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November 23, 2020

Statement by Mr. Hilbers and Mr. Cools on Brazil
(Preliminary)
Executive Board Meeting
November 25, 2020

We thank Staff for the excellent report and Mr. Bevilaqua for his insightful Buff statement. This report is a particularly important surveillance product, given the key role of the Brazilian economy in the region. From the Fund's perspective, regional spillovers can have a direct impact on the Fund's credit risk profile, in light of the high concentration of Fund resources in the region. We support the thrust of the report and would like to add the following points for emphasis.

We express our sympathy to Brazil for the losses resulting from the COVID-19 pandemic. The crisis has raised major economic challenges for Brazil. At the same time, Brazil's economy suffers from vulnerabilities preceding the COVID-19 crisis. Brazil's recovery from the 2015-16 crisis was slow, with GDP per capita at the end of 2019 7% below the 2014 level, and total factor productivity currently close to 1980s levels. Going forward, it is important to improve the economy's growth potential. The pension reform passed in October 2019 is an important achievement to that end**.**

We welcome the Brazilian authorities' commitment to an expenditure ceiling and fiscal adjustment. Brazil's fiscal support during this crisis as a percentage of GDP has been among the largest of G20 countries, and twice the average of emerging markets economies. We commend the authorities for thus having more than compensated the impact of the COVID-19 shock on poverty and income inequality. That said, the resulting increase in debt may undermine market confidence and require interest rate hikes. The large and partially unreversed capital outflows of earlier this year show that Brazil is vulnerable to such confidence shocks. Improved policy targeting may help the government to manage a gradual rather than a sudden withdrawal from the current broad-based fiscal support package.

We continue to advocate for a banking reform in Brazil in order to improve total factor productivity growth. Such reform should focus on improving the efficiency of financial intermediation, increasing competition and consequently reducing elevated intermediation costs. We welcome progress on the Brazilian Instant Payments System (PIX) and Open Banking, which will lead to better access to and more competitive costing of financial services.

We welcome the proposal to reform the tax system. The existing imbalance between indirect and direct taxes explains in large part the regressivity of the Brazilian tax system. With the COVID-19 crisis rolling-back Brazil's progress in fighting poverty and inequality, we welcome staff's advice to make personal income taxes more progressive including by introducing dividend taxation. Not only can a tax reform simplify government revenue administration and broaden tax revenues, it will also improve the business climate and attract private investment.

We would like to emphasize the opportunities of trade liberalization. The Brazilian economy is one of the most closed major economies in the world. Greater openness to trade would improve productivity growth.

We hope Brazil will be able to propose concrete labor market regulations to integrate informal workers into the formal economy. A large informal sector complicates the provision of government support, exacerbates unemployment shocks, and undermines the business climate.

Finally, we are disappointed to see relatively minor mentions of climate change in the report. The Amazon is one of the world's most important pieces of natural heritage and biodiversity, but is threatened by excessive deforestation, in part driven by environmentally unsustainable production methods. IMF Staff should help facilitate Brazil's green recovery from the current crisis by providing policy advice on a sustainable recovery, as well as providing advice on climate change mitigation and adaption.