

# BRAZIL

## Key conditions and challenges

**Table 1** 2020

Population, million	212.6
GDP, current US\$ billion	1424.6
GDP per capita, current US\$	6702.2
International poverty rate (\$ 19) <sup>a</sup>	4.6
Lower middle-income poverty rate (\$3.2) <sup>a</sup>	9.1
Upper middle-income poverty rate (\$5.5) <sup>a</sup>	19.6
Gini index <sup>a</sup>	53.4
School enrollment, primary (% gross) <sup>b</sup>	132.5
Life expectancy at birth, years <sup>b</sup>	75.7

Source: WDI, Macro Poverty Outlook, and official data.

Notes:

(a) Most recent value (2019), 2011 PPPs.

(b) Most recent WDI value (2018).

After a strong contraction in the second quarter of 2020, Brazil's recovery was supported by large fiscal stimulus, limiting the annual contraction to 4.1 percent. Recovery momentum is expected to propel growth to 3.0 percent in 2021, but the upsurge of Covid-19 cases raises downside risks. Poverty will likely rise with more limited fiscal support and as the labor market remains soft. The government must find a balance between effective social protection and a sustainable fiscal framework, while re-launching the structural reform agenda.

In the last decade, the Brazilian economy grew by an average 1.4 percent per year (0.6 percent per capita). Most of the growth in the past ten years was driven by favorable demographics, while total factor productivity declined due to structural bottlenecks, such as a complex tax system and a cumbersome business environment that discouraged entrepreneurship. Despite promoting important projects like the labor and pension reform, a new legal framework for sanitation, changes to the bankruptcy law and the independence of the Central Bank, human capital progress was slow and the state intervention policies in specific sectors were ineffective. The public budget was under increasing pressure from the high level of mandatory current expenditures and increasing pension obligations. The economy was still recovering from the deep recession of 2015 and 2016 when it was hit by the Covid-19 crisis. Uneven income growth, declining incomes of the poorest 40 percent and households in lagging regions falling further behind led to higher poverty and inequality levels than those following the 2015/16 recession. The crisis aggravated Brazil's challenges in poverty reduction. The large federal fiscal response through the direct transfer program *Auxilio Emergencial* (AE) led to a decrease in poverty and inequality in 2020, thanks to the broadened inclusion

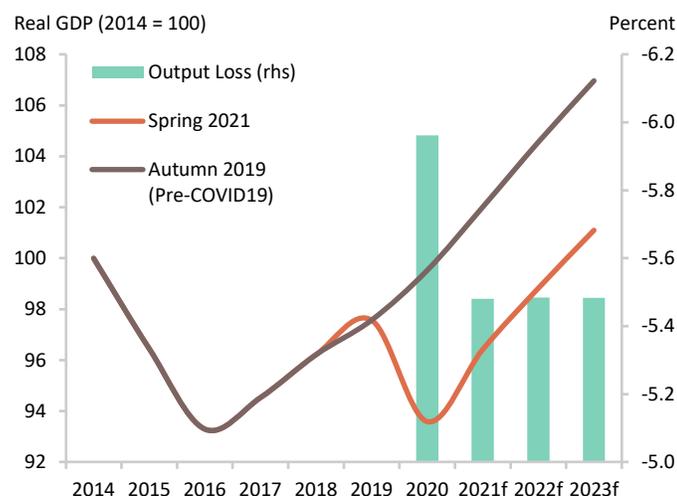
base and high amount of transfers (up to 750 USD equivalent in total).

A successful vaccination campaign is critical to overcoming the health crisis and recovery in the services sector. Other needed reforms include trade liberalization, privatization of public enterprises, the tax system, flexibilization of the public expenditures and public servants' career.

## Recent developments

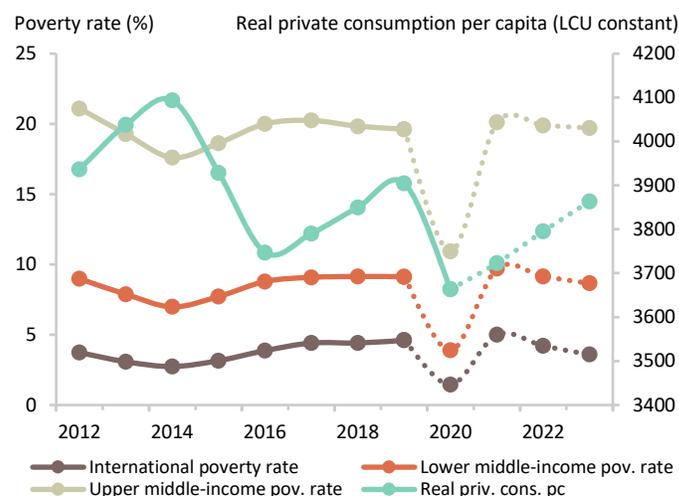
Brazil's economy contracted by 4.1 percent in 2020. The AE program launched in March cushioned the plunge and supported a consumption-led recovery, further aided by lower interest rates, job sustenance programs and the easing of social distancing measures. Industry and retail sales followed suit, exceeding pre-Covid levels by end-2020. Meanwhile, services, that are important for job creation, remain weak as Brazil's high virus case count continues to affect face-to-face activities. Agriculture expanded considering soaring commodities prices and a weakened exchange rate. The labor market deteriorated, with unemployment climbing 2.3 p.p. reaching 13.9 percent in December. Labor force participation fell by 6.8 p.p. between December 2019 and September 2020, recovering by 1.7 p.p. by December 2020 (to 56.8 percent). More than 6mn people lost their jobs in 2020 and most of them gave up looking for a job. Among women, one in five were out of the labor force, due to the need to take care of relatives or housework.

**FIGURE 1 Brazil / Revisions to Brazil's GDP growth forecast, compared to last MPO**



Sources: WB staff calculations.

**FIGURE 2 Brazil / Actual and projected poverty rates and real private consumption per capita**



Source: World Bank. Notes: see Table 2.

The current account deficit narrowed from 2.7 percent in 2019 to 0.9 percent in 2020, due to a steep fall in imports, but FDI flows held up. Inflation accelerated in the second half of 2020, as food prices increased by 15 percent given the increase in commodity prices and the exchange rate depreciation. Nevertheless, the shock is considered temporary, as inflation expectations are well anchored.

The fiscal expansion of 11.2 percent of GDP led the primary deficit to rise from 0.8 percent of GDP in December 2019 to 9.5 percent in 2020. Accordingly, public debt jumped to 88.6 percent in 2020.

The pandemic effects on the labor market led to a fall on households' labor income that was felt across the income distribution. In contrast, the increase in social transfers (with AE representing over 40 percent of households' income for those in the bottom quintile in November) led to a projected decrease in poverty to 10.9 percent (for US\$5.5, 2011 PPP line), and 1.4 percent (or 3.2 million people) living in extreme poverty (US\$1.90 PPP).

## Outlook

Covid-19 erased income gains since the last recession in 2016. In 2021, a partial GDP recovery of 3.0 percent is expected, as the carryover is high, and growth likely resumes its pre-Covid pace. Industry will lead the recovery, while the services sector will be dragged down by the activities whose performance depend on the vaccination program. The vaccination campaign is expected to accelerate throughout the year. Mining and agriculture growth will be supported by improving external conditions. The recovery underway is expected to continue into 2022 with 2.5 percent growth, before the economy converges to a 2.3 percent rate from 2023 onwards. Poverty reduction is expected to be limited. The expiration of the AE in December 2020 is expected to decrease households' income, especially for those at the bottom of the distribution. Without the labor market absorbing discouraged workers and the unemployed, labor incomes will stall

and the reduction in poverty is likely to remain temporary. In 2021, poverty rates (at \$5.50 2011 PPP) are projected at slightly higher levels than before Covid-19 and return to 19.7 percent in 2023. Inflation is expected to return to the official target in 2021, as exchange rate related shocks dissipate, while primary deficit decreases to 2.4 percent. Total gross debt will reach 89.7 percent, and further fiscal adjustment will be required to comply with Brazil's expenditure rule.

Risks to the recovery continue to be high. Should the AE transfer program be renewed, currently under discussion in Congress, it will likely increase the primary deficit in 2021, support household consumption and soften poverty increase. The resurgence of the pandemic is leading some local governments to impose new lockdowns, which may slow the pace of recovery. The pace of recovery in the labor market is a risk as job creation depends on a sustained demand recovery scenario and on the implementation of structural reforms, both to boost potential growth and to promote fiscal consolidation.

**TABLE 2** Brazil / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2018	2019	2020 e	2021 f	2022 f	2023 f
<b>Real GDP growth, at constant market prices</b>	1.8	1.4	-4.1	3.0	2.5	2.3
Private Consumption	2.4	2.2	-5.5	2.3	2.6	2.4
Government Consumption	0.8	-0.4	-4.7	0.0	0.0	0.0
Gross Fixed Capital Investment	5.2	3.4	-0.8	5.1	5.1	4.7
Exports, Goods and Services	4.1	-2.4	-2.2	5.0	5.0	5.0
Imports, Goods and Services	7.7	1.1	-10.2	6.0	6.0	6.0
<b>Real GDP growth, at constant factor prices</b>	1.7	1.3	-3.8	2.9	2.5	2.3
Agriculture	1.3	0.6	2.0	1.5	1.6	1.5
Industry	0.7	0.4	-3.5	5.5	1.9	1.8
Services	2.1	1.7	-4.6	2.2	2.8	2.5
<b>Inflation (Consumer Price Index)</b>	3.7	3.7	3.2	5.4	3.5	3.4
<b>Current Account Balance (% of GDP)</b>	-2.2	-2.7	-0.9	-1.5	-2.1	-2.5
<b>Net Foreign Direct Investment (% of GDP)</b>	4.0	2.5	3.5	2.6	2.6	2.6
<b>Fiscal Balance (% of GDP)</b>	-7.5	-6.6	-14.2	-6.2	-6.8	-6.4
<b>Debt (% of GDP)</b>	75.3	74.3	88.6	89.7	91.1	92.5
<b>Primary Balance (% of GDP)</b>	-1.6	-1.0	-9.5	-2.4	-1.3	-0.8
<b>International poverty rate (\$1.9 in 2011 PPP)<sup>a,b</sup></b>	4.4	4.6	1.4	5.0	4.2	3.6
<b>Lower middle-income poverty rate (\$3.2 in 2011 PPP)<sup>a,b</sup></b>	9.1	9.1	3.9	9.7	9.1	8.7
<b>Upper middle-income poverty rate (\$5.5 in 2011 PPP)<sup>a,b</sup></b>	19.8	19.6	10.9	20.1	19.9	19.7

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.

Notes: e = estimate. f = forecast.

(a) Calculations based on SEDLAC harmonization, using 2013-PNADC-E1, 2018-PNADC-E1, and 2019-PNADC-E1 Actual data: 2019. Nowcast: 2020. Forecasts: 2021 to 2023.

(b) Projection using point-to-point elasticity (2013-2018) with pass-through = 0.87 based on private consumption per capita in constant LCU.

Estimates for 2020-2021 based on microsimulations to reflect emergency policy measures implemented in 2020.