

Hope in the future

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TREASURY SECRETARY ARNO AUGUSTIN is optimistic about Brazil's fiscal situation. He notes that the country's net debt declined from 60% of GDP in 2002 to 34% last year and state debt fell from 20% of GDP to 11%. He believes 2015 will be a year of good growth for the country, the favorable trend of fiscal indicators will continue, and the effect of the international crisis will probably be lower. "We are very confident about the fiscal situation for 2014," he says. He is reassuring, stating that the tax benefits and incentives necessary because of the international crisis are over with and in 2014 there will be no new ones. Also, the Treasury will not be transferring significant resources to BNDES or capitalizing state-owned banks. Augustin does report that the Treasury will provide US$1.7 billion to help electricity distribution companies withstand the effects of increased costs due to the prolonged drought. In general, he believes, Brazil can view the future with more confidence.

***The Brazilian Economy*—Considering the very weak economy, what steps does the Treasury plan to take?**

Arno Augustin—We are working with a recovering economy that grew by 2.3% in 2013, a much better result than in 2012. Production of capital goods is recovering. Tax revenue is getting better … . We are very confident about the fiscal situation in 2014. The benefits and incentives the economy needed to cope with the international crisis are over with and for the current year there should be no new benefits and incentives. This certainly will be reflected favorably in tax collections.

How do you think foreign investors view the government's policies?

Foreign investors have seen Brazil very positively; they hold an increasingly larger

share of domestic debt. This means that they trust [the government], and see a country with strong fundamentals.

A cut in public spending was recently announced. Was it positive? How do you see the downgrade by Standard and Poor's (S&P)?

S&P's decision to change the risk rating for Brazil is inconsistent with Brazil's solid fundamentals. S&P itself highlights clearly Brazil's many positive points: its solid institutional structure; the soundness of public accounts, both fiscal and external sector; the composition of public debt, which is almost entirely in local currency and mostly with fixed interest rates or indexed to inflation; and a manageable level of net external debt. The government reaffirms its commitment to meet the fiscal primary surplus target of 1.9% of GDP this year, continue with fiscal consolidation, give priority to investment, and work for sustainable growth.

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Some say that we have a structural fiscal problem. What is your view?

The main government expenditures are under control and falling. That is the case for wages, interest payments, and social security pensions. Spending on wages and salaries fell from 4.9% of GDP in 2002 to 4.3% in 2013; interest on public debt declined from 7.7% of GDP in 2002 to 5.2% in 2013. The social security deficit is also diminishing. Revenues from concessions and dividends are recurring revenues; they were treated as primary revenues in 2013 and will be so treated in 2014. Dividends rose sharply because state-owned enterprises today are performing better. … We have been able to increase revenue with lower tax rates and reduced taxes; this is an ideal situation. … The same goes for expenses. The expenses that have grown are education and investments. Fortunately, those types of investment have a favorable economic effect. This year and next year, we'll have stronger participation of private investment from concessions without fiscal cost to the government. The concessions for ports, highways, railways, airports, petroleum, and electric power mean a significant improvement in terms of more investment and better infrastructure, at no fiscal cost.

But what about productivity and competitiveness?

The competitiveness of the economy was one of our biggest concerns. … The government promoted the exchange rate devaluation, which in the beginning is not good but in the medium and long term is positive for the economy; a decrease in interest rates; and exemptions from payroll taxes that will have a significant effect in terms of improving company competitiveness.

This year interest rates have gone up somewhat and the expectation of both the Central Bank of Brazil and the U.S. Fed is for higher interest rates in 2015. How will public debt and the primary surplus be affected in this scenario?

The main effect of U.S. interest rate changes on Brazil's domestic interest rates has already occurred. The U.S. increase was intense in 2013. … From now on we should see some increase in U.S. rates, but much smaller. For Brazil, I think the level of the interest rate in general is better. The rate has a tendency to fall and that is what will happen. Net public debt has fallen from 60% of GDP in 2002 to 34% in 2013.

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The National Development Bank (BNDES) has expanded its loans significantly in recent years. How should it behave in the future?

The BNDES transfers funds from the government to the private financial system at lower interest rates to support economic policies. … The government opted to transfer to BNDES significant resources to support private investment. The main BNDES operation is the Program for Investment. The BNDES has significant resources at its disposal, and we hope that the international crisis recedes. … What had to be done has been done and for 2014 there should be no significant transfers to BNDES or capitalization of state-owned banks.

How do the measures in the energy sector affect the public budget?

Because the Brazilian electricity system has been suffering from a very severe drought, currently it has lower production of hydroelectric power. This has had a heavy economic impact. …The Treasury will contribute US$1.7 billion and seek funding in the market so that distribution companies can pay their commitments until electricity rates are raised next year.

How does the Treasury contribute to the good performance of the Brazilian economy?

Our role is to work to improve Brazil's economic fundamentals. We have to ensure that the government has solid medium- and long-term fundamentals; better debt management and public bonds to improve the conditions under which Brazilian companies borrow funds abroad. We also have to control public spending and track state finances. Ultimately, the Treasury does all this fiscal analysis to build a framework for medium- and long-term fiscal sustainability. ■