

Macroeconomic Impacts of an Employer of Last Resort Policy in Brazil

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The Hyman P. Minsky Summer Conference June 27-29, 2010



Paper Outline

- The favorable economic environment in Brazil: Things have changed.
- Despite the favorable economy, some things may never change.
- The Case for an Employer of Last Resort in Brazil.
- Macroeconomic Impacts



INTRODUCTION

- Brazil has been experiencing a favorable macroeconomic environment:
 - Monetary
 - Sovereignty, non-convertible currency (since Jan 1999)
 - External net creditor
 - Macroeconomic stability
 - Growth based on domestic expansion
 - Healthy financial system



BRAZIL IS NOT THE SAME, THINGS HAVE CHANGED...

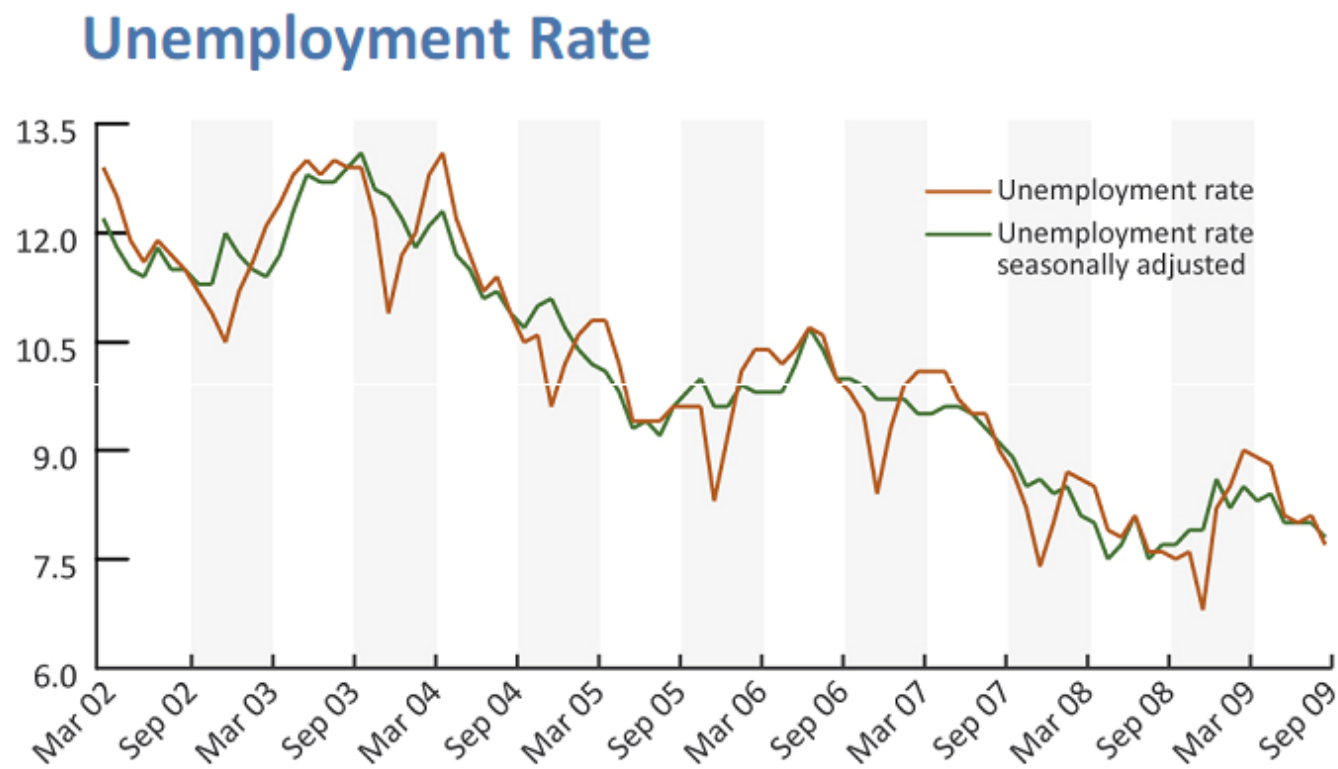
- Historically Low Unemployment Rates.
- Historically Low Interest Rates.
- Reduced External Vulnerability - Net External Creditor.
- Economic Growth primarily based on the expansion of domestic consumption and investment.



BRAZIL IS NOT THE SAME, THINGS HAVE CHANGED...

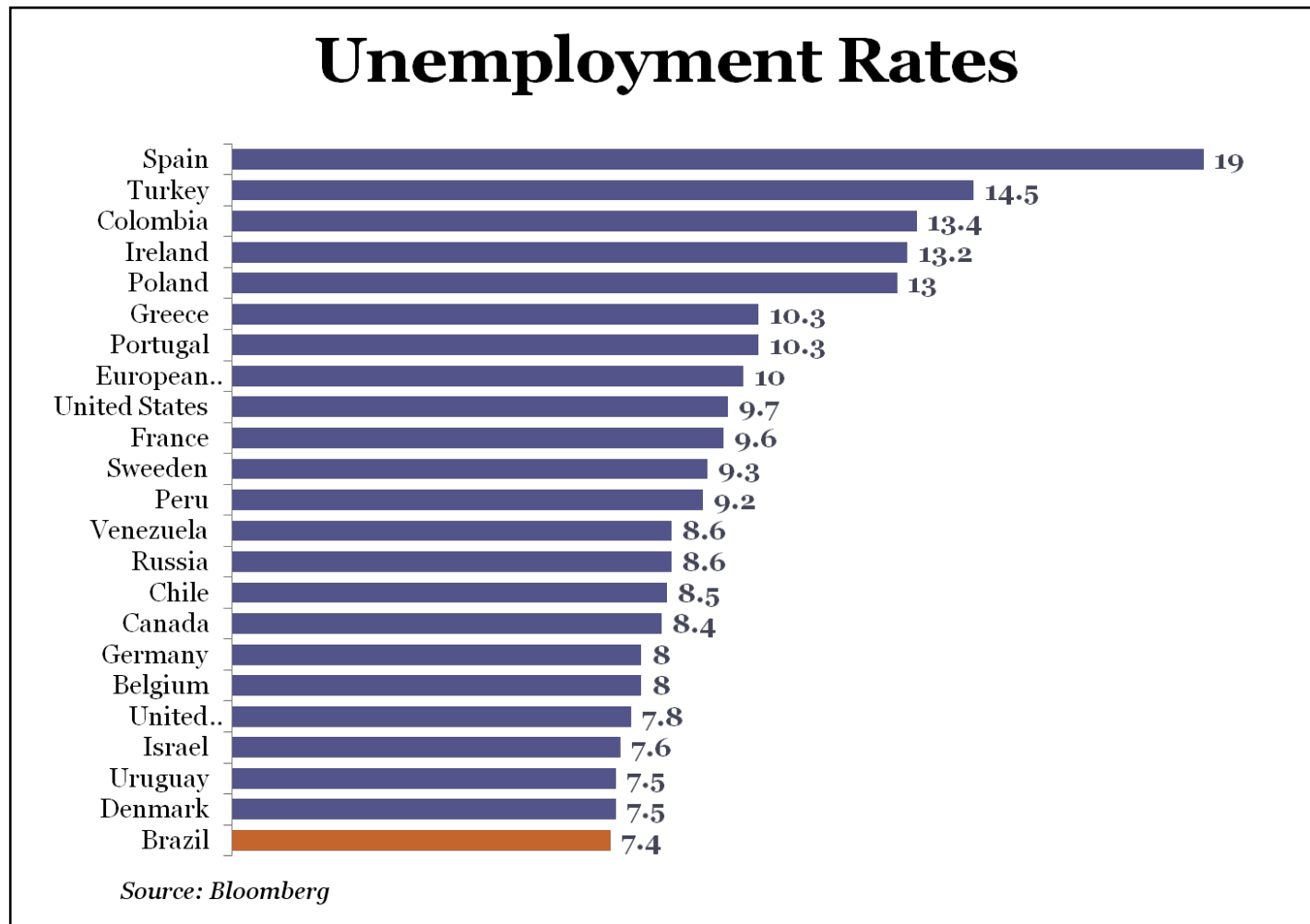
- Increase in real incomes (wage and salaries).
- Credit Expansion (mainly consumption, auto and housing).
- Improved income distribution (middle class is increasing +25 M people between 2003-2009).
- Active role played by the Government (PAC, social programs, state enterprises, public banks, etc).

- Historically Low Unemployment Rate.

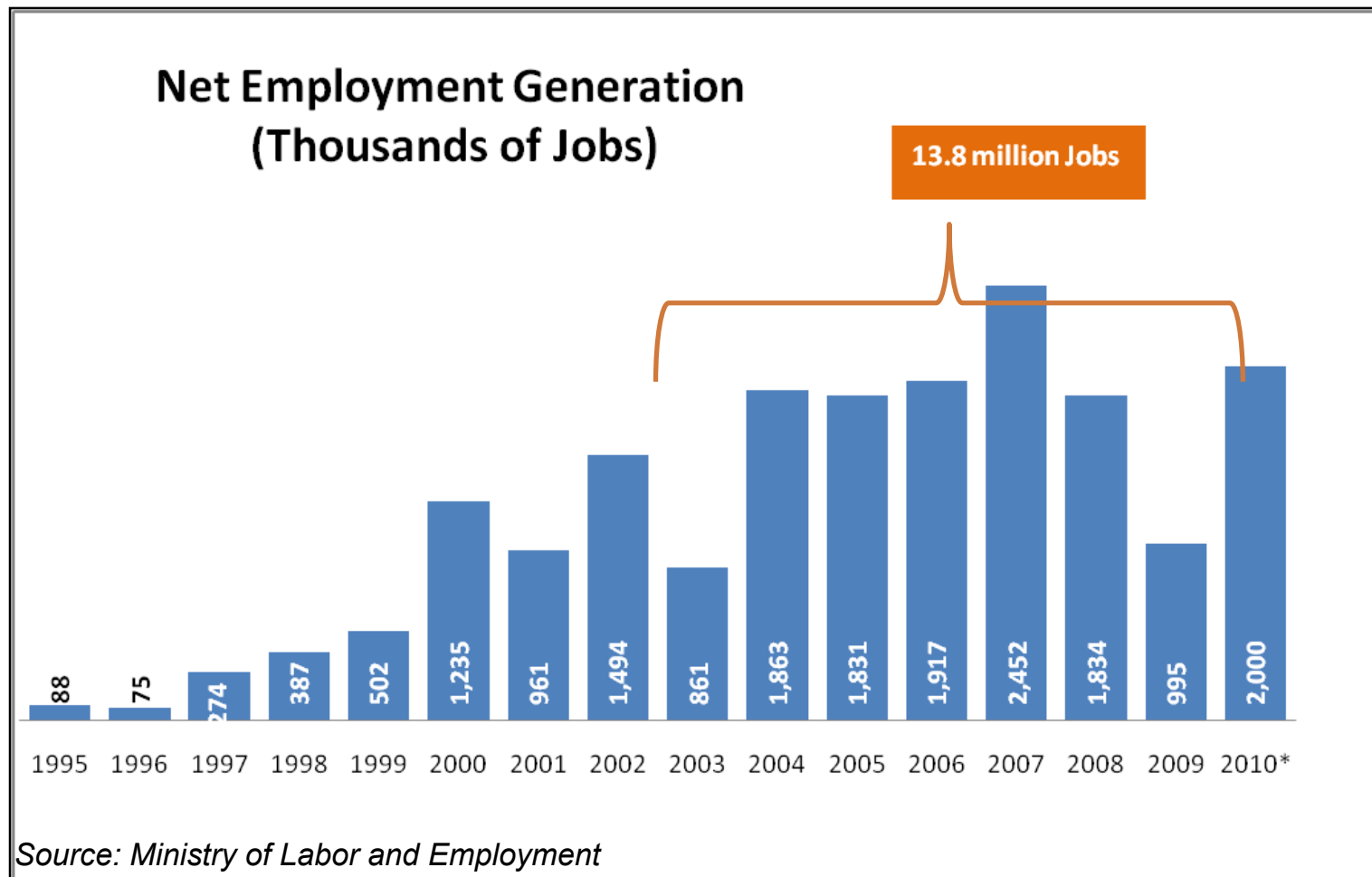


Source: IBGE

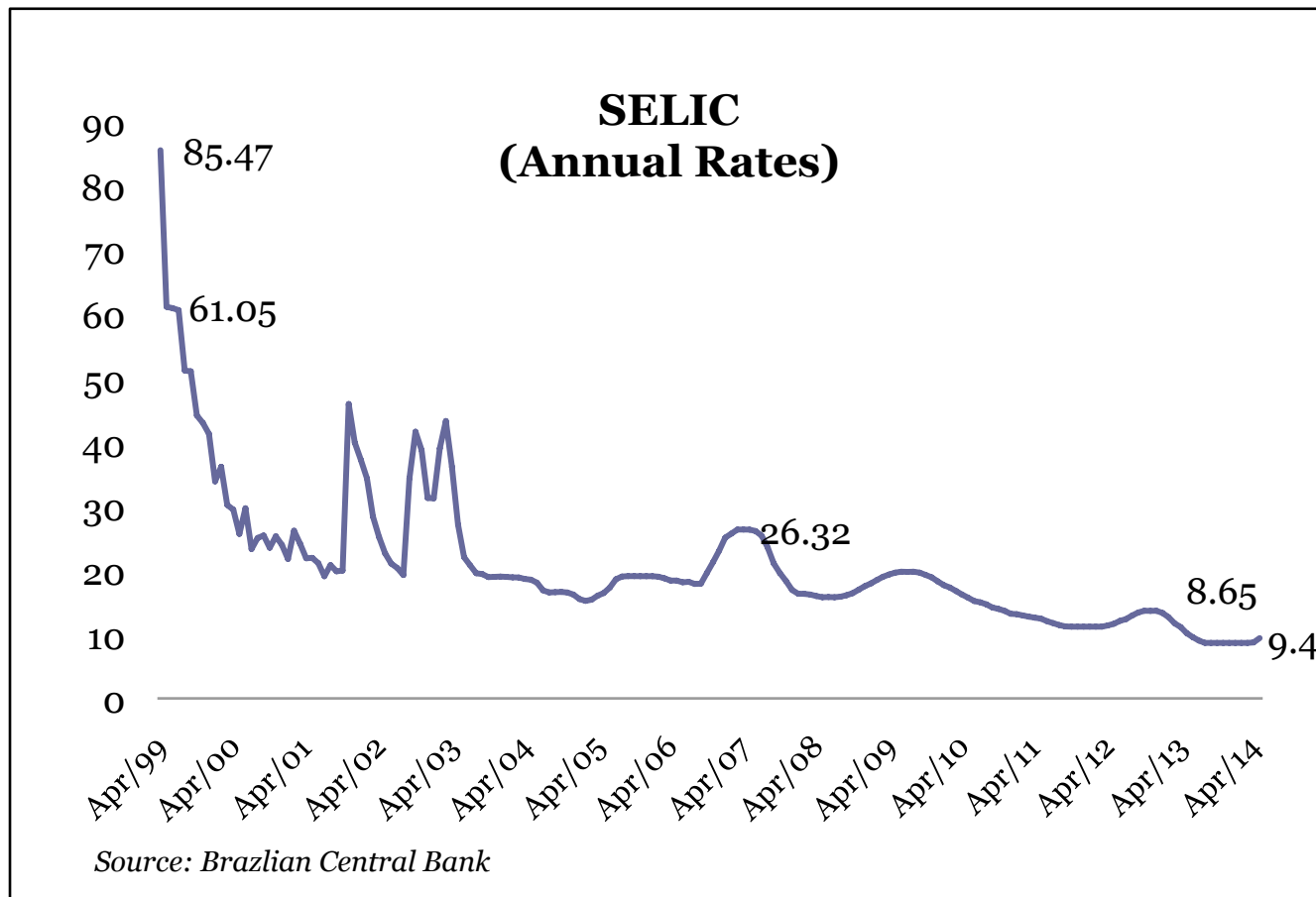
- Low Unemployment Rate compared to other economies



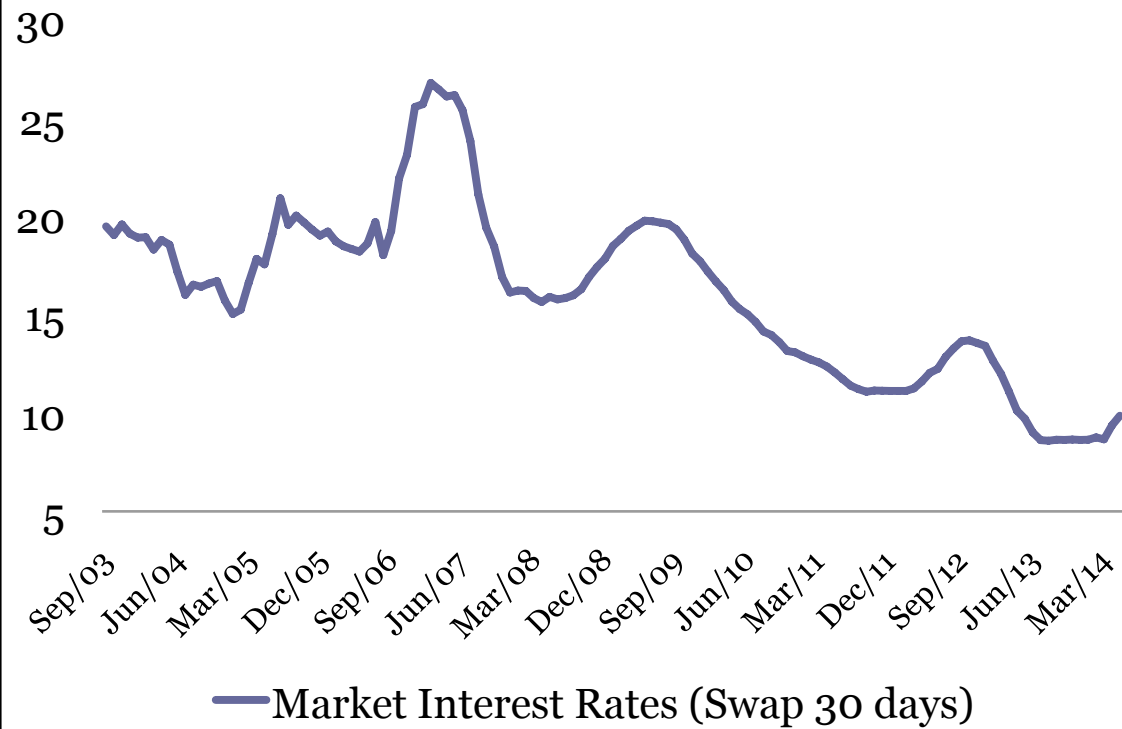
- The Brazilian Ministry of Finance estimates that almost 13,8 million jobs will be created between 2003 and the end of 2010.



Historically Low Interest Rates

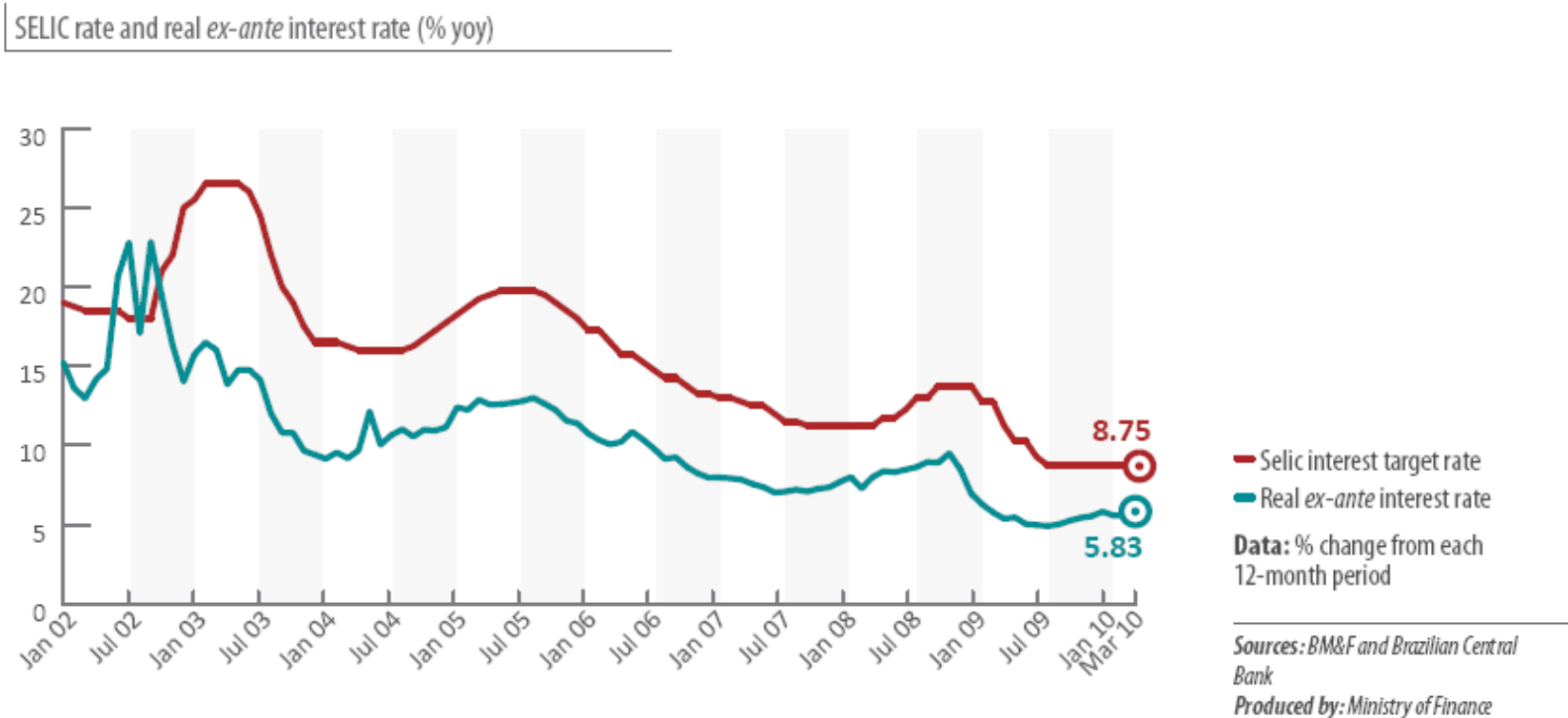


Market Interest Rates



Source: BM&F

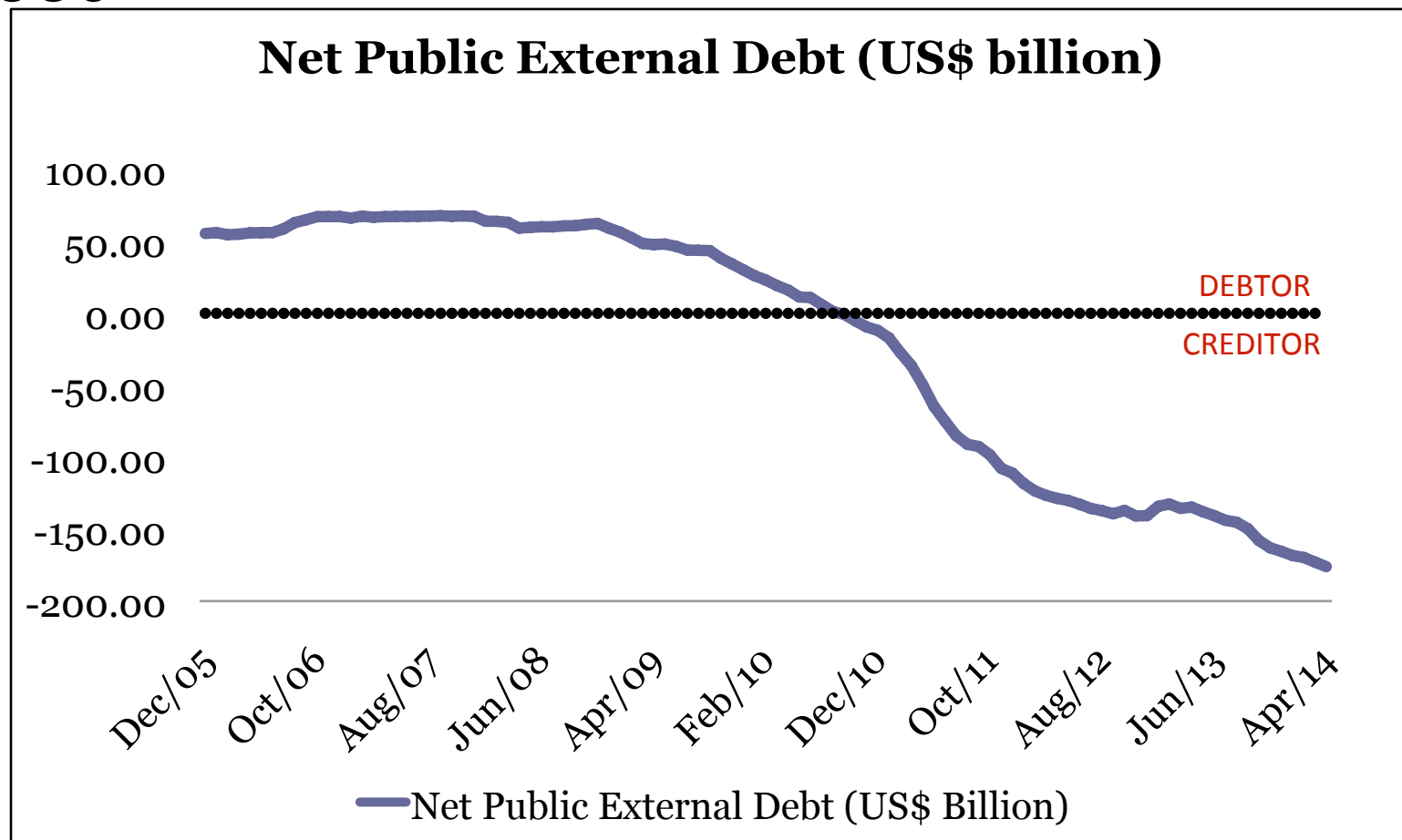
- Interest rates, both nominal and real, reached their lowest historical levels in 2009.





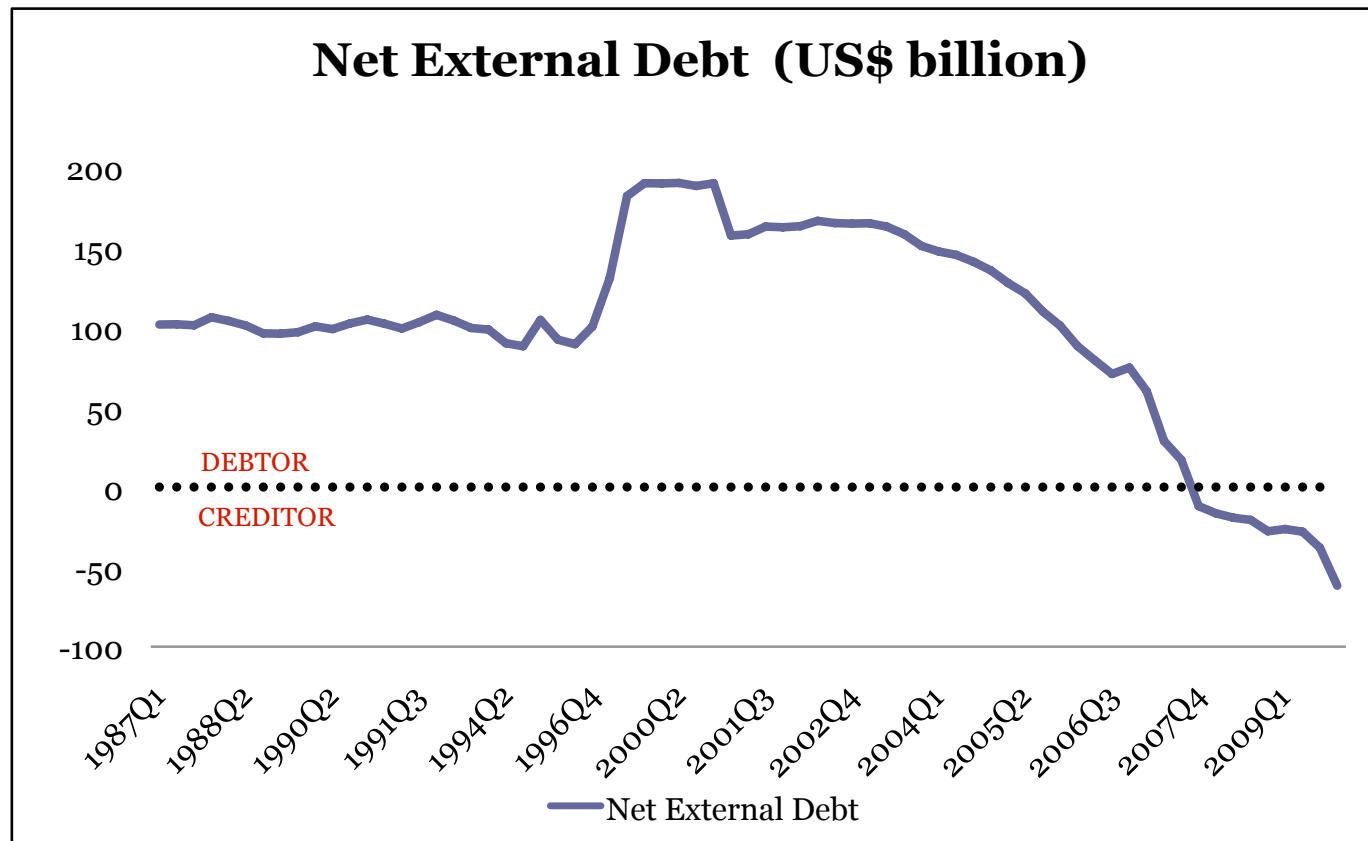
Lower External Vulnerability

- Brazil has consistently reduced its net public *external* debt. It became a *net external creditor* in 2006



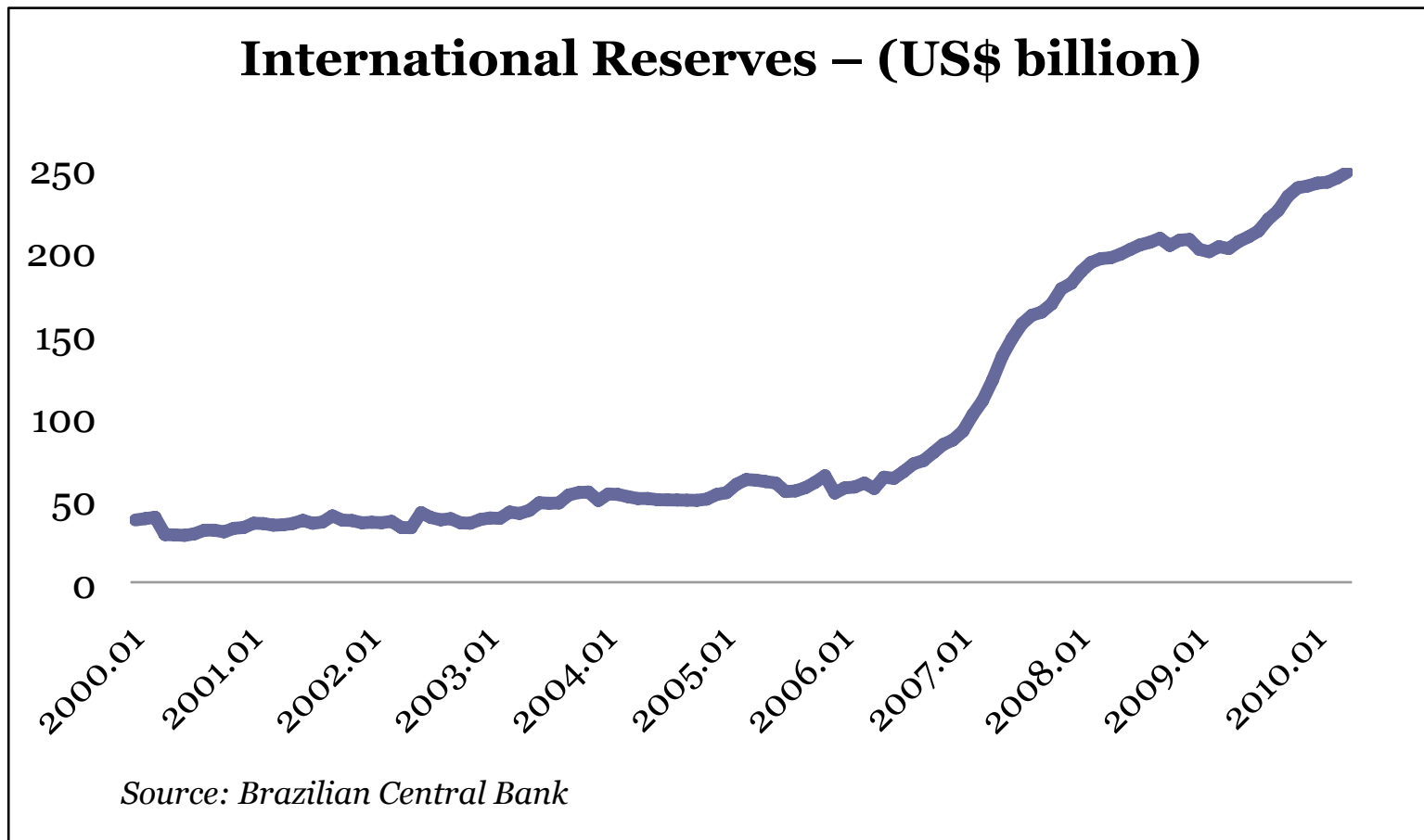
Source: Brazilian Central Bank

- Brazil became an *external net creditor* in 2007. External indebtedness has ceased to be a risk to economic stability

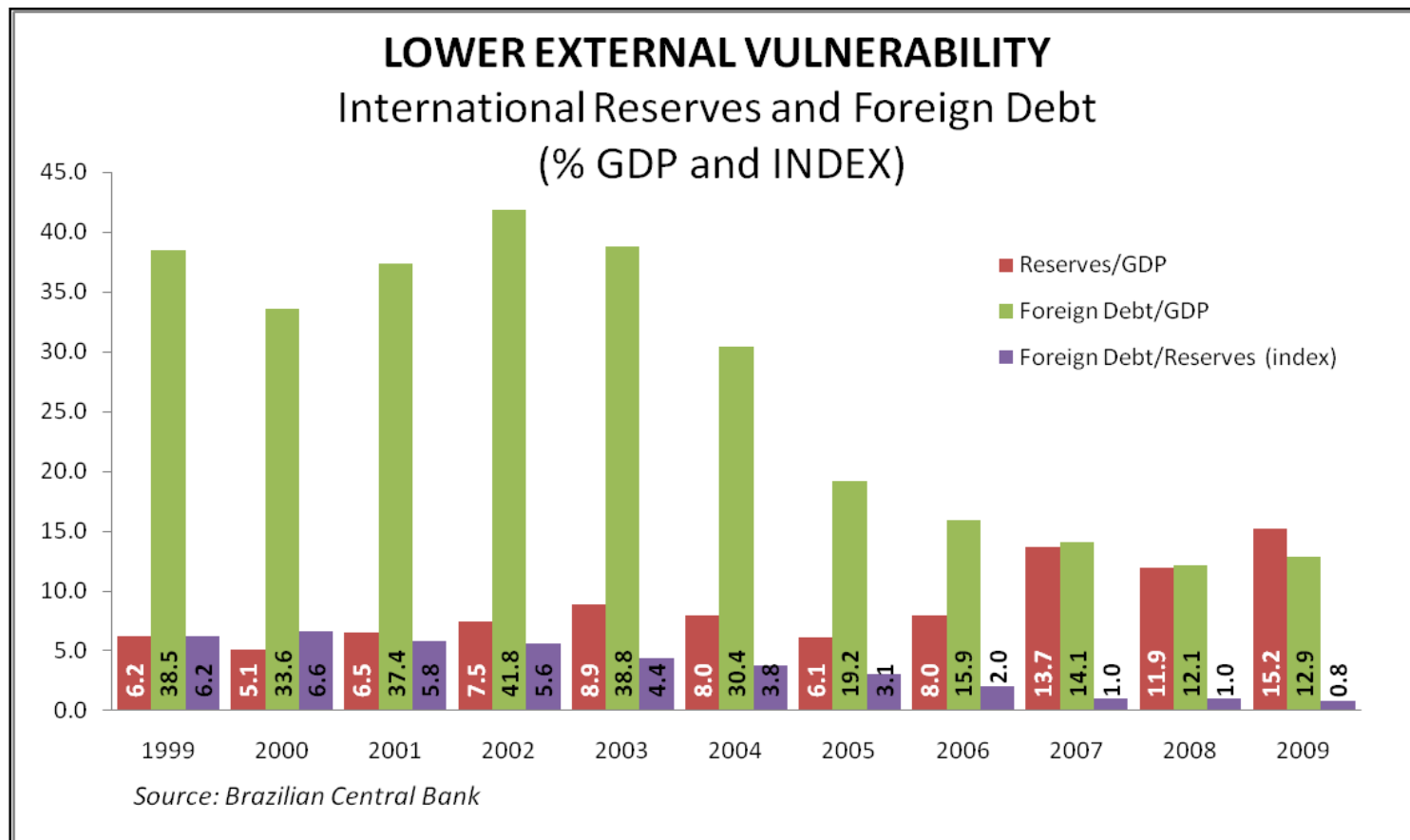


Source: Brazilian Central Bank

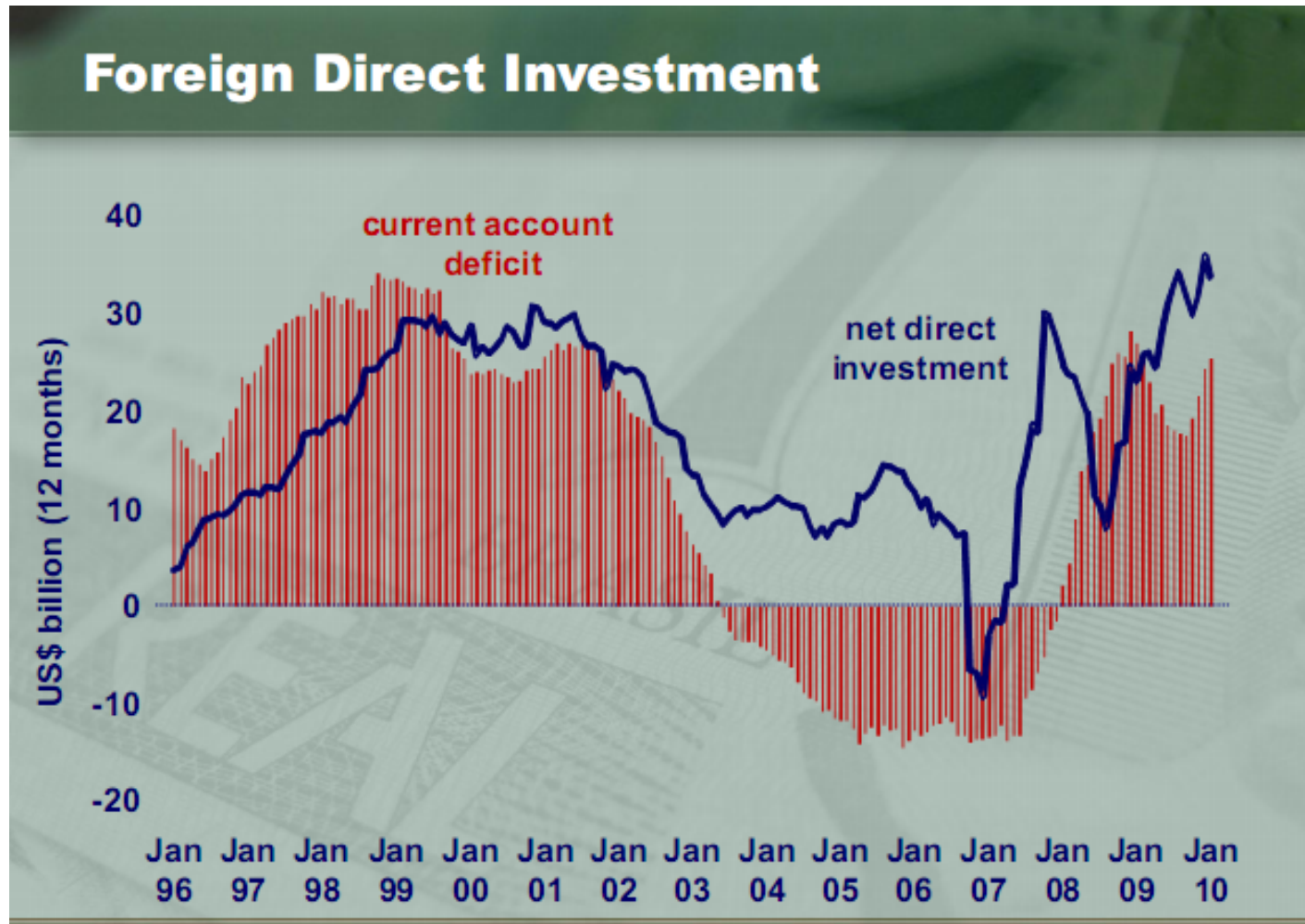
- Brazil has enlarged its volume of international reserves to historically high levels in the latest years.



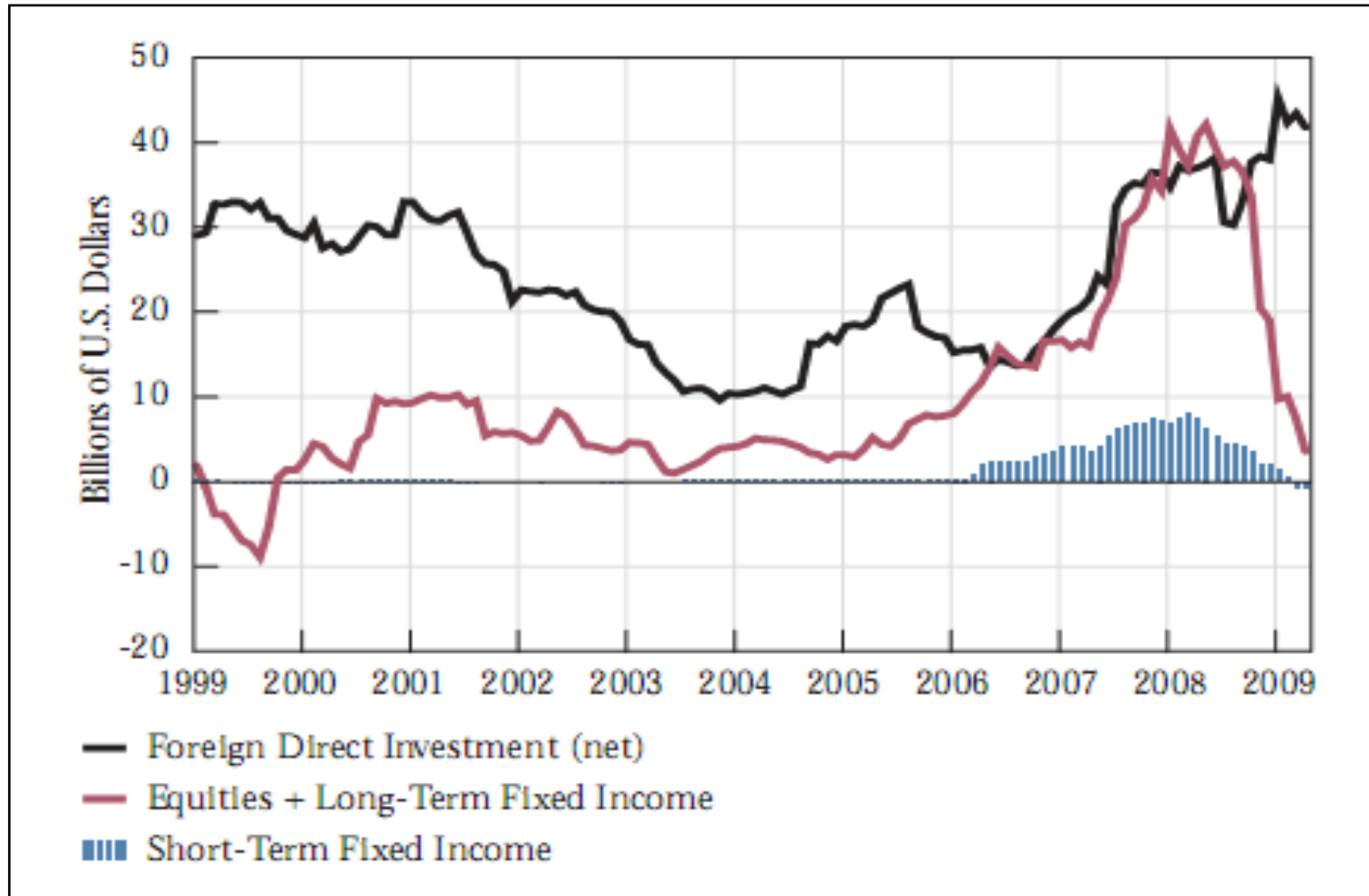
- The increase in international reserves and the reduction of the external debt enabled the country to overcome the worst crisis in years.



- Increase in foreign direct investment



Foreign Direct Investment and Company Equity in Brazil, 1999-2009



Source: Kregel 2009 "Brics"

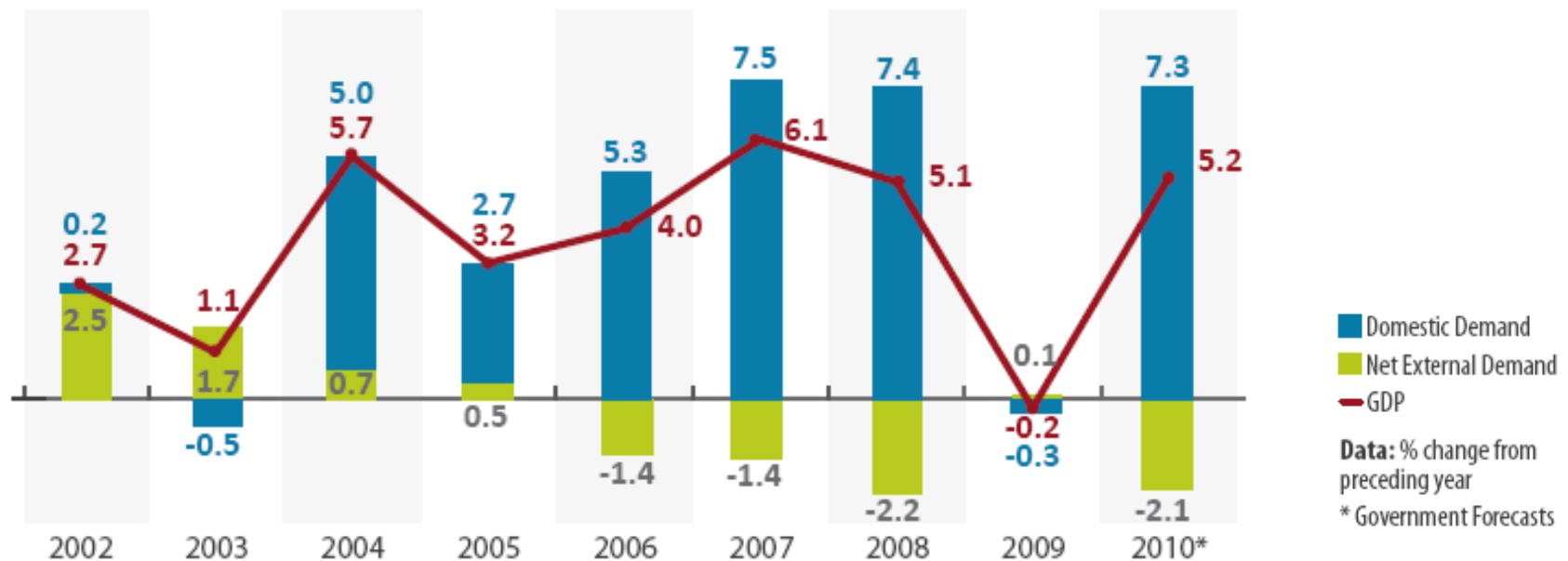


Expansion based on Domestic Markets

- The increased credit level, real incomes and employment generation place altogether the Brazilian domestic market as a driving force for economic growth in the following years.

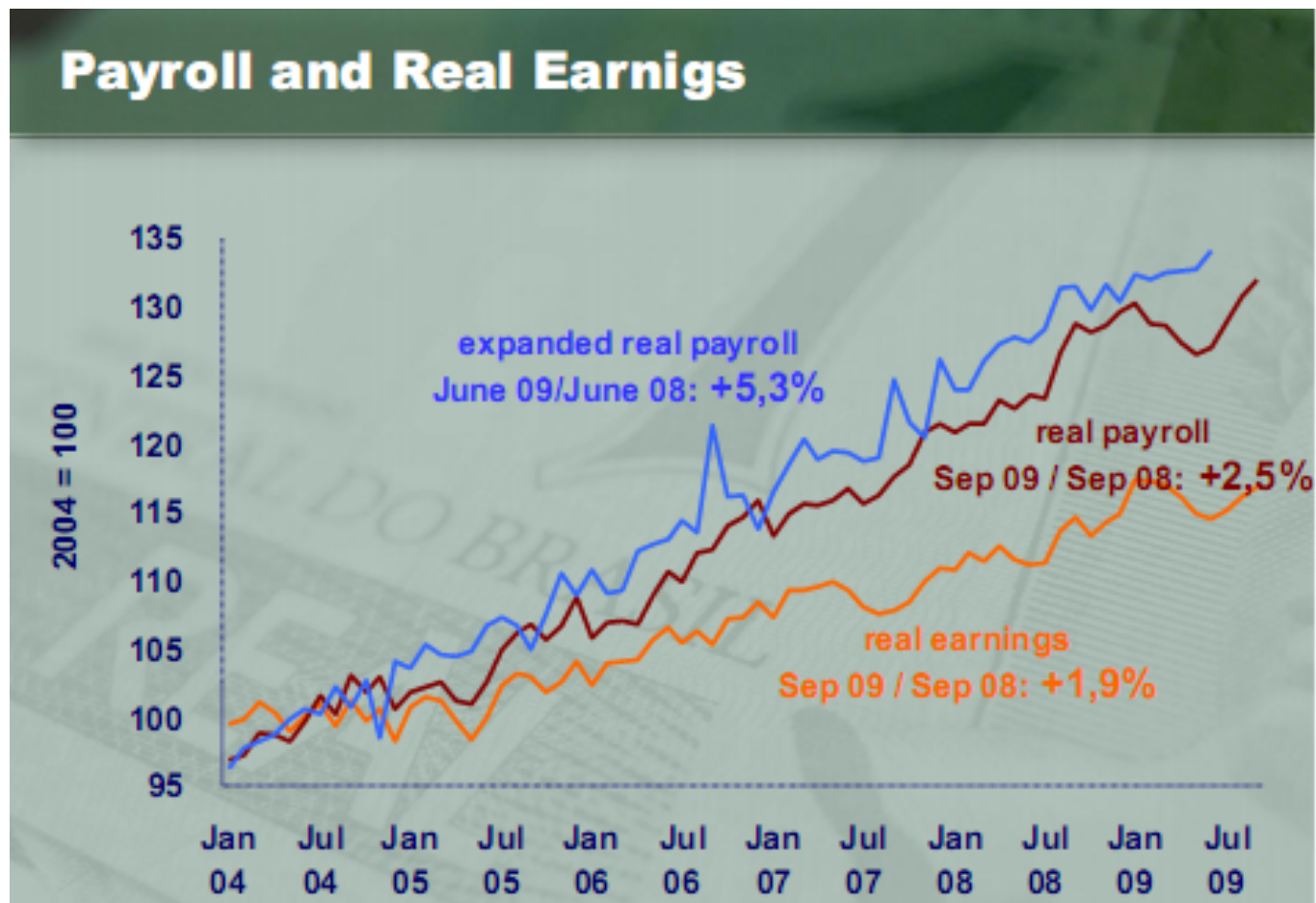
- Domestic demand growth in Brazil

Composition of Mass Market (% yoy)



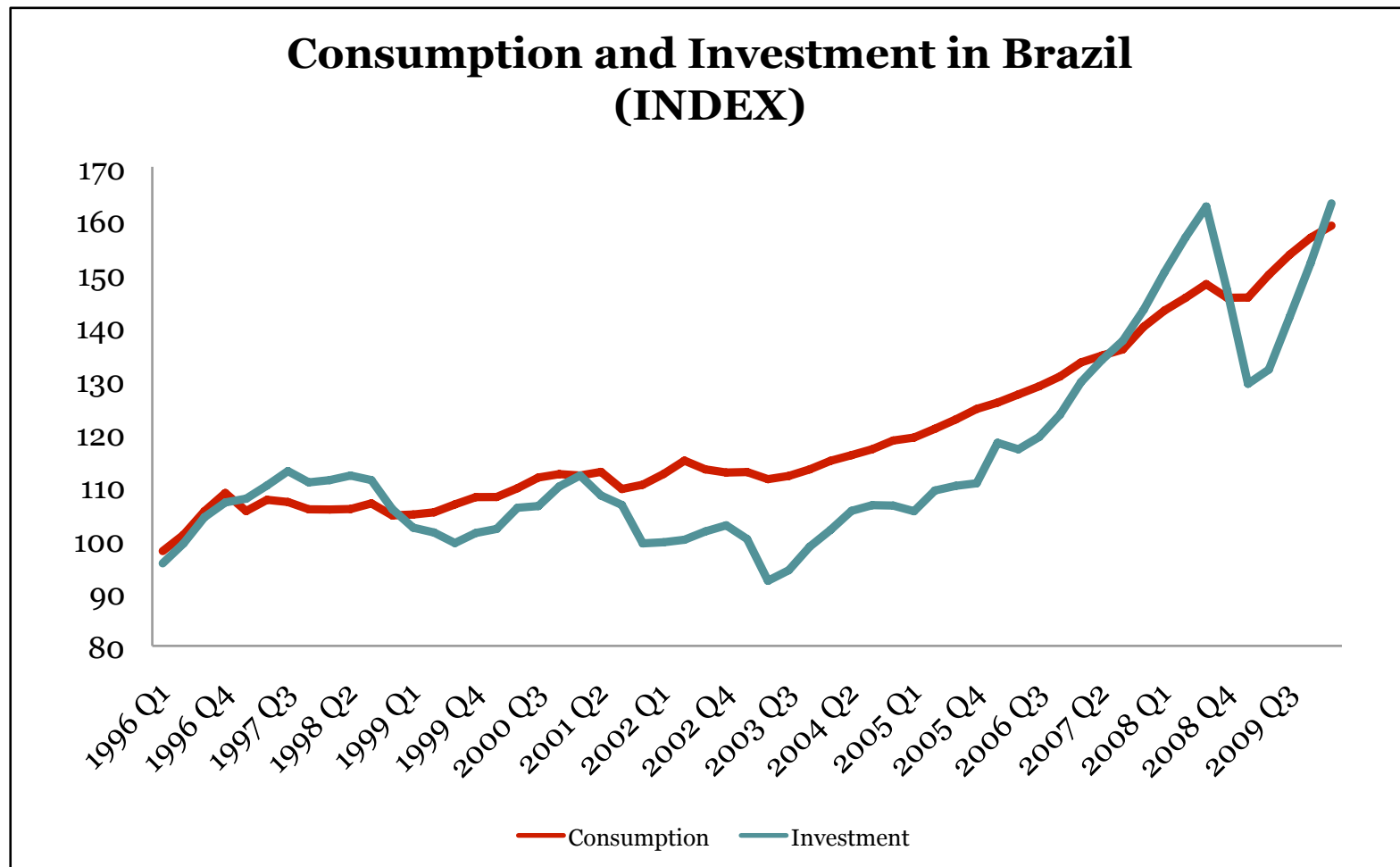
Source: "Brazilian Economy Outlook, 2010" produced by the Ministry of Finance.

- Payroll and Real Earnings increase.



Source: “ *Brazil Beyond the International Crisis*”, 2009, produced by Brazilian Central Bank.

- Increase in private consumption and investment



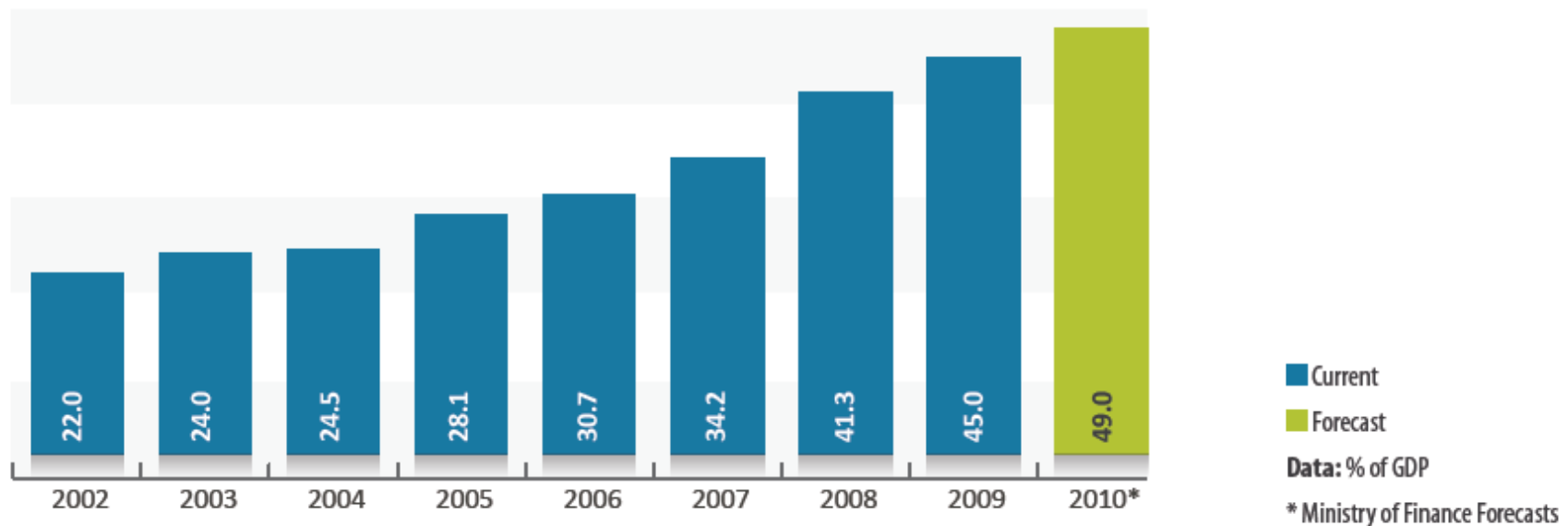
Source: Brazilian Central Bank



Credit Expansion

- Credit Concessions have reached the record level of 45% of GDP and are expected to reach 49% of GDP in 2010.


Financial system loans (% of GDP)



Source: “Brazilian Economy Outlook, 2010” produced by the Ministry of Finance.



Active Role Played by the Government

- 
- Expansion of Public Investment.
 - Investment Expansion Program (BNDES).
 - Credit Expansion led by Public Banks.
 - “*Minha Casa, Minha Vida*” (Housing Program):
US\$ 15.6 billion in subsidies and US\$ 33.3 billion in investments.
 - Expansion of Social Programs like “*Bolsa Familia*”.

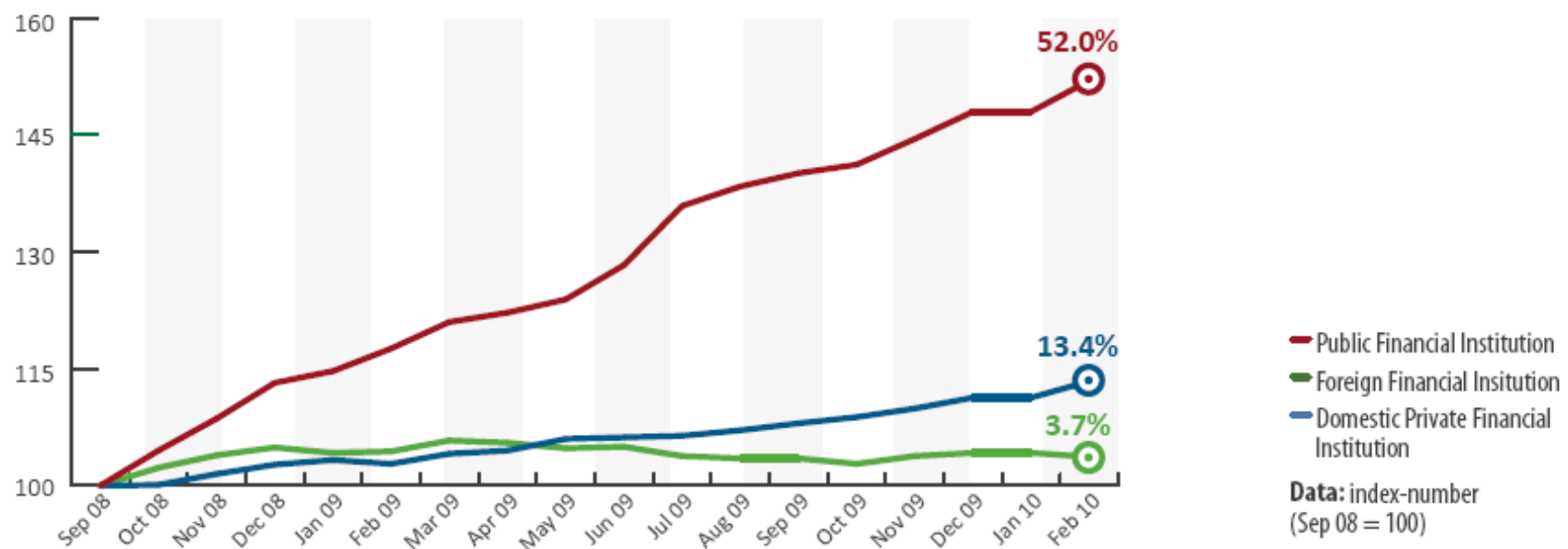
Quadro1
Síntese da estrutura de intervenção social do Estado brasileiro

Áreas	Principais Programas/Ações	Beneficiários/Resultados em 2008
1. Previdência Social Regime Geral Prev. Social	Aposentadorias e Pensões – área Rural	7,8 milhões de benefícios na área rural
	Aposentadorias e Pensões – área Urbana	15,2 milhões de benefícios na área urbana
	Auxílio-Doença, Auxílio-Maternidade e outros Auxílios - área Urbana e Rural	1,7 milhão de beneficiários
Previdência do Servidor Público (Regimes Próprios Prev. Social)	Pagamento de Aposentadorias e Pensões - Executivo, Legislativo e Judiciário	União: 530 mil servidores inativos e 448 mil pensionistas; Estados: 1,1 milhão de servidores inativos e 384 mil pensionistas; Municípios: 401 mil inativos e 151 mil pensionistas
2. Emprego e Defesa do Trabalhador	Seguro-Desemprego	6,9 milhões de trabalhadores
	Abono Pis-Pasep	8,4 milhões de trabalhadores com renda até 2 SM (em 2007)
3. Desenvolvimento Agrário	Pronaf	2,2 milhões de contratos
4. Assistência Social	BPC - LOAS - Pessoa Idosa	1,6 milhão
	BPC - LOAS - Pessoa com Deficiência	1,8 milhão
	Programa Nacional de Inclusão de Jovens – Pró-Jovem	400 mil jovens
	Programa Bolsa Família	11,6 milhões de famílias
5. Saúde	Atenção Básica em Saúde Assistência Ambulatorial e Hospitalar Especializada Vigilância, Prevenção e Controle de Doenças e Agravos Assistência Farmacêutica e Insumos Estratégicos	23 mil equipes de Saúde da Família; 50% da população coberta pelo PSF; 2,3 bilhões de procedimentos ambulatoriais, 11 mil transplantes, 215 mil cirurgias cardíacas, 9 milhões de procedimentos de quimioterapia e radioterapia e 11,3 milhões de internações; Serviço de Atendimento Médico de Urgência (SAMU) já conta com cerca de 2,5 mil veículos, cobrindo 1.163 municípios e 100 milhões de pessoas; cobertura vacinal para doenças infantis acima de 90% em 25 das 27 UFs, aproximando-se de 100% em 14 UFs
6. Educação	Brasil Alfabetizado e Educação de Jovens e Adultos	4,1 milhões de estudantes atendidos pela rede pública
	Brasil Escolarizado	40 milhões de estudantes atendidos pela rede pública: 4,9 milhões na educação infantil, 28,1 milhões no ensino fundamental, 7,3 milhões no ensino médio
	Qualidade na Escola	
	Distribuição de Livros Didáticos	
	Complementação da União para o Fundeb	
	Programa Nacional de Alimentação Escolar	40 milhões de estudantes atendidos
	Brasil Universitário	615 mil estudantes matriculados na rede pública federal (2007)

Fonte: INEP/MEC; MDS; MPS; Boletim do Servidor/Siape; MTE; MDA, AEPS/MPS e IBGE

- Credit Expansion led primarily by public banks. The amount disbursed by public financial institutions has grown 52%.

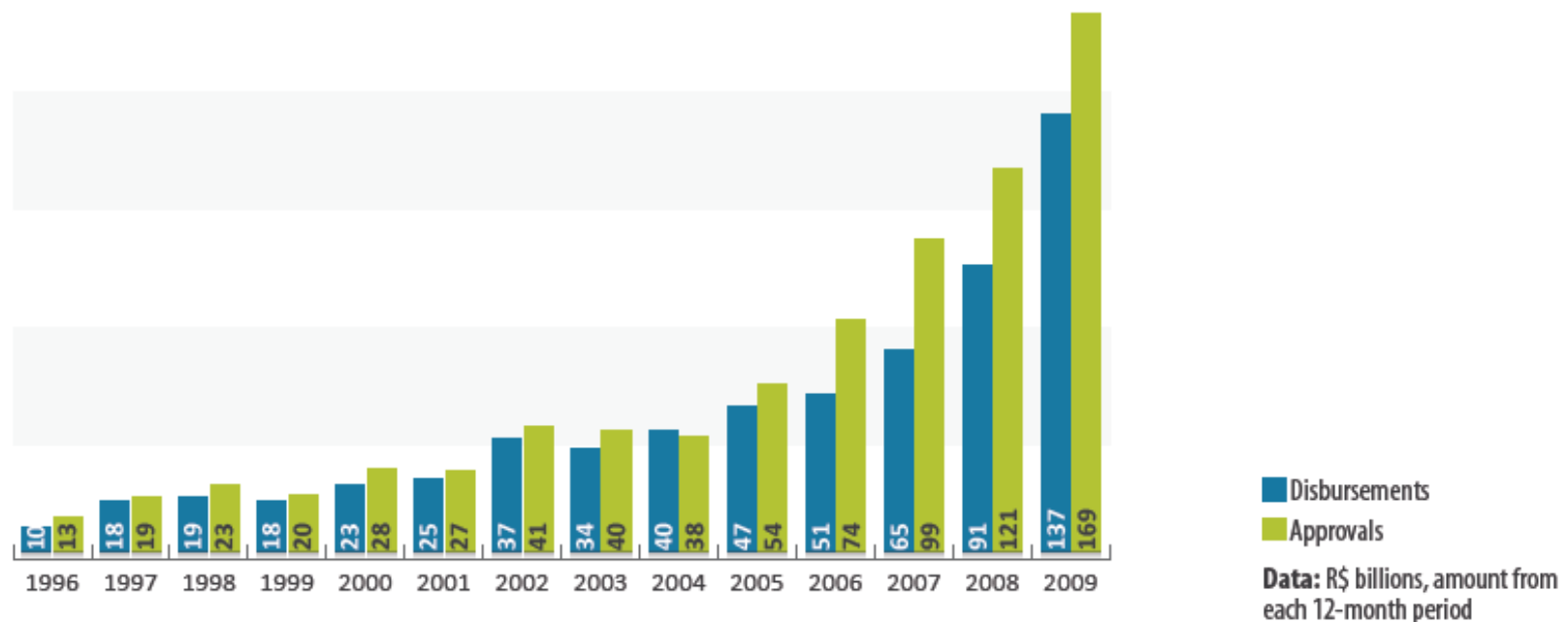
Financial system credit transactions development, according to capital control - index-number (Sep 08 = 100)



Source: "Brazilian Economy Outlook, 2010" produced by the Ministry of Finance.

- Total disbursements from the Brazilian Social and Economic Development Bank (BNDES) increased 53% in the last 12 months.

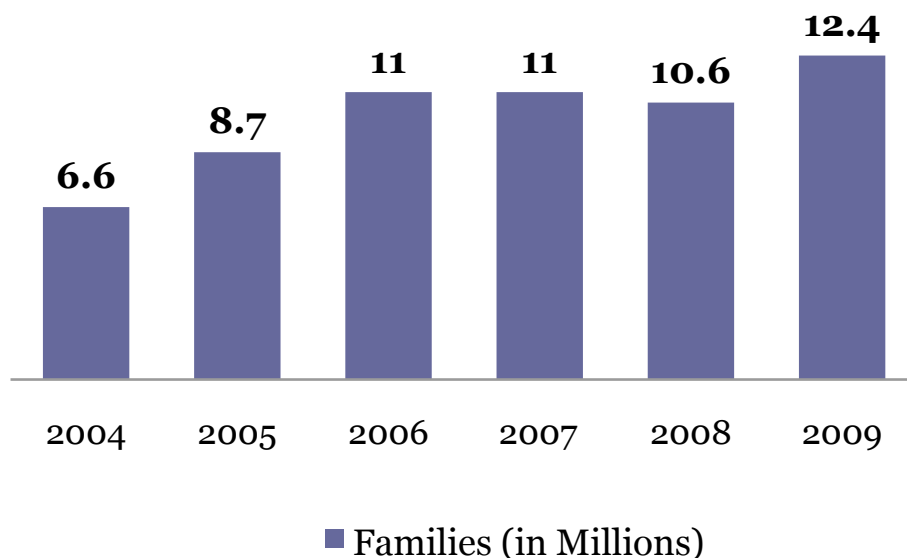
BNDES credit (R\$ billion)



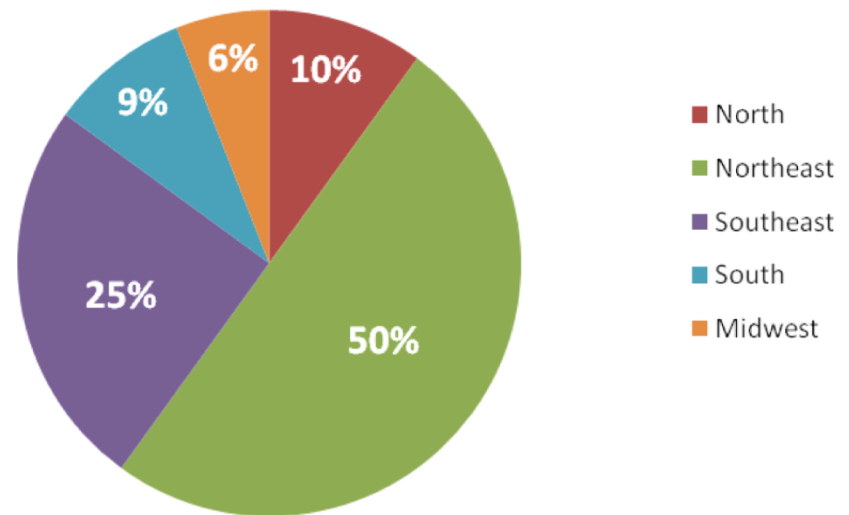
Source: “Brazilian Economy Outlook, 2010” produced by the Ministry of Finance.

- *Bolsa familia* has benefited 12.4 million families (almost 43 million people) in 2009.
- 50% of those families are located in the northeast

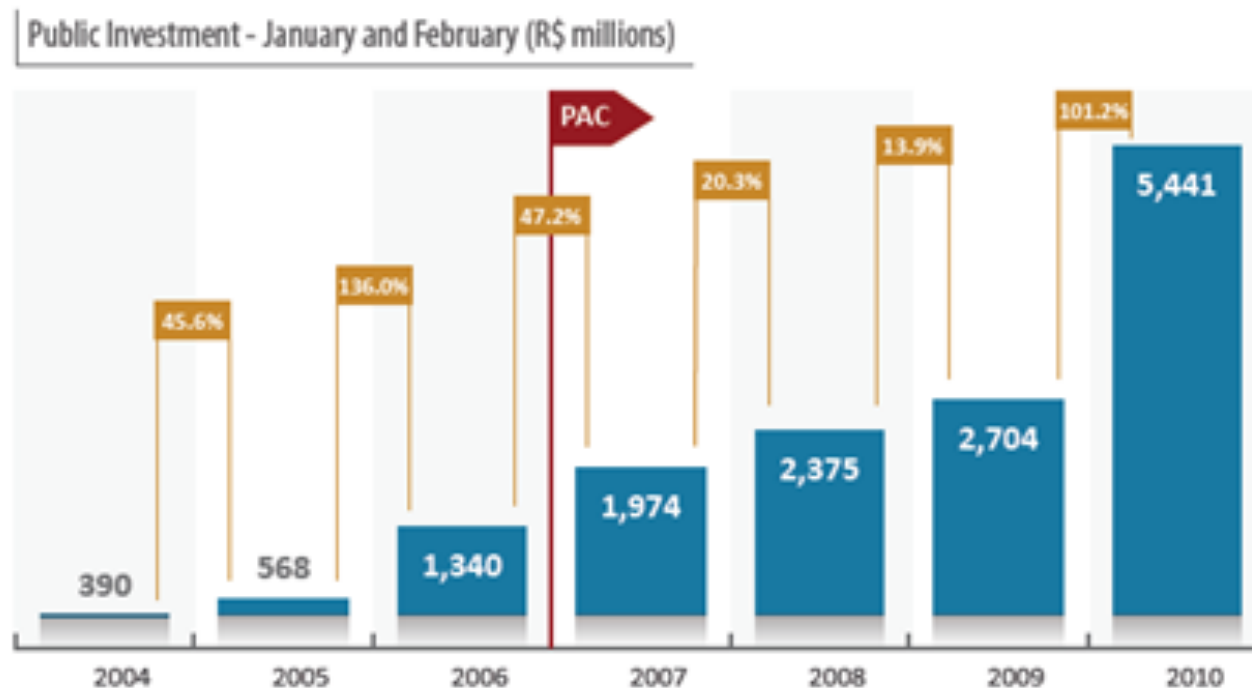
**Bolsa Familia Beneficiaries
(N° of families)**



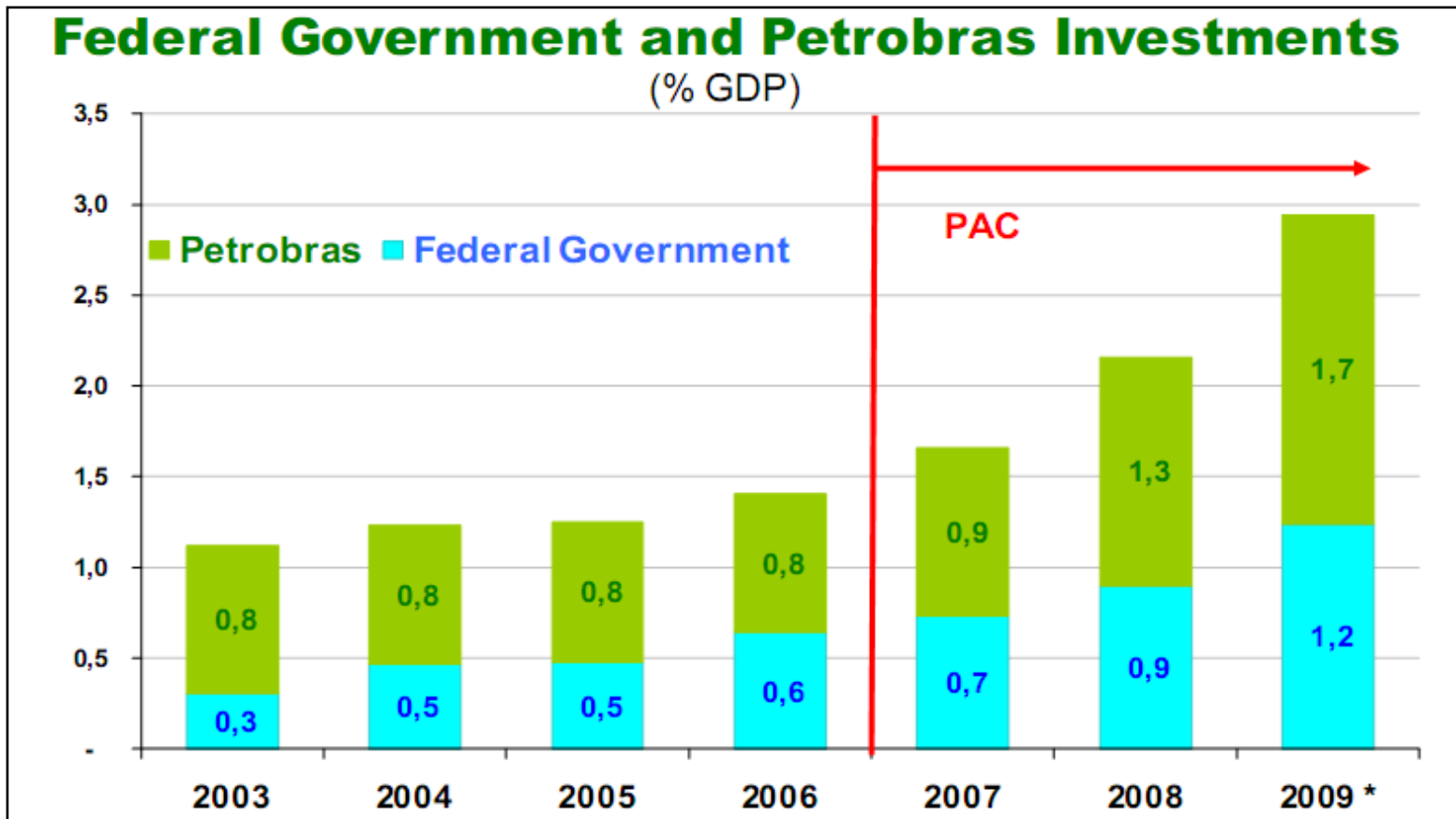
**Bolsa Familia Beneficiaries by Region
(% of families)**



- Substantial Increase in Public Investment as the Growth Acceleration Program (PAC) advances.



Source: “Brazilian Economy Outlook, 2010” produced by the Ministry of Finance.

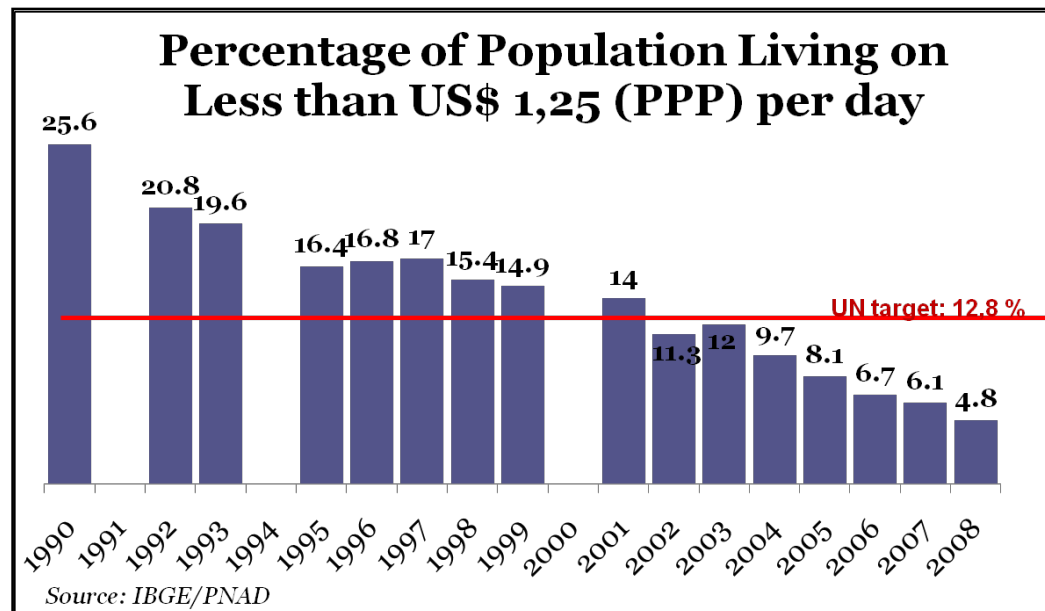
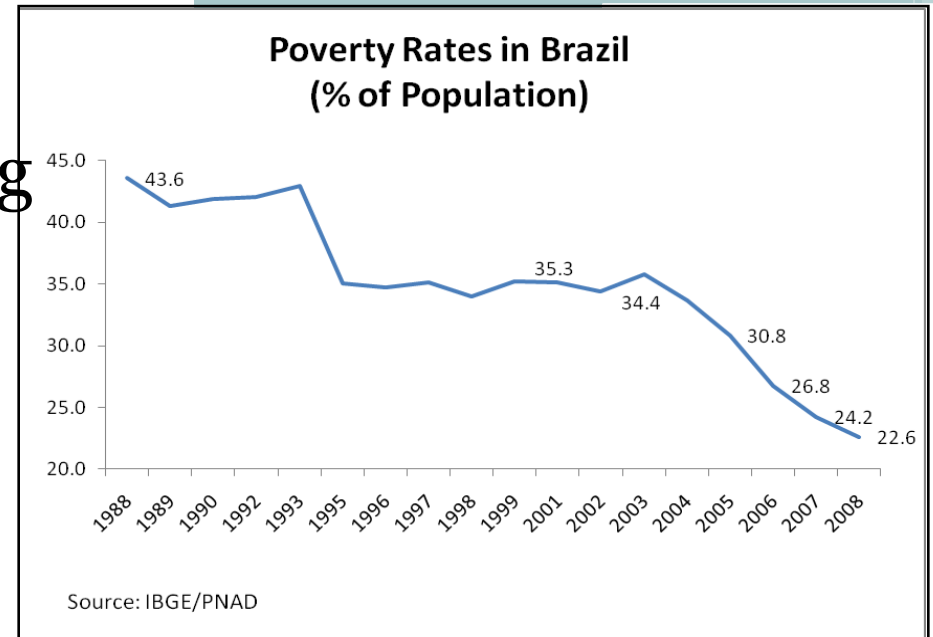


Source: Ministry of Finance.

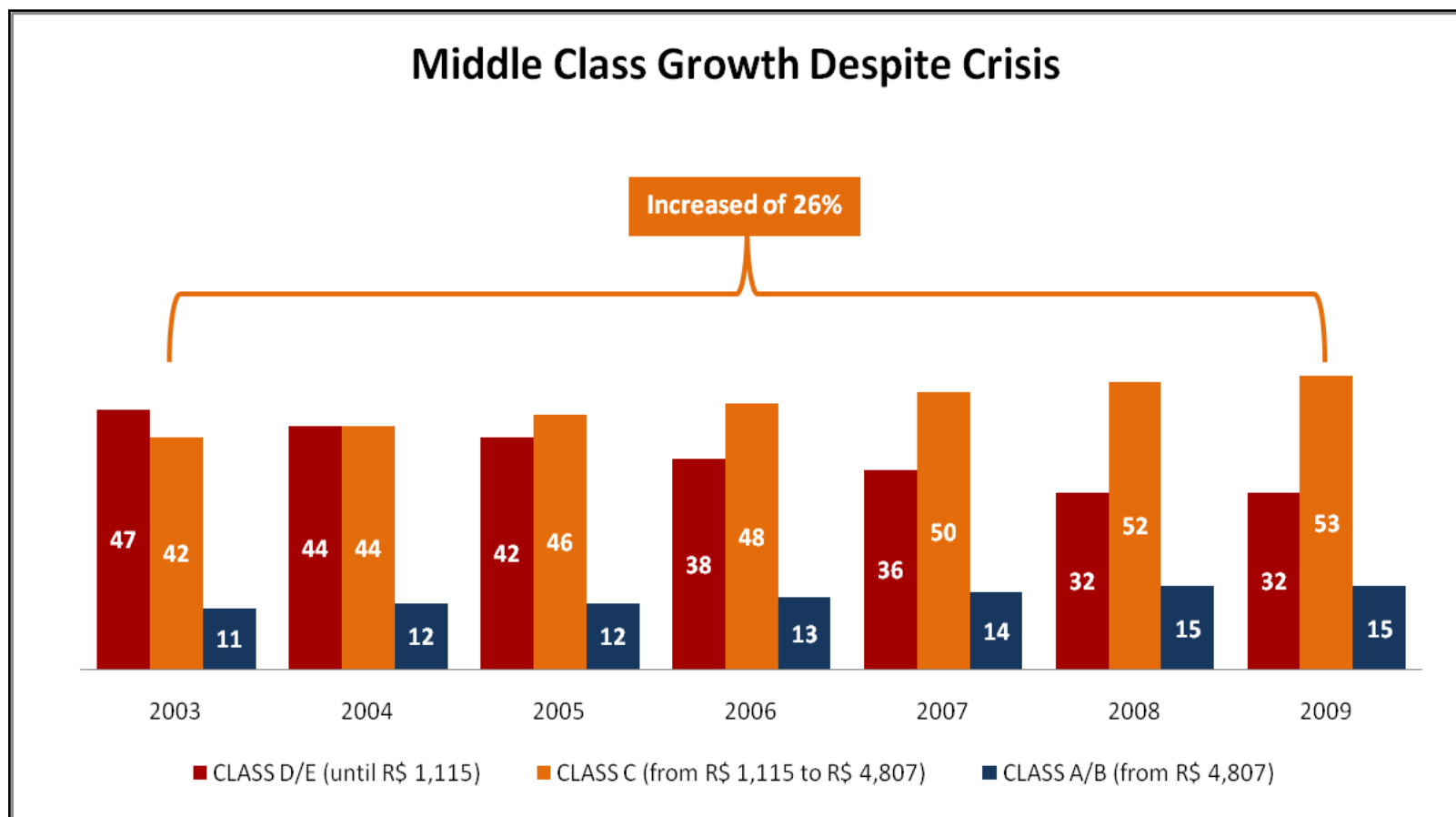


Reduction in Poverty Rates and Income Inequality

- The percentage of the Brazilian population living in poverty and extreme poverty fell dramatically over the last two decades.

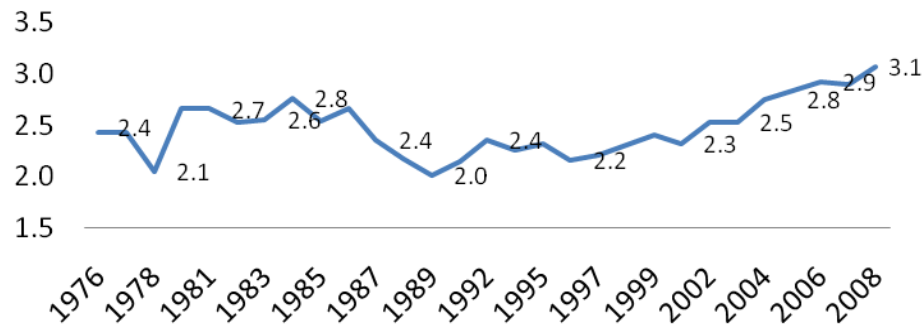


- 25,9 million Brazilians joined the middle class between 2003 and 2009.

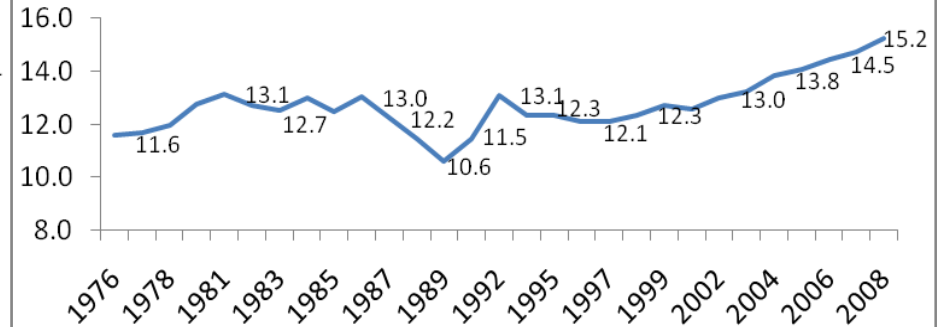


Source: IBGE/PNAD

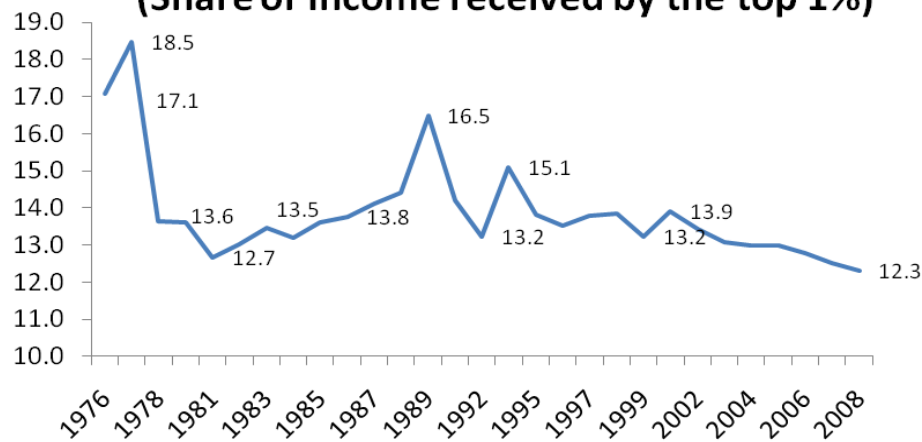
Income Distribution
(Share of Income received by the
bottom 20%)



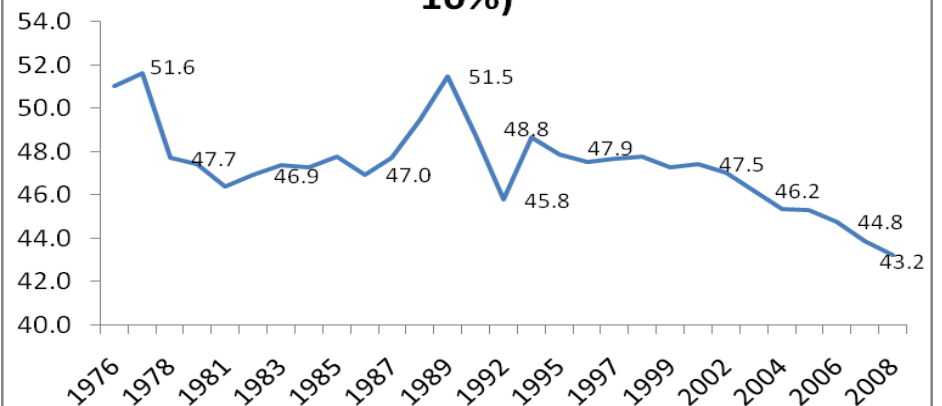
Income Distribution
(Share of Income received by the
bottom 50%)



Income Distribution
(Share of Income received by the top 1%)



Income Distribution
(Share of Income received by the top
10%)



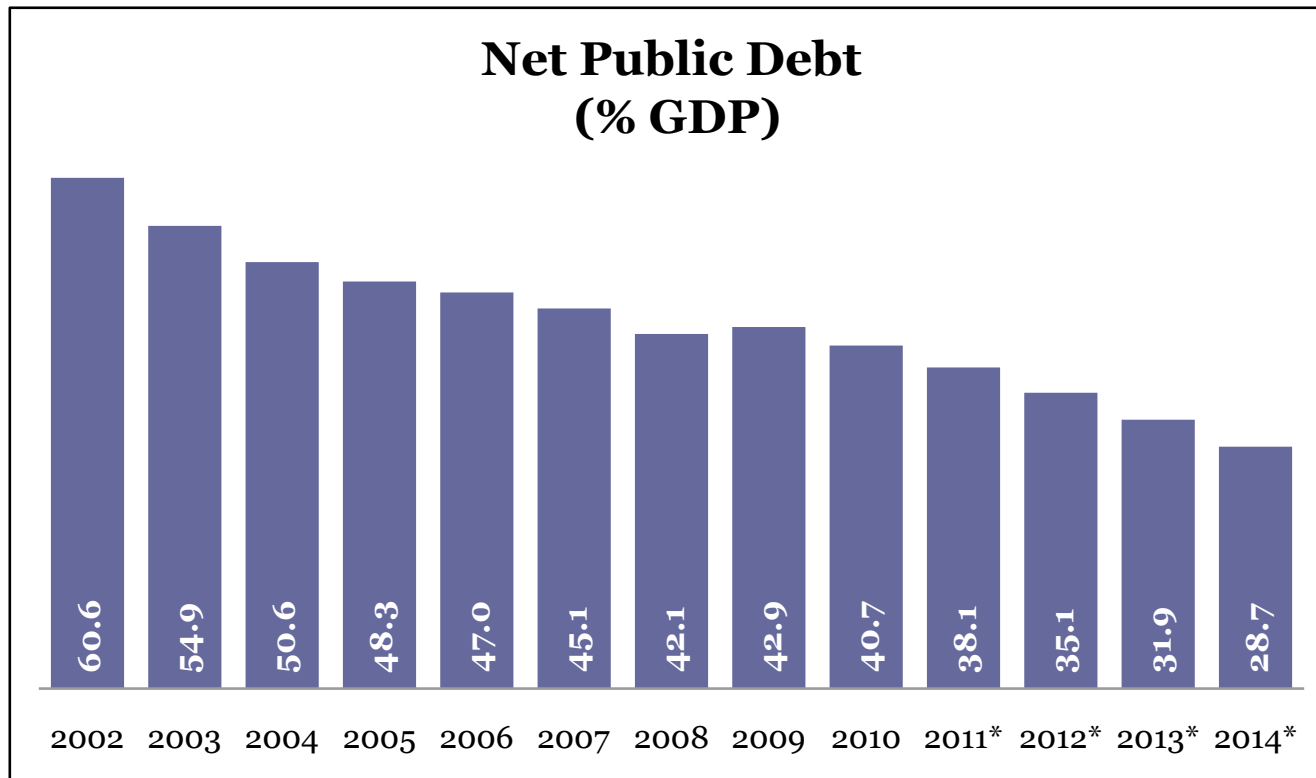
Source: IPEA



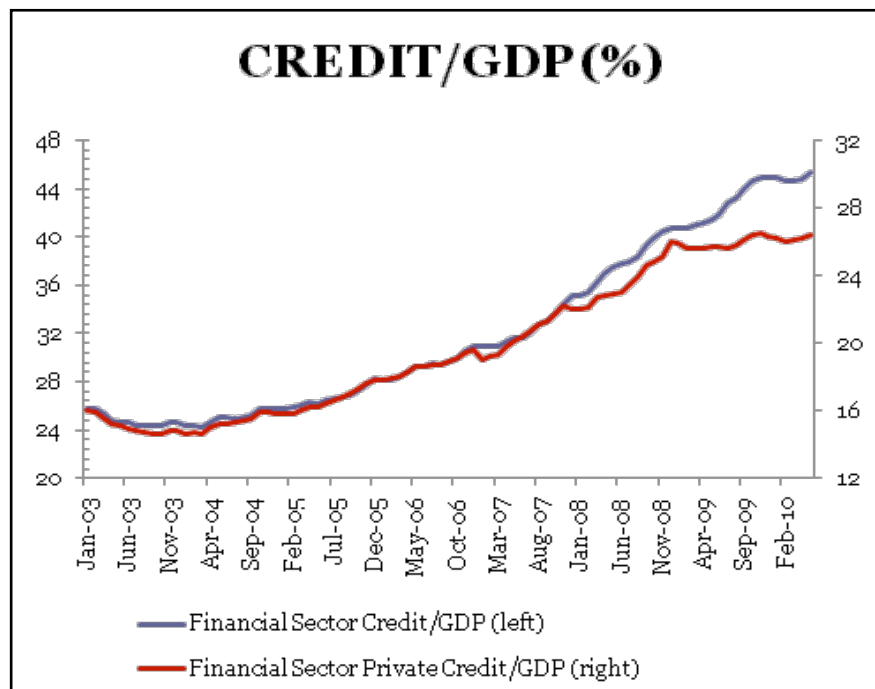
Risks

- The domestic expansion of credit represents a double-edge sword: it busts domestic demand (lower income families benefited from this process) but also increases fragility *a la* Minsky.

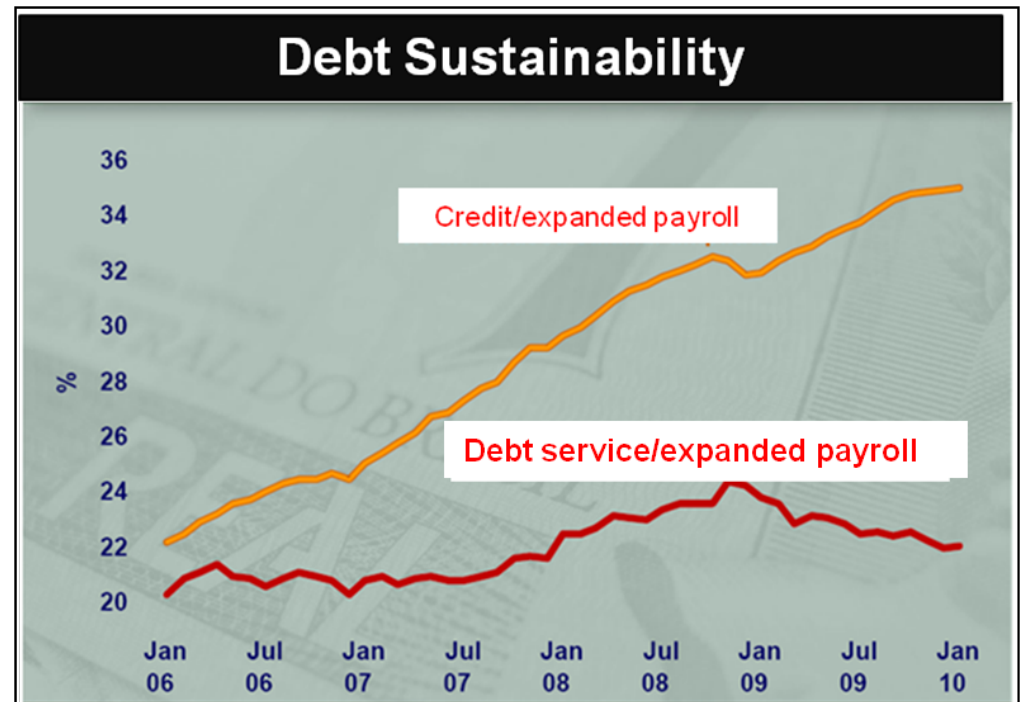
- Public sector net debt to GDP ratio fell from 60.6% in 2002 to 42.9% and it is expect to reach 28.7% in 2014.



- Real increases in wage and salaries compensated this but are sensitive to changes in interest rates (the current tightening cycle) and economic conditions.

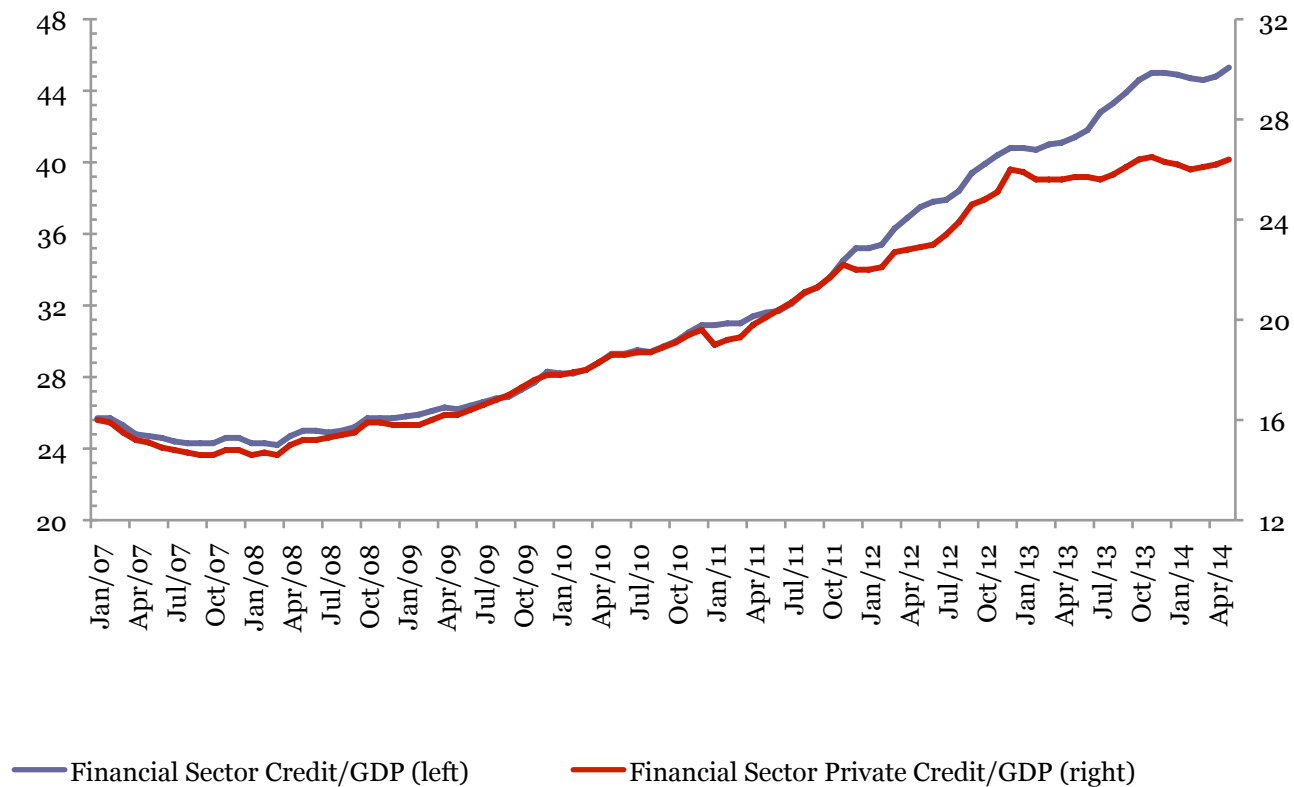


Source: *Brazilian Central Bank*



Source: “*Brazil Beyond the International Crisis*” 2009, produced by *Brazilian Central Bank*.

CREDIT/GDP (%)





Brazil, Some Things May Never
Change...



THE RELEVANCE OF AN EMPLOYER OF LAST RESORT IN BRAZIL

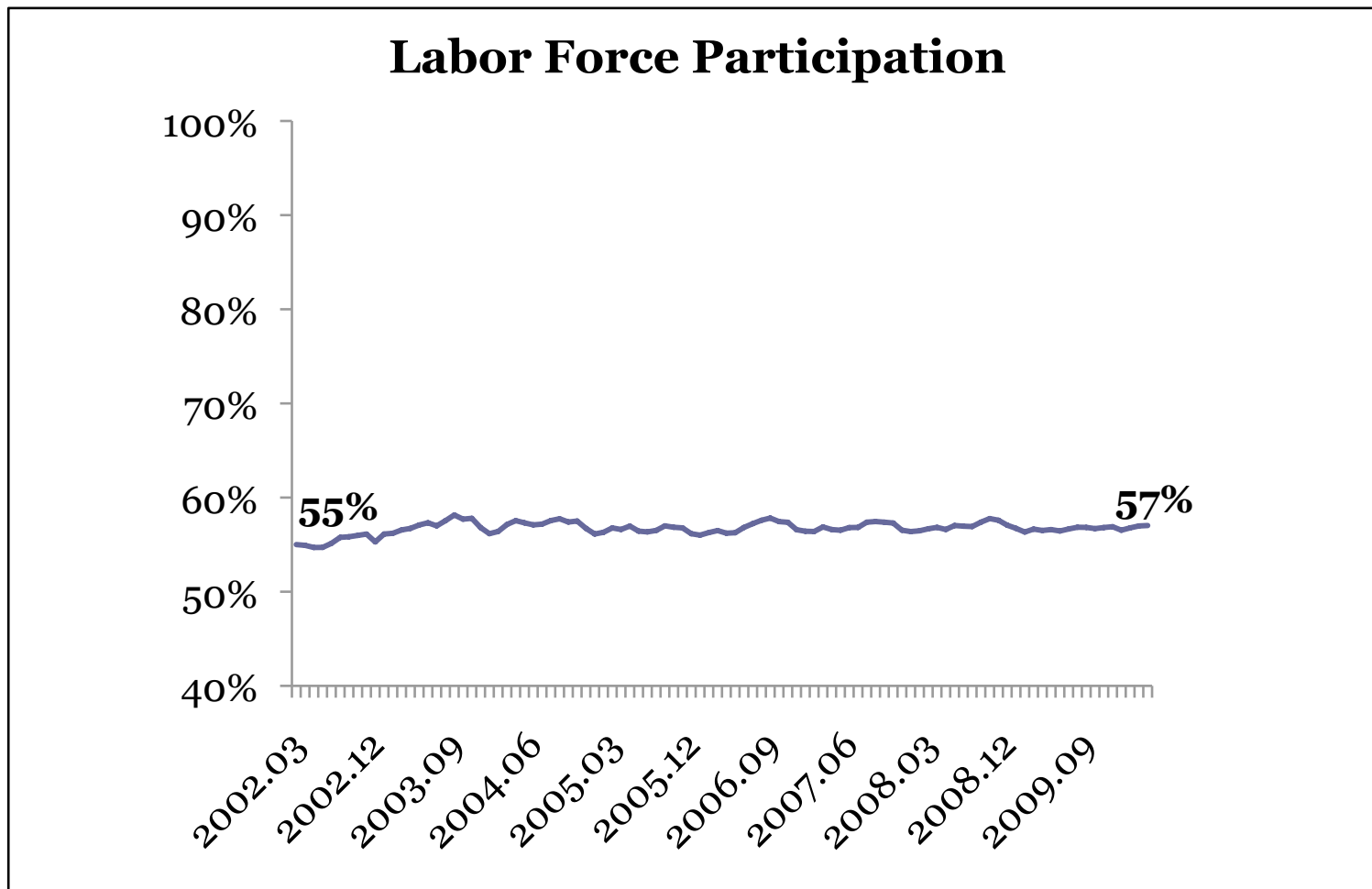
- Despite the favorable macroeconomic conditions, Brazil still faces exceptional challenges to unemployment and poverty reduction.
- Racial, regional and gender discrimination
- Low levels of labor force participation.
- Need for wide scale training opportunities.
- Income inequality remains a major problem.



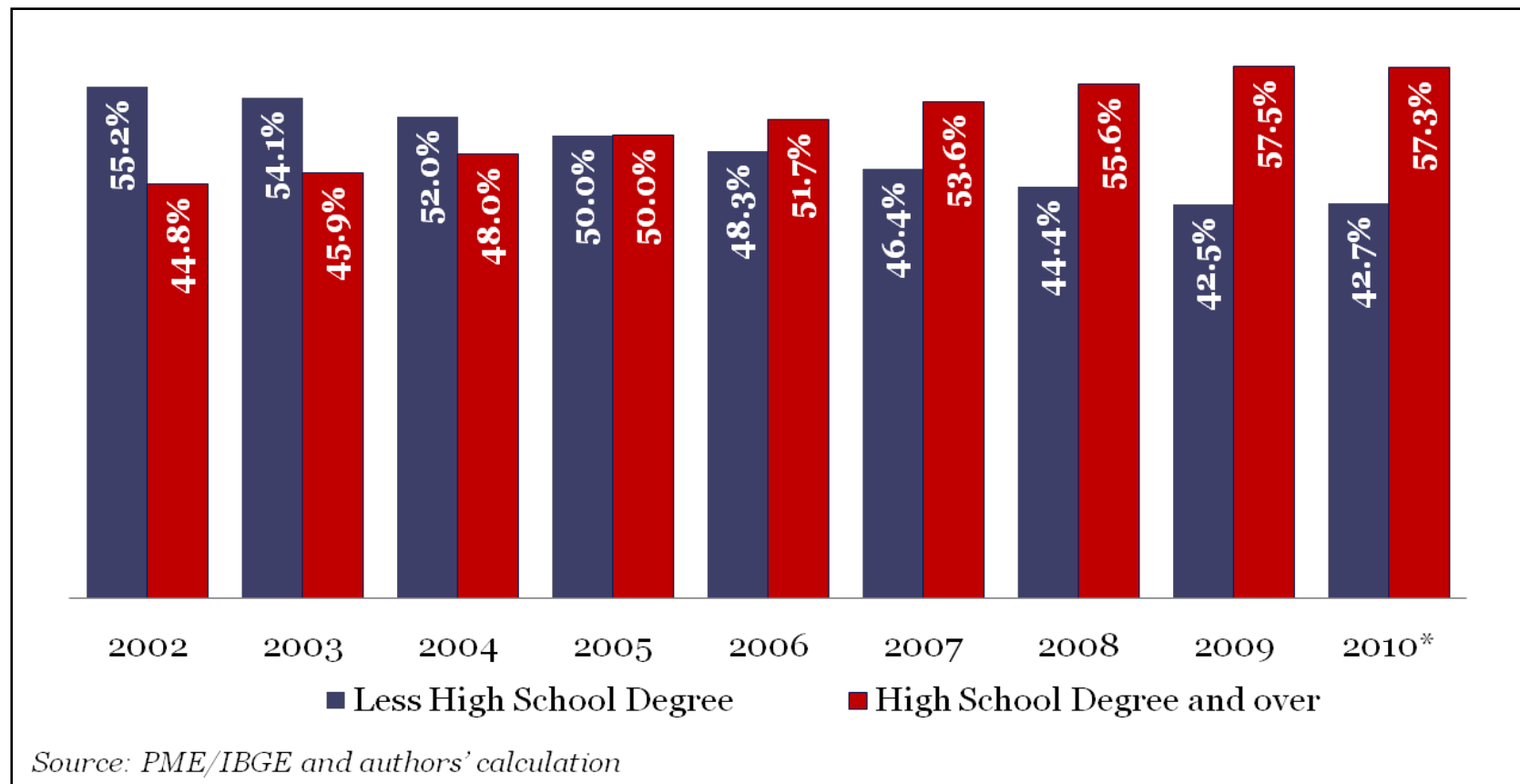
THE RELEVANCE OF AN EMPLOYER OF LAST RESORT IN BRAZIL

- Social and economic exclusion
- Need for social and infrastructure capital
- High child and maternal mortality rates
- High poverty rates specially among northeast families
- Poverty, unemployment and idleness has been inducing the youth into crime activities, specially in urban areas

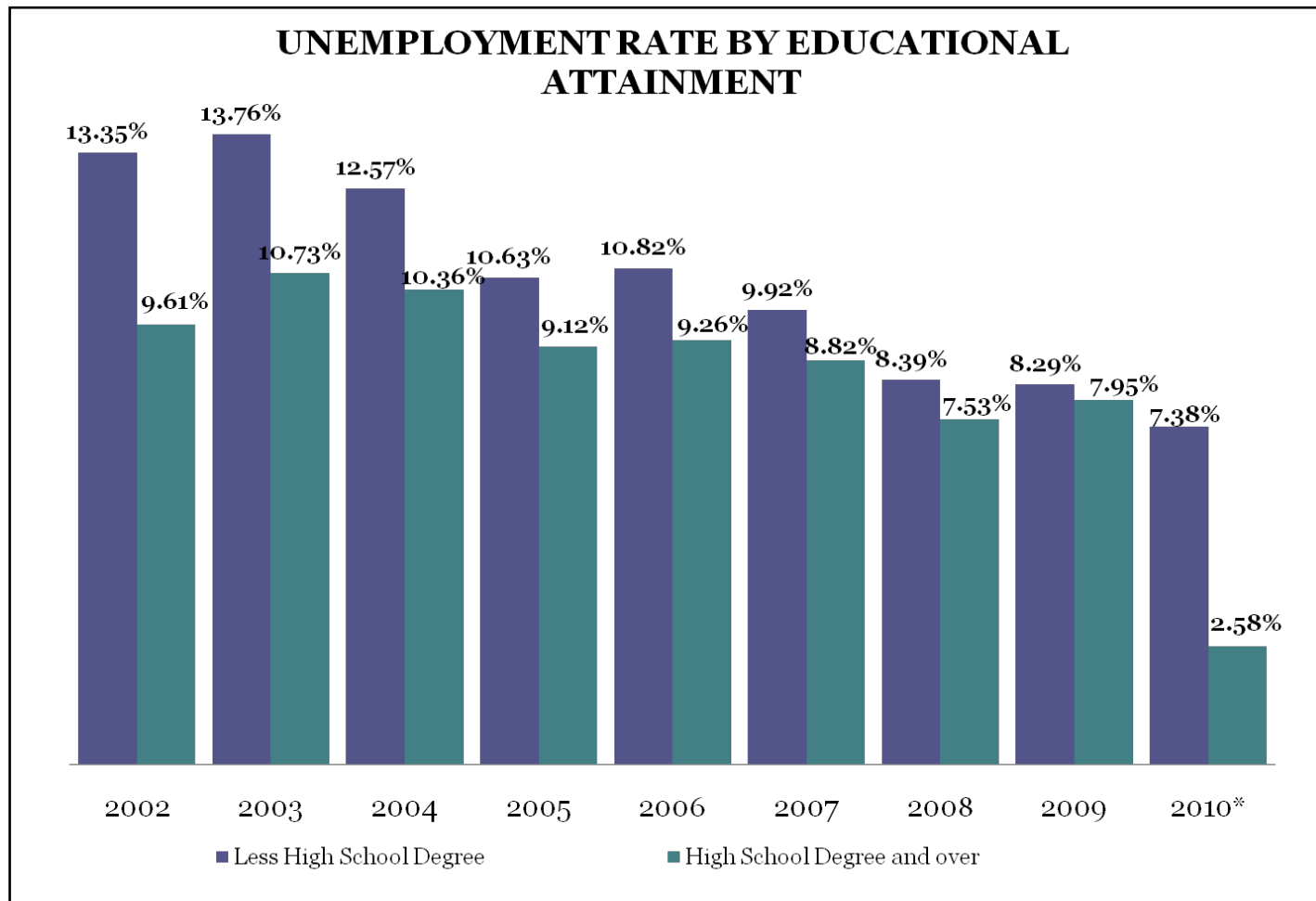
- Low labor force participation ratio.



- Need for wide scale training opportunities: the Brazilian labor force has low educational attainment.

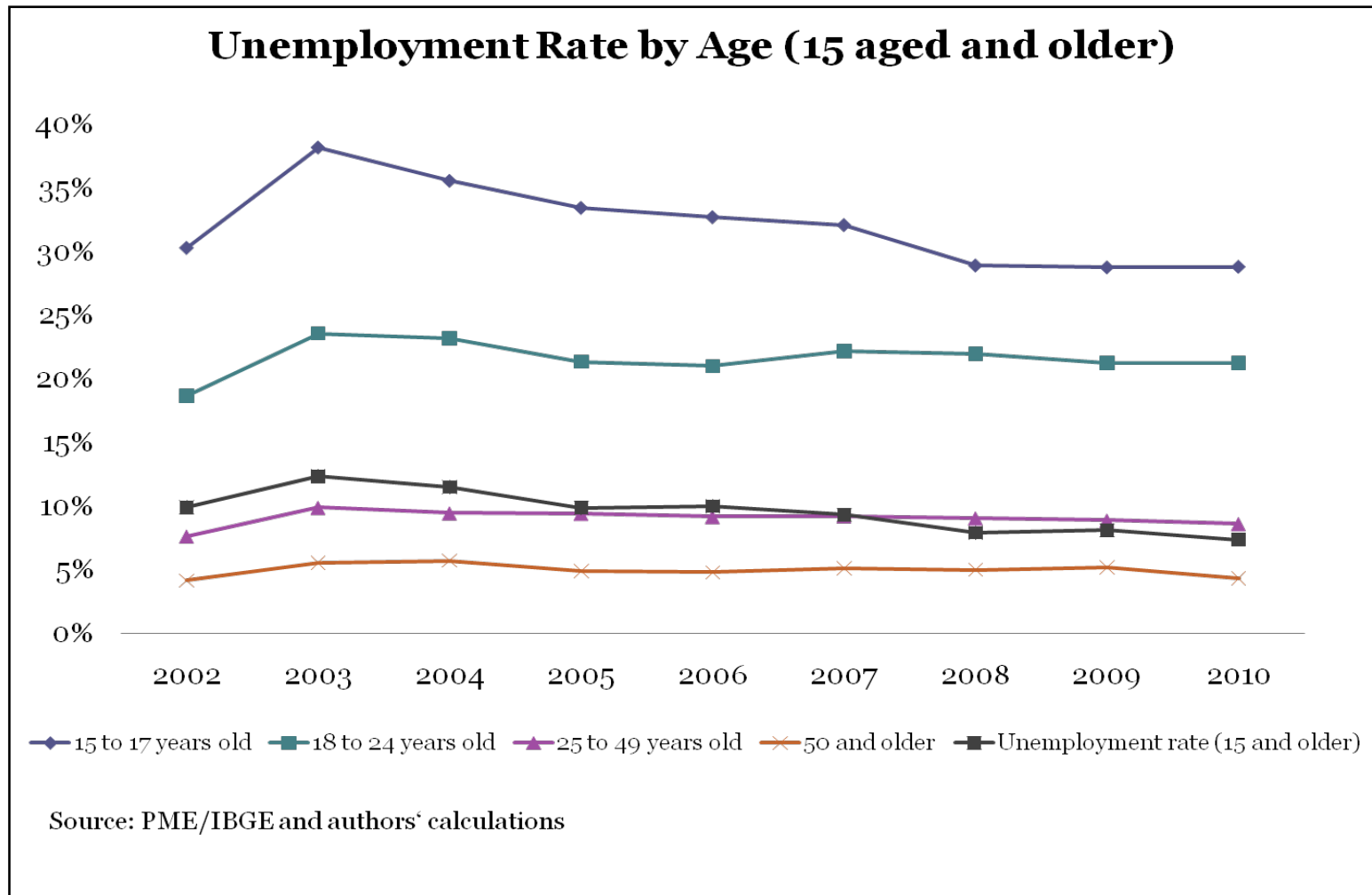


- Unemployment among unskilled workers is higher.

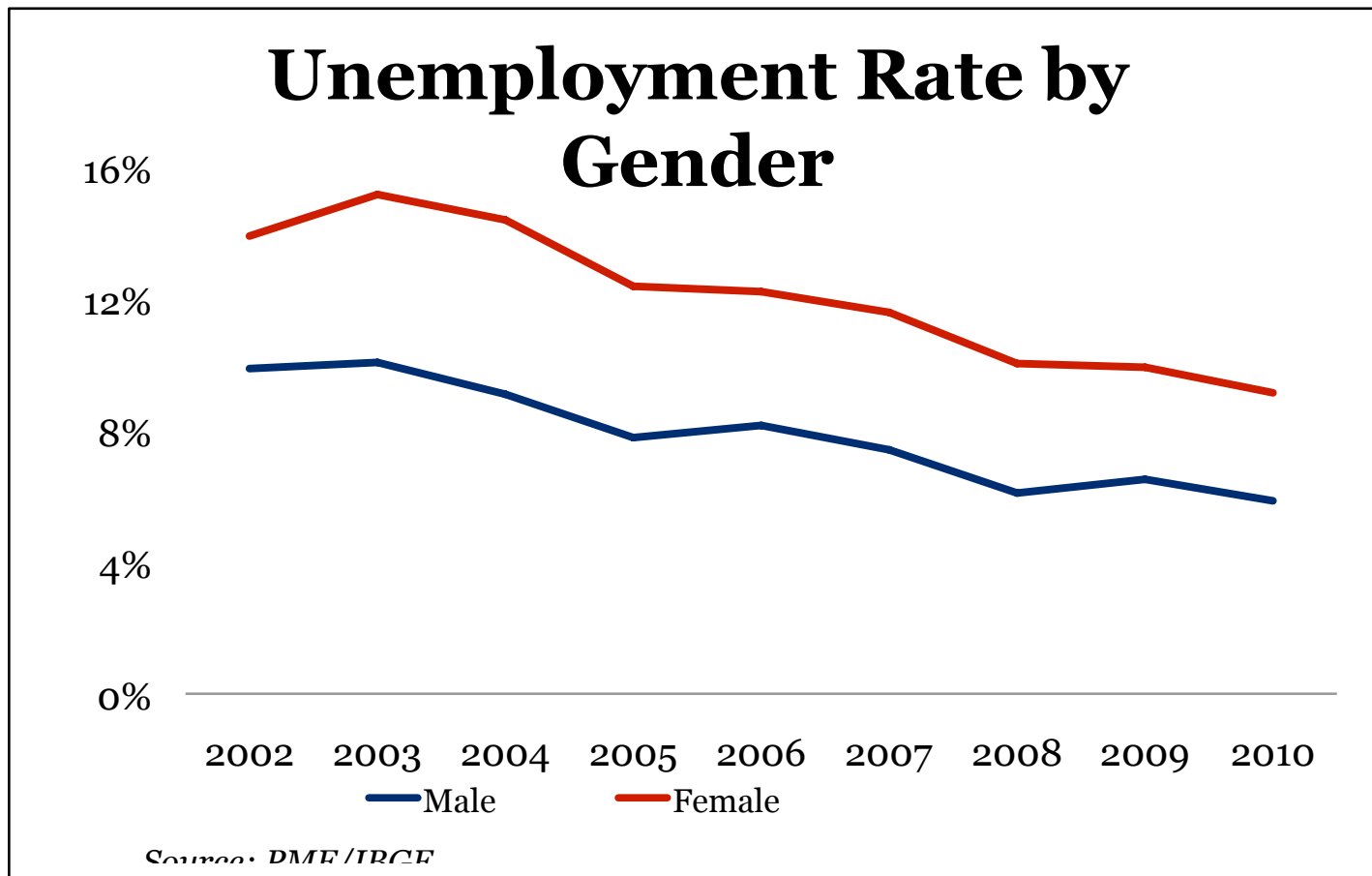


Source: PME/IBGE and authors' calculations

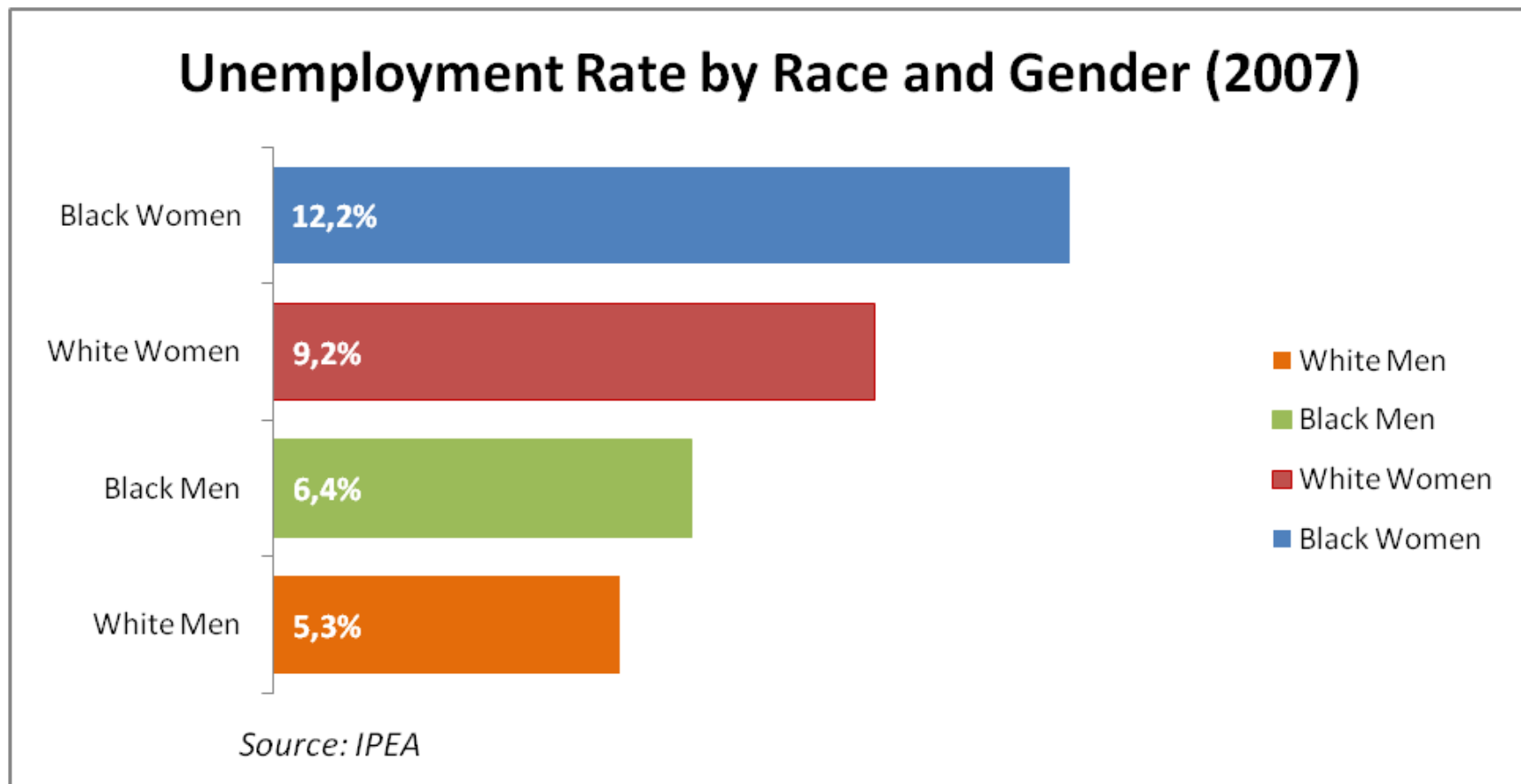
- Unemployment among youth significantly higher



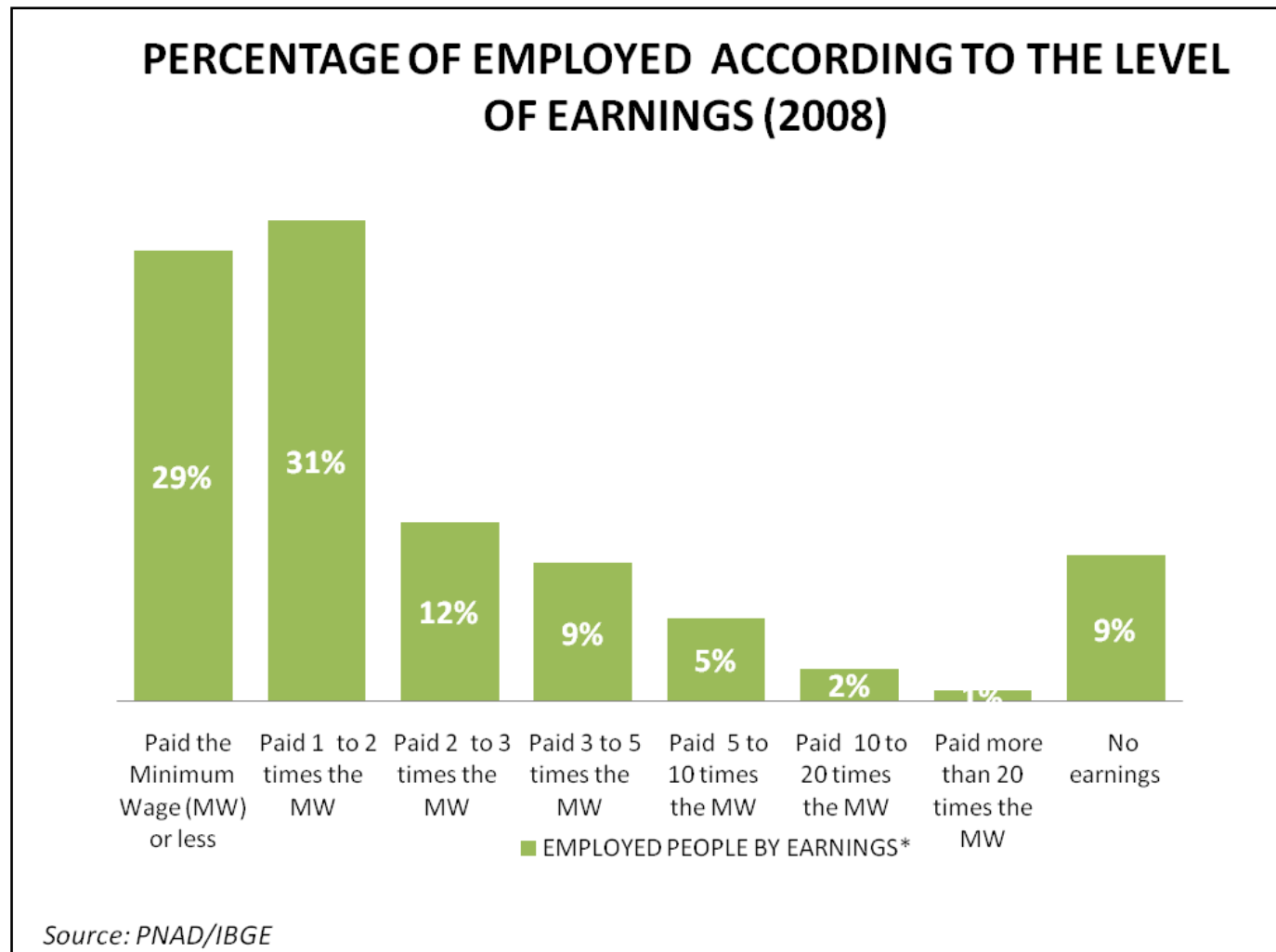
- Unemployment among women significantly higher than among men



- Unemployment rates by gender and race.



- In Brazil 29% of the employed people earned less than the minimum wage.

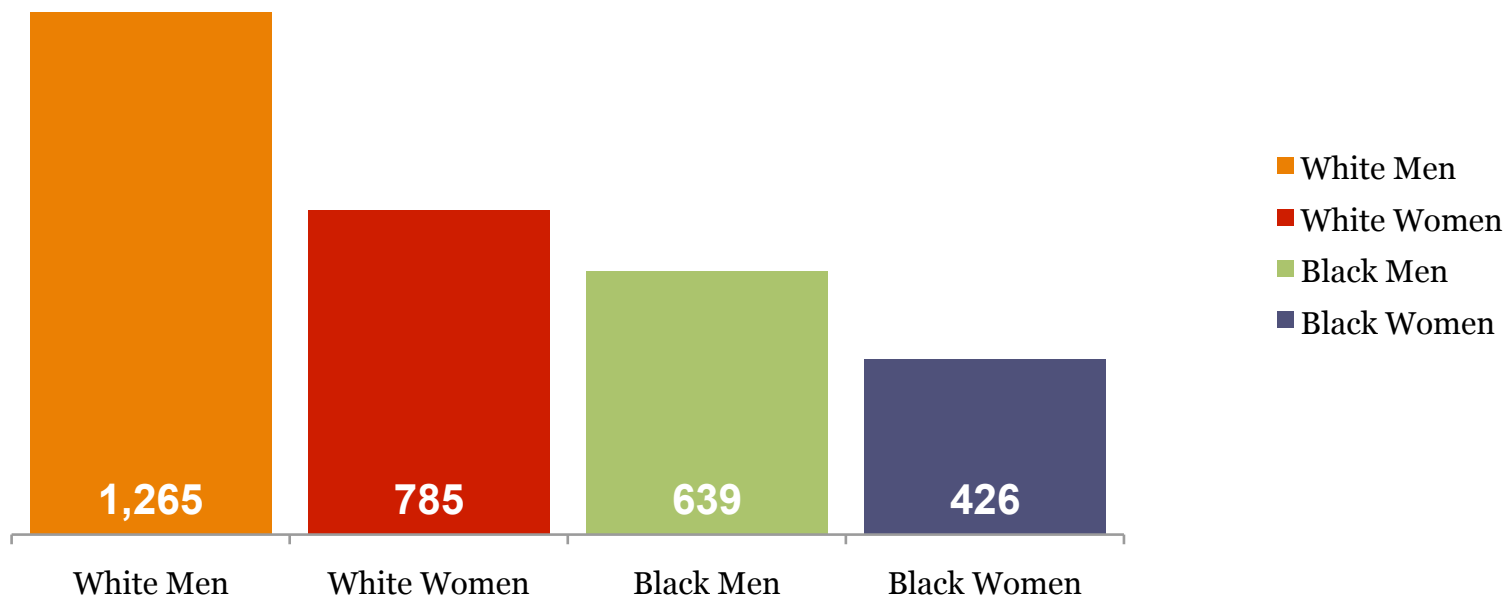


- This number is even higher for employed women. In 2008, 33% of all employed women earned the minimum wage or less.



- Racial and Gender Income Inequality:

Average Income By Gender and Race (R\$ 2007)



- Poverty remains an issue, specially in the Northeast of Brazil where 41,2% of the families are poor (family per capita income is less than 1/2 the minimum wage).

POVERTY AND EXTREME POVERTY BY REGION (2008)	% of Brazilian Families under Poverty and Extreme Poverty					
	Brazil	Region				
		North	Northeast	Southeast	South	Midwest
Families under Extreme Poverty	7,4	10,7	17,0	3,2	2,8	4,3
Families under Poverty	15,2	21,8	24,3	10,6	10,0	13,8
TOTAL	22,6	32,5	41,3	13,8	12,8	18,1

GENDER AND REGIONAL INCOME INEQUALITY	Real Monthly Average Earnings (R\$)					
	Brazil	2008				
		North	Northeast	Southeast	South	Midwest
Male	913	705	540	1,091	1,091	1,126
Female	514	400	342	595	605	601
Total	706	547	438	831	840	858

- 35% of heads of the household are women and they earn significantly less than men.
- 28% of the Brazilian population live in the Northeast.

- In 2008, the employed population with less than 3 years of study (17 million people) earned, on average, less than the minimum wage.

Employment and Average Earnings by Educational Attainment						
Years of Study	Employed People (in thousands)			Average Earnings (2008 R\$)		
	2004	2008	Δ %	2004	2008	Δ %
3 years of study or less	17,067	14,945	-12.4	331.75	413.78	24.7
4 to 7 years of study	22,078	20,760	-6	499.62	586.68	17.4
8 to 10 years of study	13,538	15,307	13.1	602.7	692.04	14.8
11 years of study or more	27,608	36,950	33.8	1,446.68	1,509.96	4.4
Source: IBGE						



ELR Simulation

LABOR FORCE, EMPLOYED, UNEMPLOYED, and NOT IN THE LABOR FORCE			
		2008	%
A	LABOR FORCE (thousands)	93,325	100%
A.1	Employed	86,060	92.2%
A.1.1	Less than 8 years of study	33,241	35.6%
A.1.2	8 to 10 years of study	15,275	16.4%
A.1.3	11 or more years of study	37,544	40.2%
A.2	Unemployed	7,265	7.8%
A.2.1	Less than 8 years of study	2,296	2.5%
A.2.2	8 to 10 years of study	1,938	2.1%
A.2.3	11 or more years of study	3,031	3.2%
B	NOT IN THE LABOR FORCE (Millions)	64,885	100%
B.1	Ready and Willing to Work	7,612	12%
B.2	Not Willing to Work	57,273	88%

Potential ELR participants = A.2.1 + A.2.2 + B.1 = 11, 846

COST ESTIMATION

Number of ELR participants:	11,846	
Minimum Wage	R\$ 510	
	(R\$ billions)	(% GDP)
Total Wage cost	72.5	2.31%
Administration and Material Costs	36.3	1.15%
Wage + Material Costs	108.7	3.46%
Payroll costs for employer	49.3	1.57%
GROSS TOTAL COSTS	158.1	5.03%



How many Brazilians would be benefited?

- We estimate that almost 12 million Brazilians would become part of the program.
- That corresponds to 7.5% of the Brazilian Civilian Noninstitutional Population (LB+NLB).
- We estimate that almost all Brazilian families would be out of extreme poverty and hunger.



Direct Impacts:

- We estimate that ELR would have guaranteed employment for 12 million Brazilians at a monthly wage of R\$ 510,00.
- Government spending would increase by **R\$ 108,7 billion** (3.46% of GDP).
- The resulting consumption would have led to **R\$27,2 billion** in **taxes** paid to the government (0.9% of GDP).



Impacts on the Government Budget

- If we take into account the increase in government tax revenues generated by the increased consumption of ELR workers, then, government spending would only increase by 2,56% of GDP.
- When we include the budgetary savings for other social programs and the reductions of social costs of unemployment and poverty, then this number would go down even further to around 1,56% of GDP.

Impact on GDP:

If we consider that in Brazil:

Marginal propensity to consume = 0,75

Marginal propensity to import = 0,25

Marginal tax rate = 0,40

Multiplier = 1,25

- If government spending on ELR increases by 2,56%, Brazilian GDP would have increased by **3,20%**
- If government spending increases by 1,56%, Brazilian GDP would have increased by **1,95%**



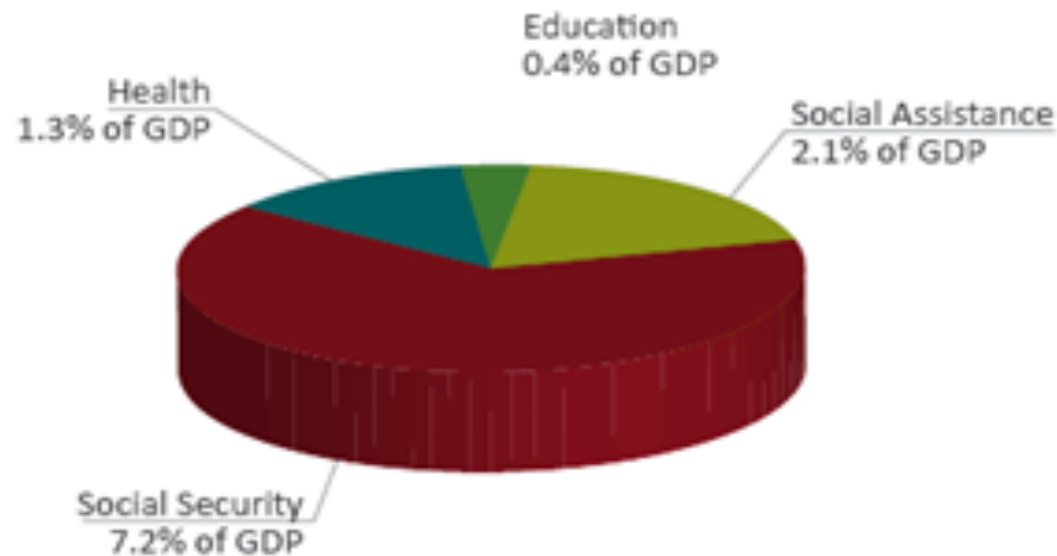
Is it Affordable?

- Of course, Brazil is a sovereign country. The Brazilian government issues its own non-convertible liability.
- It is affordable even according to the tenets of “sound finance”.

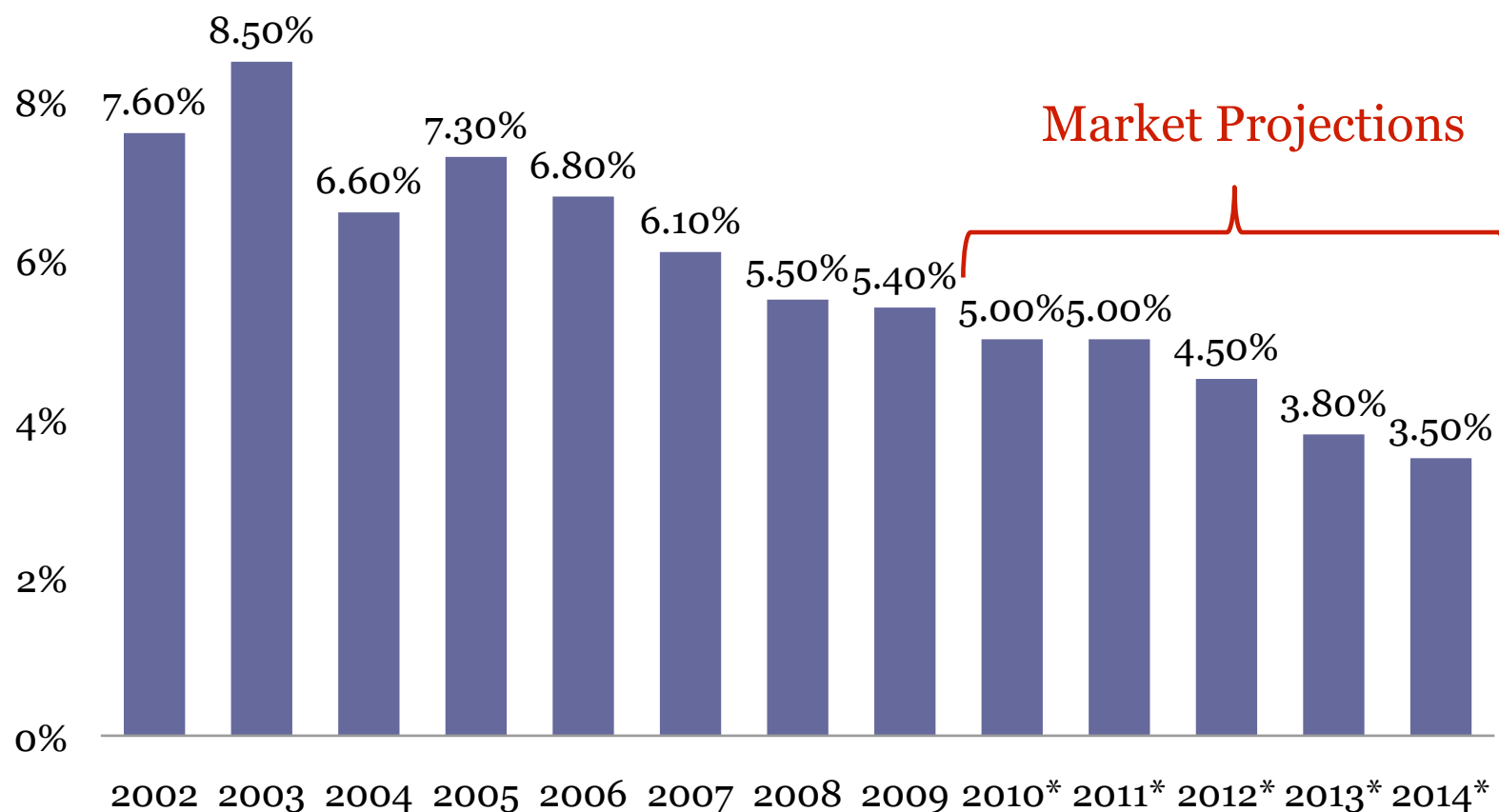
Quality of public spending

In 2009, measures have been adopted to grant the poor and those segments of the population more vulnerable to shocks during the crisis period. These measures focused primary spending on the Social Protection Net, composed by Social Security, Social Assistance, Health and Education.

Social Protection Net - 11,0% of GDP in 2009



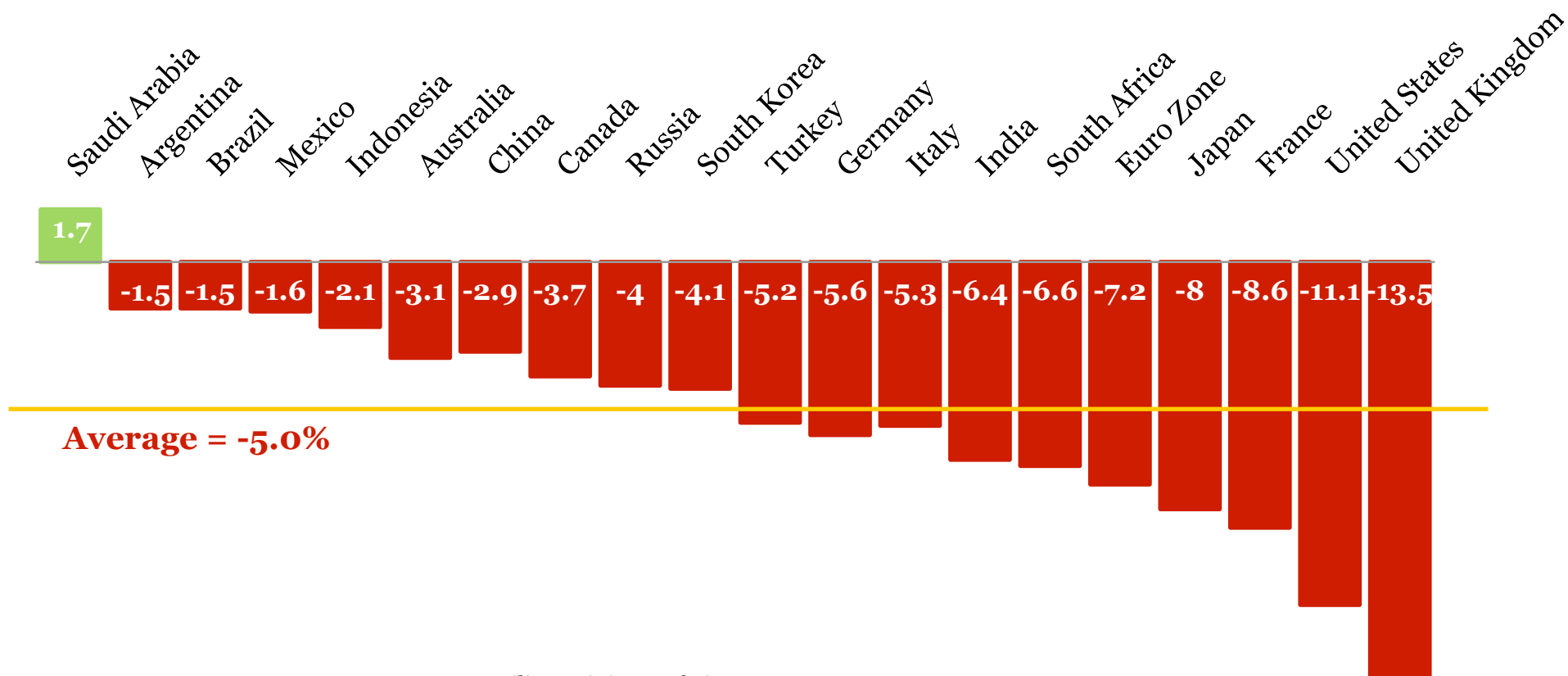
Interest Expense on the Debt Outstanding (% of GDP)



•Estimated

Source: Brazilian Central Bank

Fiscal Result (%GDP) G-20 Economies - 2009



Source: Brazilian Ministry of Finance



Is it inflationary?

- The program is designed to ensure that the deficit spending is at the right level to ensure and maintain full employment.
- Furthermore, program sets a wage anchor and acts like a buffer stock of the unemployed.

Fears and Concerns

- Unsustainable increase in government spending
=> Inflation and Crowding out.
- Creating “dependency” on state
- Unsustainable/Unproductive jobs
- Communities do not have the ability to manage
- Turning ELR workers into commodities
- External Constraints: Impact over current and financial accounts=> Impact over exchange rates



ADDITIONAL BENEFITS

- Can help to reach social targets by mobilizing resources for additional social services to be provided by the community (gender, racial, and regional effects).
- On the job training, learn by doing, strategic human capital management
- Improvement of dignity of those that have been denied the opportunity for social inclusion
- Establishes an *effective minimum wage*



ADDITIONAL BENEFITS

- The percentage of the population living in poverty or extreme poverty would be significantly reduced.
 - No worker would get paid less than the minimum wage and those able and willing to work would be employed.
- Policy targeted directly to those people “at the bottom” of the income distribution.
- Reduce income inequality (29% of the employed people in 2008 earned less than the minimum wage).



ADDITIONAL BENEFITS

- Increases labor force qualification and the productivity of unemployed workers (also increases the labor supply).
- Reduces macroeconomic instability (a major issue for Brazil).
- Induces investment (domestic and foreign).
- Reduces exposure to ROW economic fluctuations.