's victory. But it was a very marginal victory. Just barely above 1% of the total vote. Many important states are now under Bolsonaro's party. Bolsonaro's party has the largest block in congress. The political situation is not entirely in Lula's favor as we speak.

Anoop Singh:

I would not look at Brazil for public enterprise efficiency. The size of the corruption in Petrobras, in the state run construction industries and the state run development bank were historically massive. And largely explained not just Dilma Rousseff's macro policies, that largely explained the collapse of the economy in those two years. You have rarely seen such collapses as you have done in Petrobras, the construction sector and the state run development bank.

(Background discussions not clear)

Montek Singh Ahluwalia:

I can't help commenting one point. This issue of the prevalence of corruption, whenever you have an active politics, allegations of corruption are bound to expand. For example, nobody talked about corruption in China until president Xi Jinping said there is huge amounts of corruption. Suddenly we find that what was regarded as all being driven by TFBG, high levels of efficiency etc. is pervaded with corruption. So, I don't know how objective these estimates are that country X is corrupt and country X is not corrupt. The Italian public sector is notoriously corrupt.

Anoop Singh:

(Audio not enabled)

Roberto Zagha:

I don't think we can reach an agreement on that because we don't have good data. But let us leave it at suspense. But I only want to add to what Montek said. Many of the things we would say are corrupt are legal in some frameworks. We just had a bank in the US which went run out of deposits. One of the reasons for this run of deposits is a weakening of regulations. One of the reasons for these weakening regulations on this particular bank was very strong lobbying. So, this is not corruption. We had in 2008 major problems, this is not corruption. No director of bank or no CEO ended up in prison. So, we have to realize corruption is not only in public sector, it is also in the private sector. Although we don't call it that way.

Audience:

A quick question on China. Because in 2003, 2001, when the commodities boom began, both for Australia and Brazil, China was a big buyer. Both on agriculture and extractive industry especially iron ore etc. Subsequent to that I think China had made some great inroads into some Latin American economies as also some African economies. So, where is Chinese headway there today and is there a different way of looking at China by Bolsonaro's party and by Lula's party?

Roberto Zagha:

Bolsonaro hates anything which has a communist. Had a communist father, communist mother or communist grandfather or communist grandmother. So, he hated China. He wanted Brazil to move away from China but the agricultural lobby… he had very ugly words with the ambassador of China in regard of his regime, very insolent comments on China and the agricultural lobby was very efficient about bringing him to better manners. So, he wrote to China… in Brazil China cannot buy land contrary to some countries in Africa land has to be bought by nationals. The foreigners have very limited rights to land. So, it has been a flourishing relationship between Brazil and China in terms of commercial exchanges. And with Lula I don't know how it will evolve. It probably will continue to deepen. I remember that was your question.

Montek Singh Ahluwalia:

Thank you. I am going to request Rakesh to say the final words of thanks.

Rakesh Mohan:

Thank you Montek. Before I say the thanks, I want to welcome Suman Bery. I think this is the first time that you have set foot in the center for social economic progress. I don't know whether you set foot here with Brookings India. (Audio unclear from audience) That was all virtual. Setting foot here is different issue. All this is particularly valuable because he did work on Brazil for a number of years from the World Bank. So, we have a really amazing kind of discussion in that we have someone who worked a number of years… five years or four years or something like that from the World Bank and someone else who worked for a similar time but perhaps in a different period from the IMF to have commentary on Brazil. What this discussion does illustrate is the difficulty of understanding what really causes or promotes growth and development. I should have mentioned in the beginning, but now… Roberto was the secretary to the growth commission in 2010 and of course as soon a growth commission issued its report world growth started coming down after 2010. Montek, you were a member of that, right? A prominent member. Since I am also guilty of doing many reports, this is a real problem of doing a report. But I don't have any idea of the efficiency of Brazilian public enterprises etc. The only thing I would say is that there is no question that Petrobras was really full of corruption to the extend that it spread throughout Latin America including Peruvian presidents who are in jail and so on.

Roberto Zagha:

It was construction company. It wasn't Petrobras.

Rakesh Mohan:

But it was connected with Petrobras. No? Okay. I take that back, sorry. Actually, it isn't. but the issue of corruption is interesting in that it sorts of went across, beyond borders actually. So, not just proven but I think others have also been implicated. I think almost all the last… if I am not mistaken… four or five Peruvian presidents, not for this, but are in jail. Or have been in jail. And the second last one actually is in house arrest for the last three years. I think, he was also a member of your commission. Pedro Pablo Kuczynski, he had been a minister of finance earlier. So, I am just saying this to say that somethings that has happened in the last maybe 20 years in the world that corruption has become large and across borders. I don't know how much impact that it has on efficiency etc. I just want to say that comment. Really utmost thanks to Roberto for giving us the time on a subject one wouldn't really otherwise think about. I think that it is important for us to both look at what were the reasons behind Brazil's very high growth for a long period of time and it was just about like Japan for quite some time. And how it has then come down which Roberto has illustrated. Also, this whole issue that was… we didn't have a conclusion… on macro policy both fiscal and monetary. My view that it is much more to do with… it not a 'zero one' thing in terms of whether you have a conservative fiscal policy or a non-conservative. The real question is what policy. And same thing with interest rates. It is not a question that high interest or low interest. Question is how high and how low actually. But I think that this discussion went far beyond Brazil but really talking about key issues to do in terms of a macro level thinking as opposed to sectoral on how you promote growth and development. I will end by saying that the last point that Roberto made was that I think in almost all high growth experiences we have had, whether it is China, whether it is Brazil, whether it is Japan, whether it is Korea, very high top post level emphasis on growth, growth, growth. But along with inclusion etc. But growth, growth, growth. That I think again is an issue that is worth talking about. Once again thank you and Montek thank you so much for chairing this.

Montek Singh Ahluwalia:

I am going to exercise chairman prerogative to say the last words.

Rakesh Mohan:

So, I will just thank everyone and sit down.

Montek Singh Ahluwalia:

I think the point that Roberto made about corruption and I think the bank you were referring to is the SVB, right? The Silicon Valley Bank. That is not a word you normally associate with corruption, but there you are. It is very interesting to think back on the 2008 crisis in the United States spread into Europe. A lot of people said that huge amounts of profits were being shown as a result of very dubious kinds of financial innovation. These profits were actually part of the GDP of the United States. Now since 40% of corporate profit was in the financial sector in the US and corporate profits are an important part of GDP and this was the thing that was growing. In effect what happened was at a certain point these things were called balance sheet problems. And the US government stepped in in whatever ways to save the balance sheet of the banks. But had this been public sector all the stuff that was siphoned off would have been called corruption. It is not called corruption. In the United States it is called a little bit of excessive enthusiasm and what have you. The bottom line is that the money that got lost from the balance sheets of the banks and had to be replaced by taxpayers actually ended up in somebody's profits, somebody's bonuses, etc. That is what led to Christine Lagarde. Who, I mean all said and done being a French… all French people are socialists a little bit? She is the one who said that all this happened and no one went to jail. So, I mean she was talking back to that and the notion that… there is no doubt that when you have public sector you should look for corruption. The incentives are there. But the idea that it doesn't exist in the private sector is I think a little mistaken. In terms of growth impact… I mean there was a French guy in the IMF I forget the name. Anoop will probably know the name. Used to work on the national accounts team. And he said that the IMF if it was serious should not simply view the hole in the balance sheets of the banks as a one-off problem. They should go and revise the GDP growth rate of the United States during that period when my good friend Larry Summers and others were claiming that financial liberalization was contributing to growth in the US that actually wasn't doing anything of that kind. Just a thought, all you young people need to go and think about. May I add my words of thanks for Roberto. Thank you.

Roberto Zagha:

I want to thank you very much for the invitation.