Why is Brazilian productivity so low?

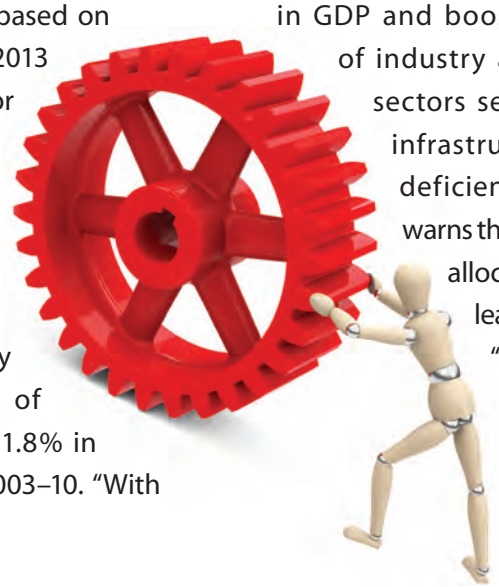
With the workforce likely to be smaller as the population ages, the need to raise productivity becomes increasingly urgent if Brazil's economy is to grow sustainably without inflation.

Thais Thimoteo

FOR DECADES LOW PRODUCTIVITY has been responsible for the poor performance of Brazil's gross domestic product (GDP). Today, increasing productivity—which rebounded slightly last year but is still far from stellar— is more urgent if the country wants to achieve more robust economic growth without pressure on wages and inflation, because the labor force is expected to decline as the population ages.

In 2013, unemployment averaged 5.4%, according to the Monthly Employment Survey (PME) of the Brazilian Institute of Geography and Statistics (IBGE). This is the lowest annual result ever. But a recent study by Fernando de Holanda Barbosa Filho, researcher, Brazilian Institute of Economics (IBRE), based on IBGE data for 2002 through 2013 shows that growth in total factor productivity– the measure of the efficiency of all inputs, labor and capital, to GDP— fell to 0.4% for 2011–13 after averaging 1.7% for 2003–10. Growth of labor productivity alone was a milder version of the same pattern, averaging 1.8% in 2011–13, down from 2.2% in 2003–10. "With the same factors of production as before, we are producing fewer goods and services than before," says Barbosa Filho. "Last year, the weak recovery in total factor productivity of 0.8% was not sufficient to make up for the loss of 0.9% in 2012." Alcides Leite, professor of economics at Trevisan Business School, explains that "Brazil has grown in the past decade because there were a large number of unoccupied workers. When these workers were put to work, total production grew. In order to sustain long-term growth, Brazil now needs to make a quantum leap in productivity."

To do so, in addition to fostering innovation, increasing investment, and improving workers' skills, there is a need to reduce the weight of less efficient sectors like services and commerce in GDP and boost the productivity of industry and agribusiness— sectors seriously affected by infrastructure and logistics deficiencies. Barbosa Filho warns that resources are being allocated to precisely the least productive sectors: "When the services sector expands, the result is to reduce total productivity."



David Kupfer, a member of the Group of Industries and Competitiveness of the Institute of Economics of the Federal University of Rio de Janeiro (UFRJ), has a different view. He believes that economic growth raises productivity rather than the contrary, because the labor market is less elastic than production. "If GDP grows 3%, for example, employment does not grow to the same extent, increasing productivity. In contrast, when the economy shrinks, businesses do not lay off workers immediately, and productivity falls," he explains. "It is natural that entrepreneurs are more willing to invest when the economy is doing well, which raises productivity," adds Julio de Almeida Gomes, former Secretary of Economic Policy of the Ministry of Finance and now professor of economics at the University of Campinas (Unicamp).

Kupfer also points out that labor productivity is being affected by high turnover of workers, who have little incentive to stay in a job when the booming labor market presents plenty of job opportunities. He says, "The high turnover of workers is a plague . . . workers quit their jobs more easily because they receive other offers. So companies have no reason to invest in training to improve worker skills and productivity."

In order not to lose workers, the Brazilian company TOTVS, developer of integrated management systems, trains its professionals regularly. The company believes that investing in people and innovation must be done by any company that intends to be competitive enough to establish itself in the international market. "Obviously we have structural problems that the government needs to address, but if we sit around waiting for them to be solved, we get nowhere. We also have an obligation to invest in our businesses. If I want to differentiate myself, being competitive I need to invest. Nothing is free," says Alexandre Mafra, TOTVS financial executive vice president. The company now has 26,000 customers and affiliates in Argentina and Mexico in addition to a research lab in Silicon Valley. Mafra explains that especially for information technology, productivity as a result of innovation is essential to business success because software systems become obsolete quickly.

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> *Fernando de Holanda Barbosa Filho*

Unicamp's Gomes believes the most effective way to increase productivity and competitiveness is to expand company operations in overseas markets as TOTVS has done. "Our companies need to be more aggressive regarding exports and internationalization so that they acquire the innovation DNA from their experiences abroad, where competition is fierce," he emphasizes.

Confidence down

Unfortunately, industry does not have the drive to invest today. With manufacturing nearly stagnant since 2010, business confidence is at its lowest, according to surveys of the

Brazilian Institute of Economics (IBRE) and the National Confederation of Industry (CNI). "In addition to low business confidence, the inability of industry to invest is also coming from competition between our domestic products and those imported, which does not allow industry to raise prices to cover their increased costs," notes Renato Fonseca, CNI research manager.

Moreover, industry must also compete for workers with the service sector. "Because of the strong growth of the services sector, we are being forced to hire professionals who are poorly educated, and to keep them on the job it is also necessary to provide wage increases and other benefits. All these costs ends up exceeding productivity gains," Fonseca says. A CNI survey shows that increases in wages have outpaced growth in manufacturing productivity. From 2001 to 2012, productivity grew by only 1.1%, while the average pay in dollars for industrial workers rose 169%, which undermines industry's external competitiveness.

How to increase productivity?

IBRE researchers Regis Bonelli and Julia Fontes call the problem of productivity in Brazil "the long-run challenge." According to their estimates for 2012–22, the Brazilian economy will be able to grow 4.4% a year only if productivity increases by 3.4% annually. Sustaining such high productivity growth will require a tremendous effort in terms of research and development of products, investment in education, and improvement of infrastructure.

Here Barbosa Filho points out that government policy may be suppressing productivity growth. Granting tax exemption to companies that are not in good shape economically only postpones their demise. "Policies that support noncompetitive companies do not provide incentives for these companies to make the changes necessary to improve their productivity. In general, recessions eliminate unproductive companies. But if you save them all, you can slow down the

Brazil's productivity fell in 2011-13.

Labor productivity		
Year	LP	Change in %
2002	100.0	
2003	98.7	-1.3
2004	102.5	3.9
2005	103.2	0.7
2006	106.0	2.7
2007	110.2	3.9
2008	113.5	3.0
2009	112.4	-1.0
2010	118.4	5.4
2011	121.4	2.5
2012	122.1	0.5
2013	125.0	2.4

Labor productivity	
2003-10	2.2
2011-13	1.8

Total factor productivity		
Year	TFP	Change in %
2002	100.0	
2003	98.5	-1.5
2004	101.3	2.9
2005	102.0	0.7
2006	104.6	2.5
2007	107.7	3.0
2008	110.5	2.6
2009	110.8	0.3
2010	113.9	2.8
2011	115.4	1.4
2012	114.4	-0.9
2013	115.3	0.8

Total factor productivity	
2003-10	1.7
2011-13	0.4

Sources: Brazilian Institute of Geography and Statistics, Fernando de Holanda Barbosa Filho estimates.