



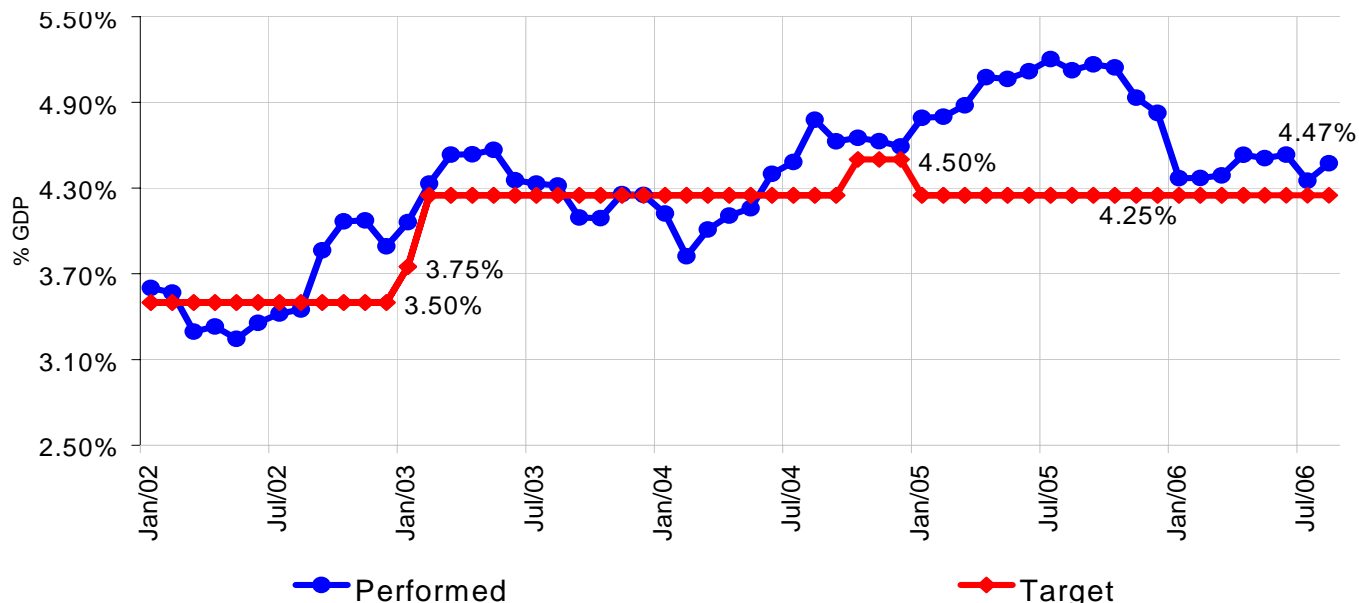
## Outlook for Brazilian Fiscal Policy

Carlos Kawall Leal  
Secretary of the National Treasury  
São Paulo  
16 de outubro de 2006



# Key reasons why we are going to achieve fiscal target in 2006

## Public Sector Primary Result (% of GDP in 12 months)



## Target Versus Performed

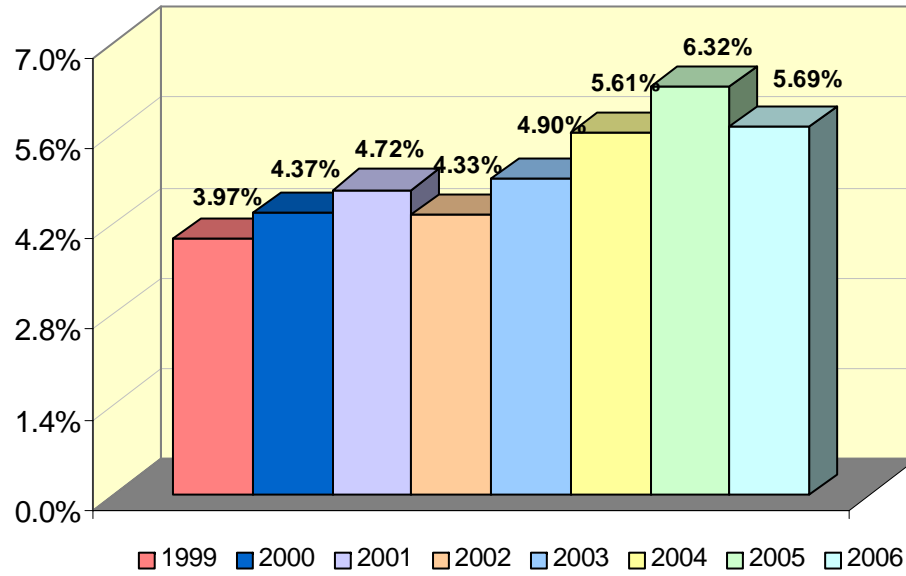
	R\$ billion					
	Target Jan-Aug (a)	Target Jan-Dec* (b)	Performed Jan-Ago (c)	(c) - (a)	% achieved	
					Jan-Aug	Jan-Dec
<b>Federal Government</b>	<b>52.2</b>	<b>67.7</b>	<b>56.8</b>	<b>4.6</b>	<b>109%</b>	<b>84%</b>
Central Government	42.9	50.0	49.4	6.4	115%	99%
Federal Enterprises	9.3	17.7	7.4	(1.9)	80%	42%

\*Decree 5.925/2006



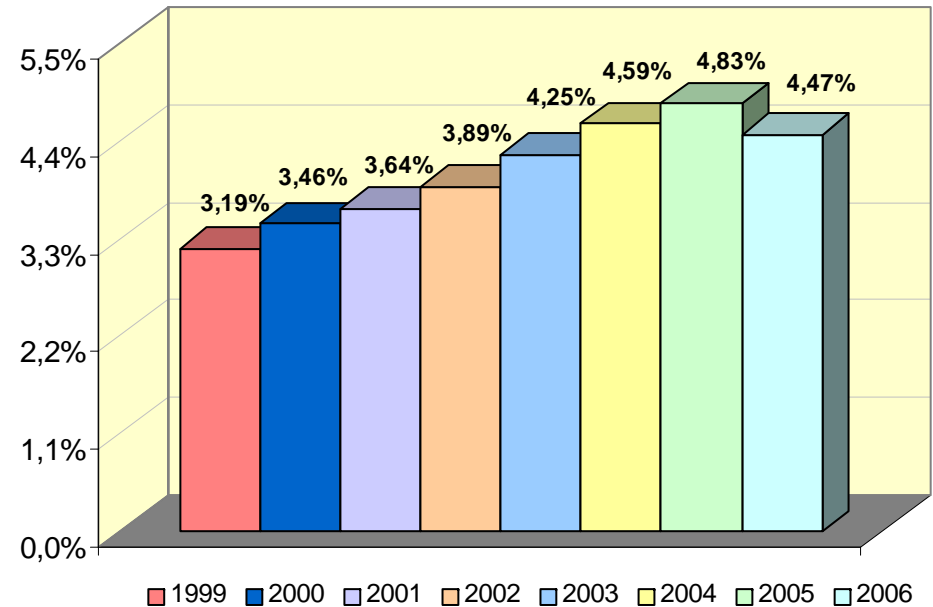
# Fiscal performance remains strong and deny the idea of “fiscal crisis”

Public Sector Primary Result  
(Up to August in % of GDP)



Source: MF/STN

Public Sector Primary Result  
(Annual in % of GDP)



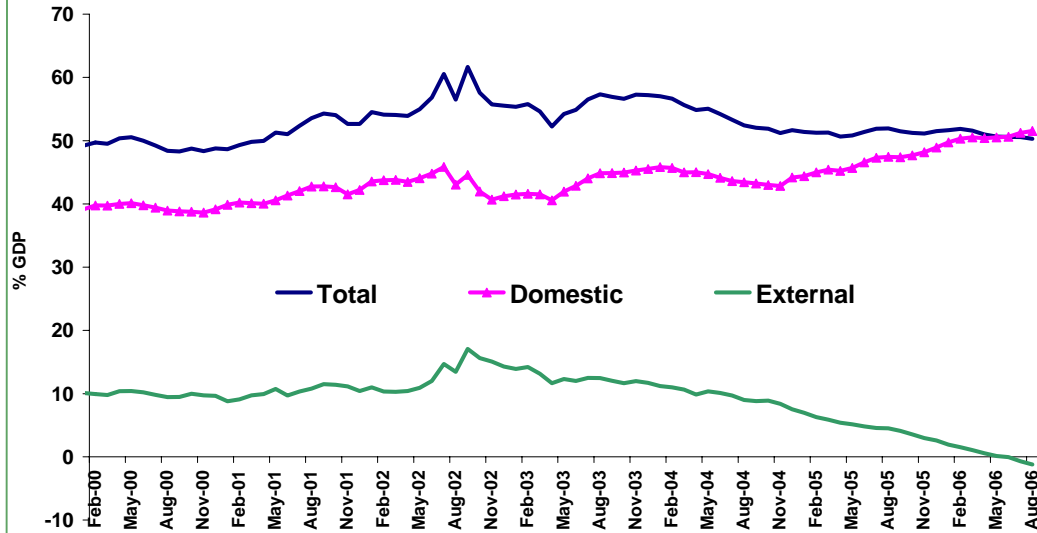
\*2006: in 12 months - August

Source: MF/STN



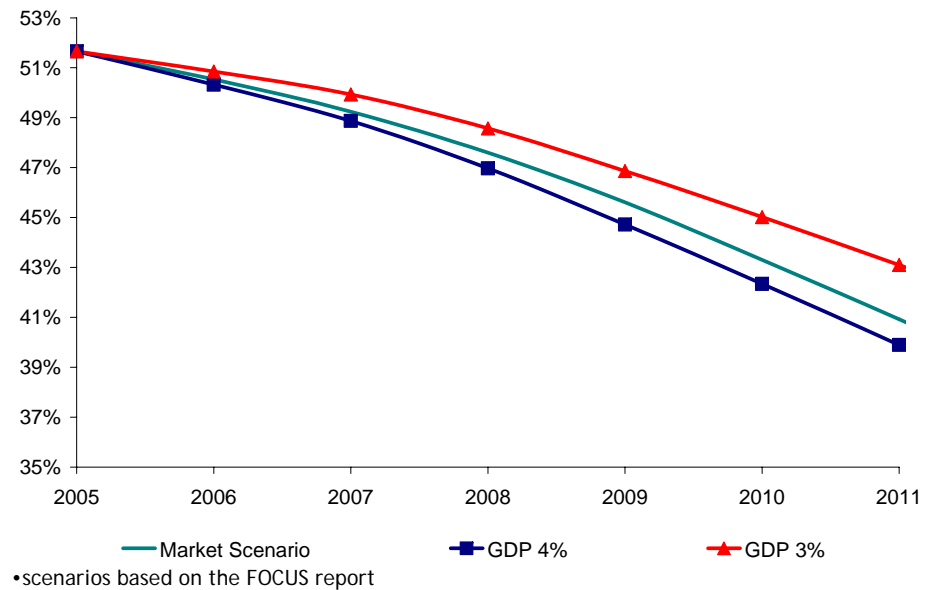
# Primary surplus of 4.25% of GDP assures the reduction of Net Public Sector Debt / GDP

## Net Public Sector Debt / GDP



Source: Central Bank and Finance Ministry/ National Treasury

## Net Debt / GDP\*





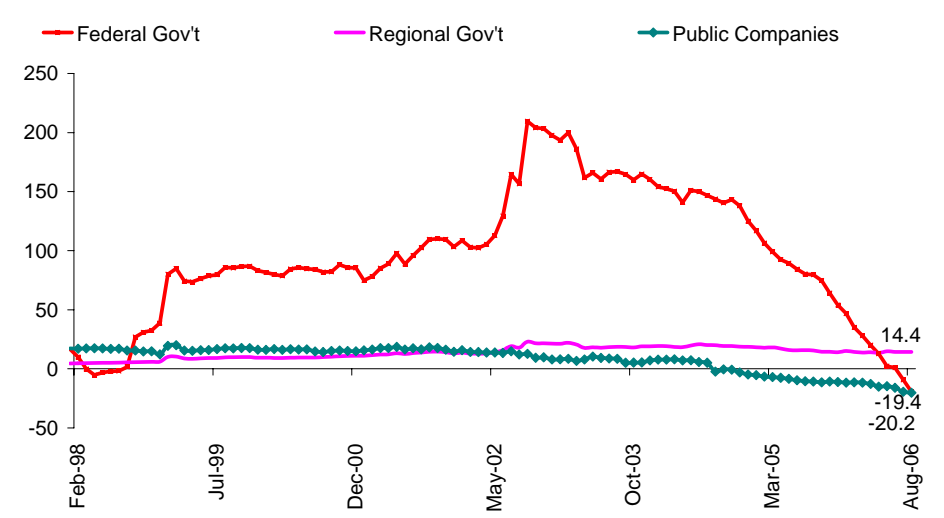
# Brazil has built a barrier against external turbulence, favoring the reduction of real interest rate in medium and long terms...

### Total Net External Debt - R\$ Bn



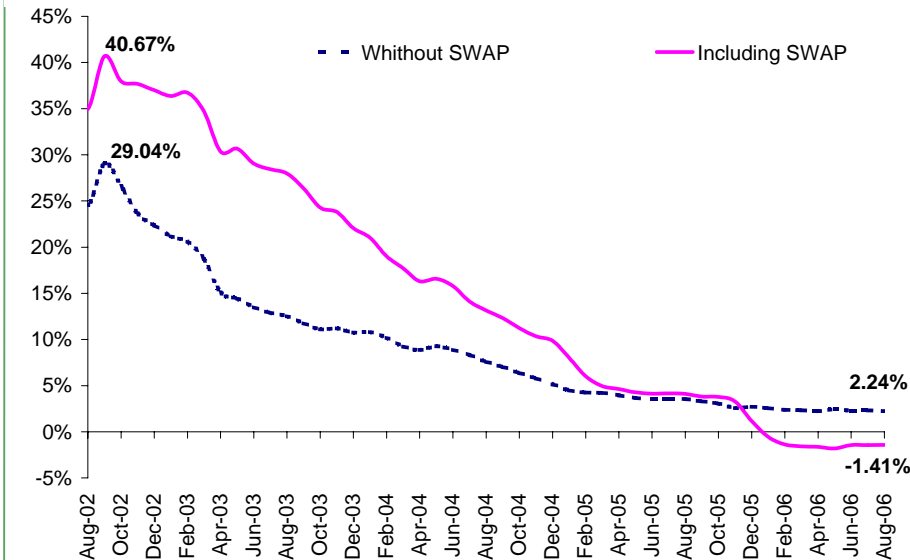
Source: Central Bank

### Net External Debt by Gov't Level - R\$ Bn



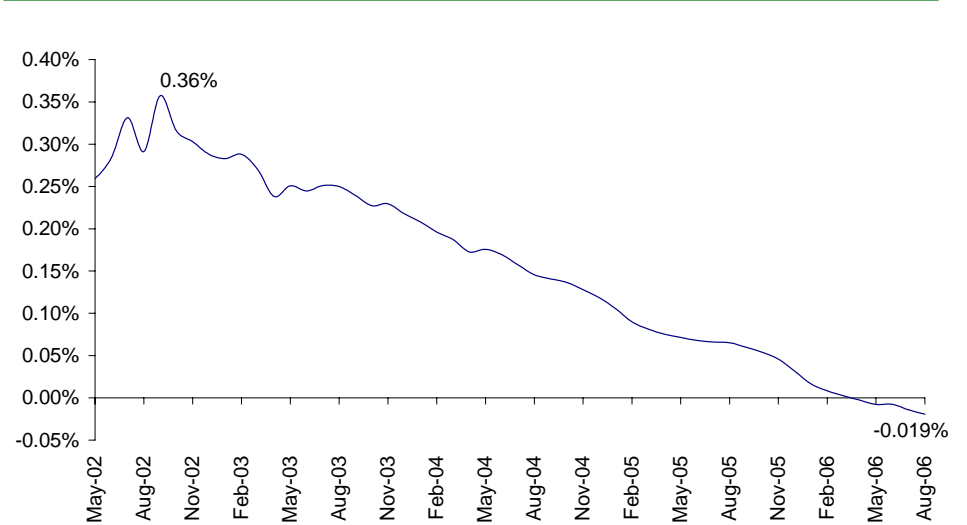
Source: Central Bank

### Dollar-Indexed Domestic Debt as % of Domestic Debt



Source: National Treasury and Central Bank

### Impact of 1% FX devaluation on Net Public Sector Debt/GDP

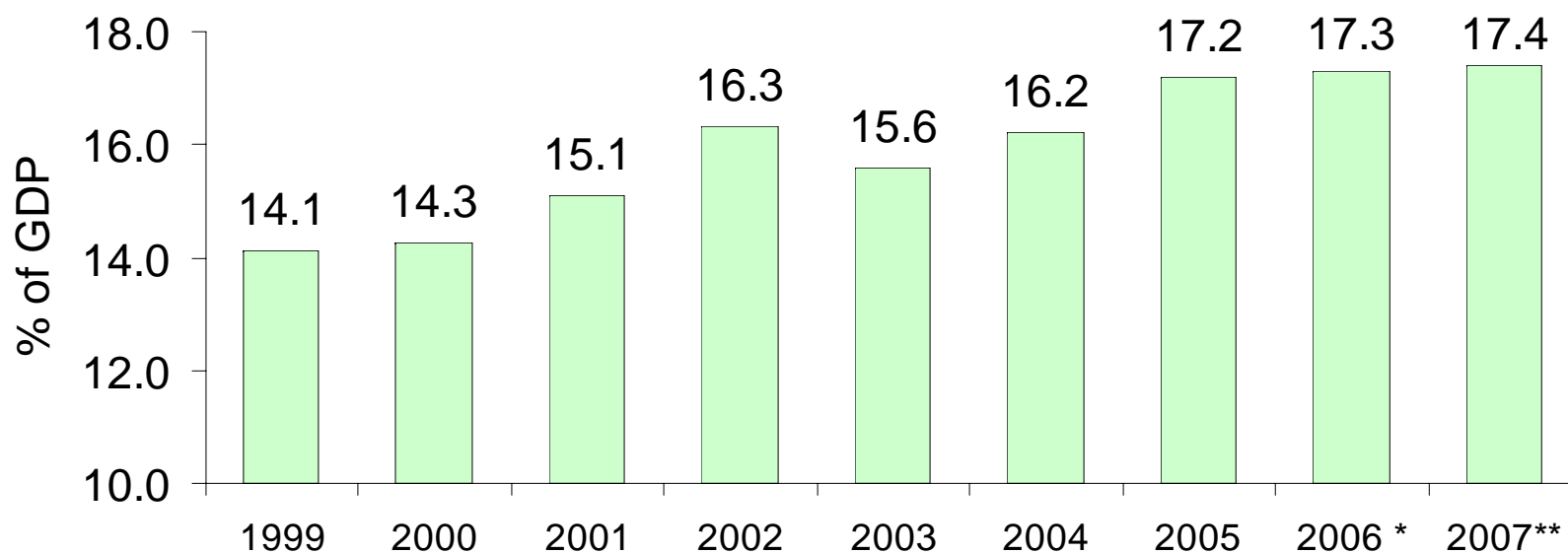


Source: Central Bank



# But fiscal adjustment has been largely underpinned by revenue increases...

SRF-Managed Revenues (% of GDP)



\*Decree 5.925/2006

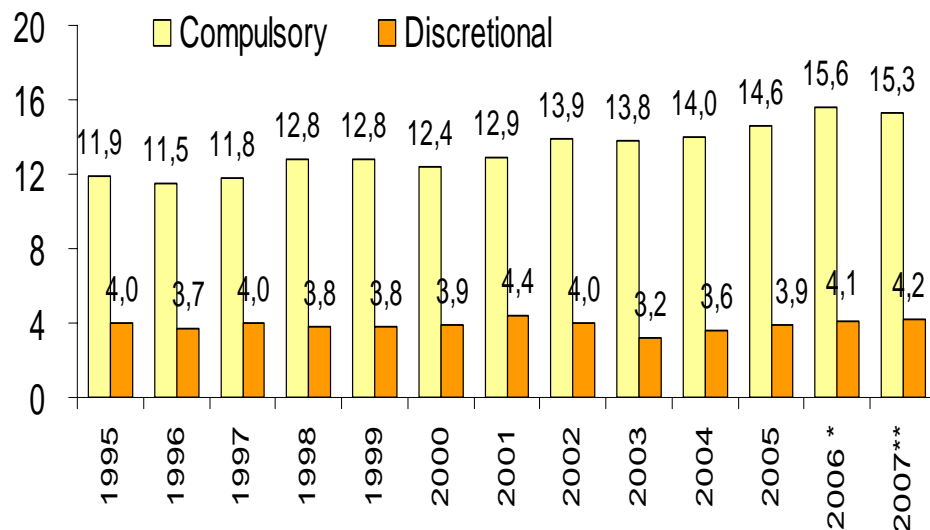
\*\* Budgetary Act Draft 2007

Source: MF/STN



# ... rather than a retrenchment of expenditure commitments

### Compulsory and discretionary expenditures, Cent Gov (%GDP)

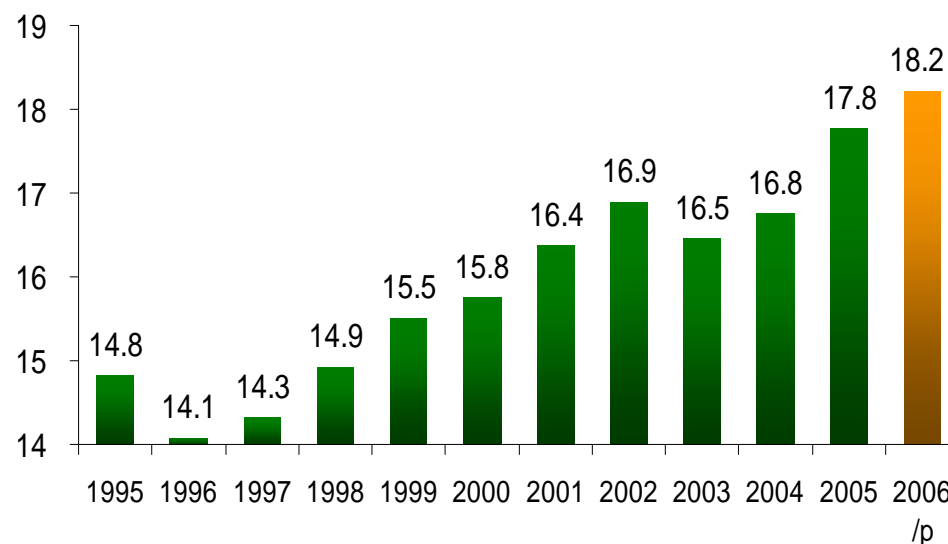


\* Decree 5.925/2006

\*\* Budgetary Act Draft 2007

Source: MPOG/SOF

### Central government current expenditures (% GDP)



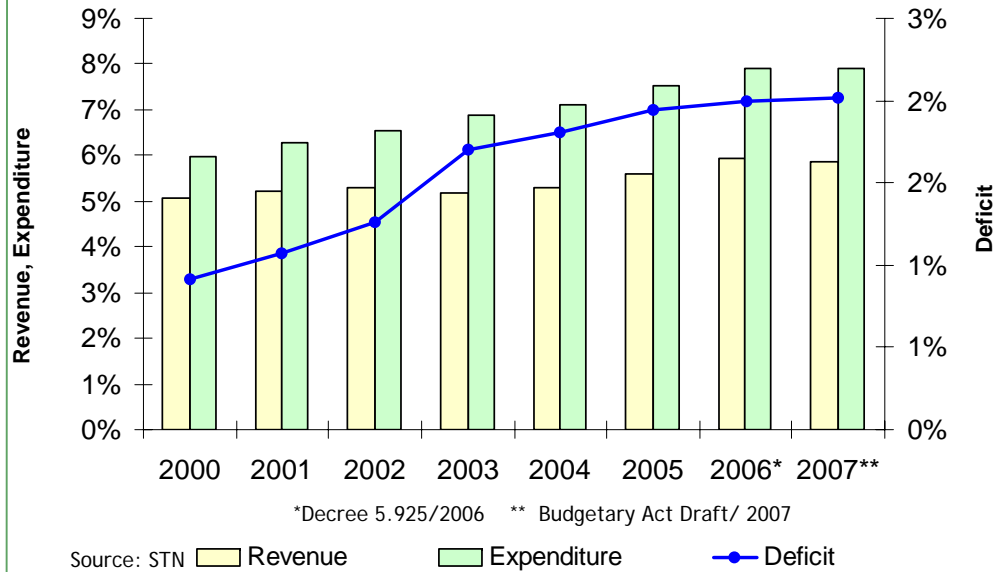
2006: Current authorized appropriation

Source: MPOG/SOF 2006/p: MF/STN



# Social security and welfare benefits are increasing in % of GDP

Social Security (RGPS) Revenue, Expenditure & Deficit (% of GDP)

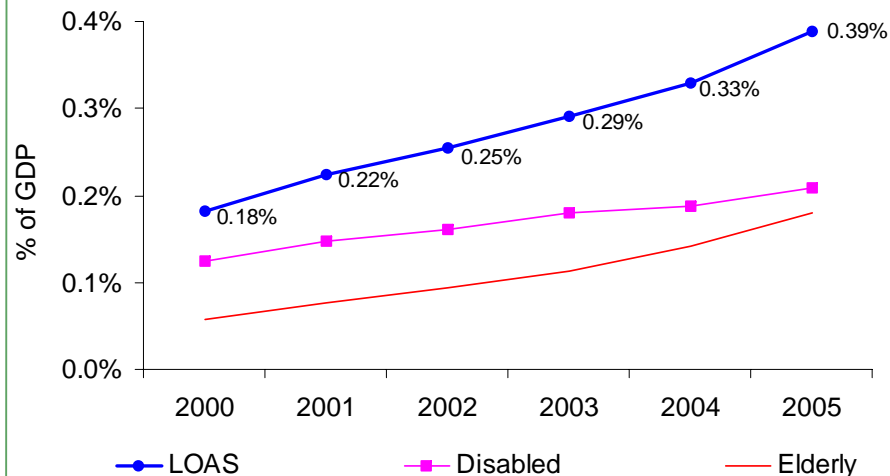


Social Security (RGPS) Revenue, Expenditure & Deficit -- urban and rural workers (% of GDP)

	Net Inflow	Social Security Benefits	Social Security Balance
2000 Total	5.06	5.97	(0.91)
2000 Urban workers	4.92	4.87	0.05
2000 Rural workers	0.14	1.11	(0.97)
2001 Total	5.21	6.28	(1.07)
2001 Urban workers	5.06	5.06	(0.01)
2001 Rural workers	0.16	1.22	(1.06)
2002 Total	5.28	6.54	(1.26)
2002 Urban workers	5.11	5.27	(0.17)
2002 Rural workers	0.17	1.27	(1.10)
2003 Total	5.19	6.88	(1.70)
2003 Urban workers	5.00	5.56	(0.56)
2003 Rural workers	0.19	1.32	(1.14)
2004 Total	5.31	7.12	(1.81)
2004 Urban workers	5.13	5.80	(0.67)
2004 Rural workers	0.18	1.32	(1.14)
2005 Total	5.60	7.54	(1.94)
2005 Urban workers	5.42	6.12	(0.70)
2005 Rural workers	0.17	1.41	(1.24)

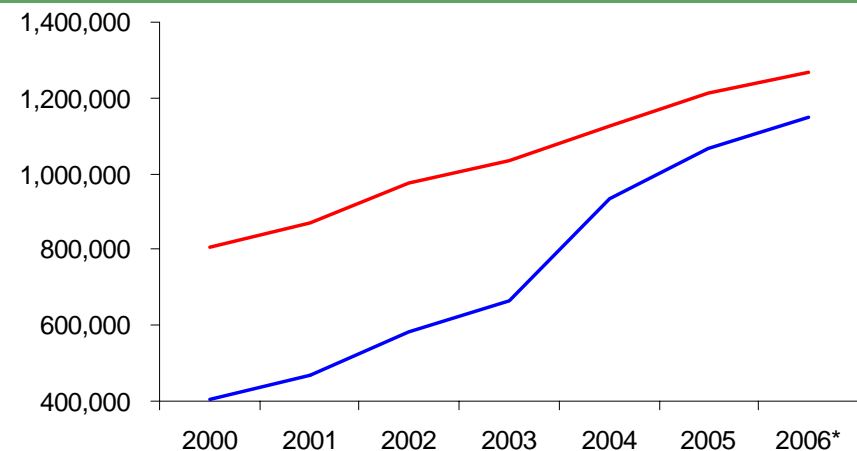
Source: MPS/SPS

Welfare Benefits (LOAS/RMV) in % GDP Accrual Basis



Source: MPS - Boletim Estatístico

Welfare beneficiaries (LOAS/RMV) December figures



\*August Position

Source: MPS - Boletim Estatístico

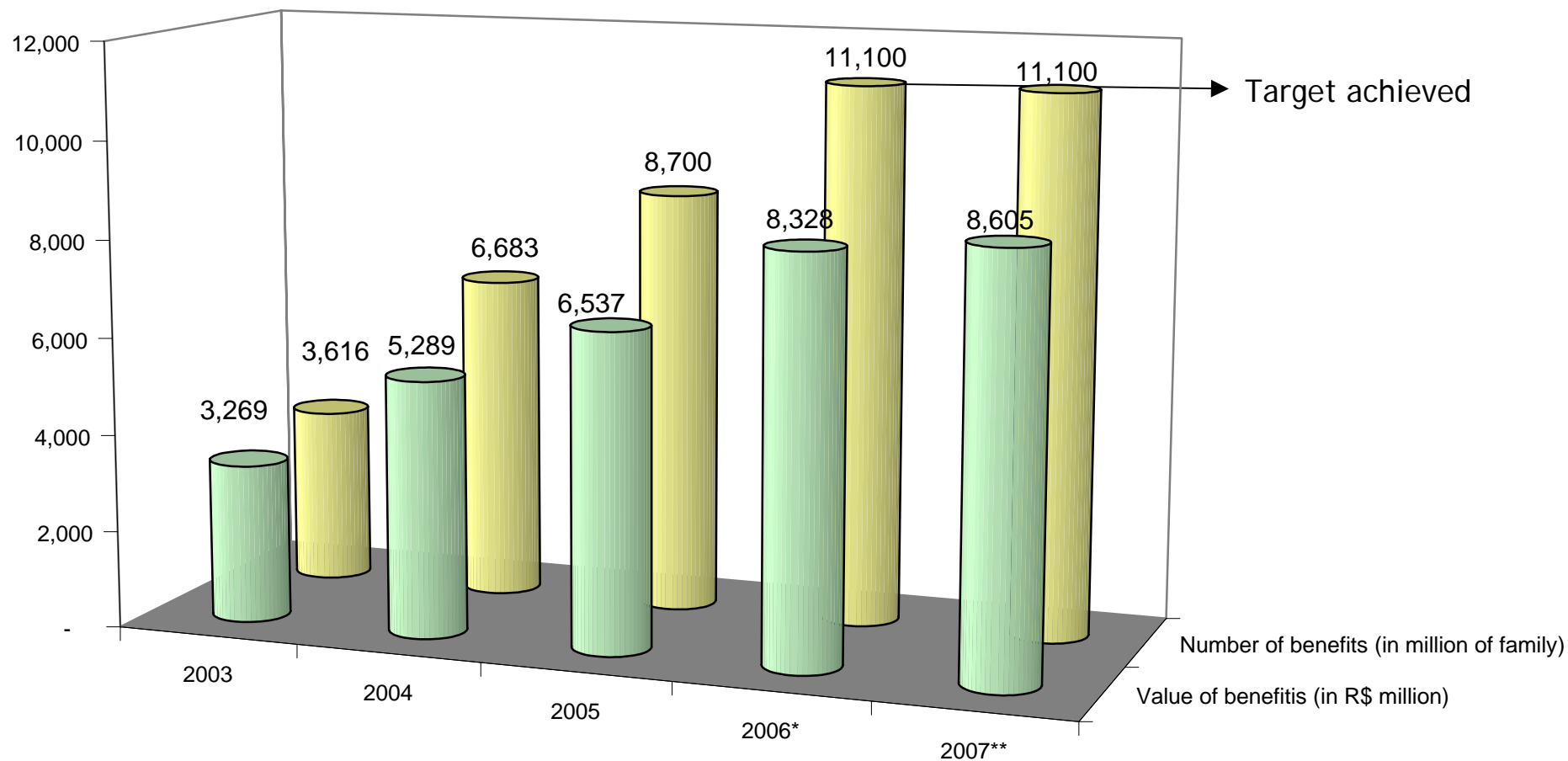
Elderly

Disabled



# “Bolsa Família” became an international reference for conditional income transfers...

## “Bolsa Família” Expenditure



\*Projeção

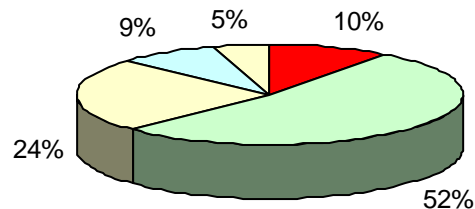
\*\*PLOA 2006



# ... reaching the estimated universe of poor families

## "Bolsa Família" Expenditure

**Regional Distribution of Bolsa Família Expenditure**



■ North ■ Northeast ■ Southeast ■ South ■ Center-West

## Bolsa Família Expenditure per Region Budgetary Law 2007

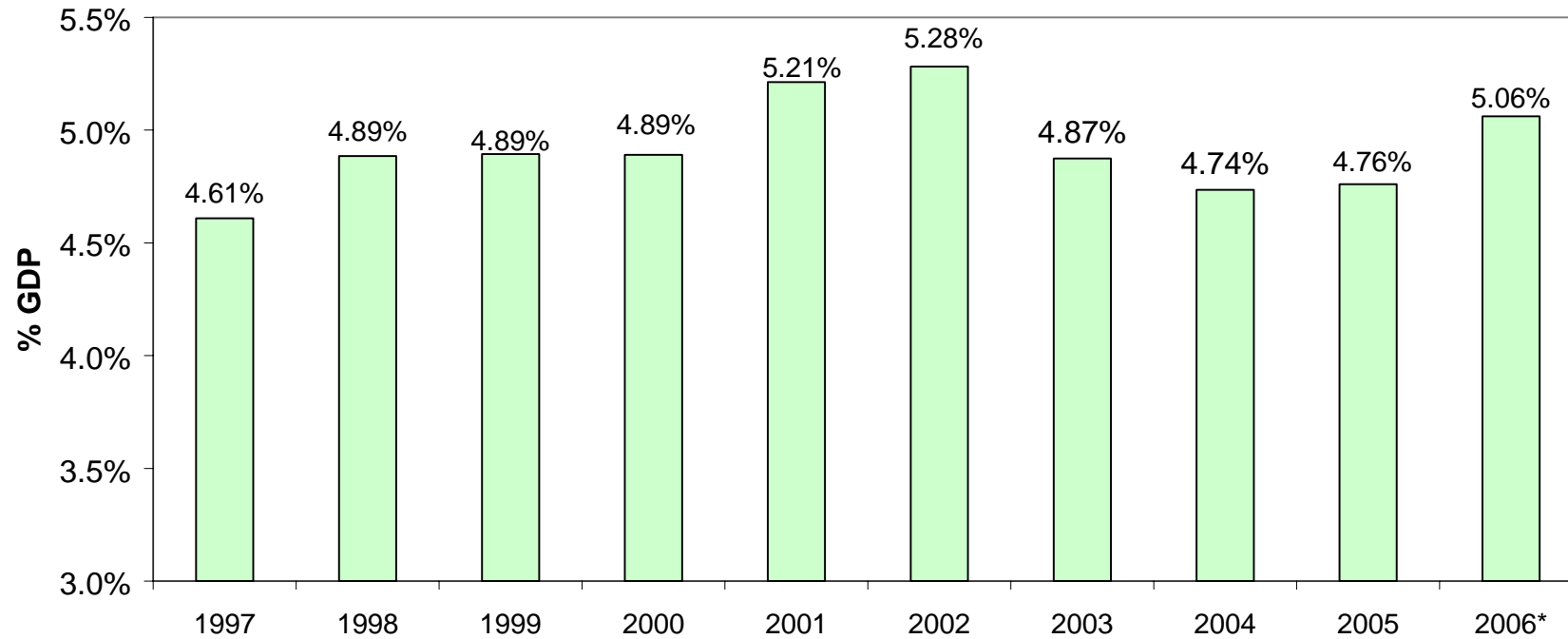
Region	Annual Value R\$	Number of beneficiaries	Monthly Average Value	Number of Poor Families (Pnad 2001 IBGE)
North	857,640,000	1,011,968	70.62	1,134,476
Northeast	4,526,180,000	5,534,610	68.15	5,259,839
Southeast	2,068,350,000	2,907,135	59.29	3,045,159
South	737,050,000	1,057,613	58.07	1,096,279
Center-West	415,980,000	609,027	56.92	668,456
<b>TOTAL</b>	<b>8,605,200,000</b>	<b>11,120,353</b>	<b>64.49</b>	<b>11,204,209</b>

Source: MDS



# Personnel expenditure is also relevant

Personnel expenditure ( % of GDP)



\*Decree 5.925/2006

\*\* Budgetary Draft Law 2007

Source: MF/STN



## Since 2004, tax cuts have become relevant

### Cumulative Effect of tax cuts

Description of the measures (Lei 11.196/05)	2004		2005		2006	
	R\$ billion	% of GDP	R\$ billion	% of GDP	R\$ billion	% of GDP
Incentive to productive investment	0.7	0.04%	3.4	0.18%	6.1	0.29%
Tax cuts to families	0.5	0.03%	2.3	0.12%	4.0	0.19%
Tax exemption for basic basket goods	3.3	0.19%	5	0.26%	5.0	0.24%
Incentive to long term savings	0.8	0.04%	2	0.10%	2.2	0.10%
Incentive to small enterprises			0.3	0.02%	1.4	0.06%
Incentive to technological innovation			0.1	0.01%	0.6	0.03%
<b>Total</b>	<b>5.3</b>	<b>0.30%</b>	<b>13.1</b>	<b>0.74%</b>	<b>19.2</b>	<b>1.09%</b>

Fonte: MF/SPE



## Concluding the diagnosis

- There is no fiscal crisis, but...
- Fiscal adjustment based on tax hikes is no longer sustainable
- Potential growth and competitiveness are threatened by high tax burden
- Low inflation makes public expenditures more rigid
- Public Debt Profile has been improved, but the net debt/GDP ratio should decrease more
- Discretionary public expenditure is small, which hinders investment level, but...
- Brazil has chosen to create a vast array of social welfare programs, which has reduced inequality and improved social indicators
- Coalition presidentialism assumes that fiscal adjustment measures require intense negotiation, different from Russia, India or China.



## Fiscal agenda for the next administration

- Maintenance of public sector consolidated primary surplus of 4.25% of GDP until 2010/11, in order to decrease the net debt/GDP ratio to 40%.
- Multiyear (five to ten years) strategy of tax burden reduction, promoting competitiveness and investment increase, in line with the federative pact.
- The reduction of tax burden should be financed by the reduction of current expenditures relatively to GDP, preserving and rationalizing social expenditures (transfers, health and education).
- Maintenance/elevation of public investment, emphasizing on quality (according to the Investment Pilot Project).

*Negotiation and joint discussion of the reduction of tax burden and expenditures cuts are essential to the political feasibility of fiscal agenda, which shall not forfeit priority social programs (e.g. "Bolsa Família") and investments.*