The coronavirus crisis and counter-cyclical policies in Brazil[*]

Luiz Fernando de Paula[**]

This paper examines the Brazilian economy during the coronavirus pandemic and the economic policies implemented in 2020 to address the economic and social crisis. Using primary and secondary sources, the article differs in its analysis from other heterodox approaches according to which state action in response to the pandemic crisis in Brazil was weak and inconsistent. It is argued that counter-cyclical actions, especially those relating to emergency aid, have had a strong counter-cyclical effect on the economy and on reducing poverty and social inequality, even though there was no strategy previously coordinated by the federal government. The article concludes that the poor outlook for the Brazilian economy relates to both the resumption of orthodox policies and the unleashing of a second wave of the coronavirus pandemic, both contributing to a slow recovery of the Brazilian economy

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INTRODUCTION

From the time the World Health Organization (WHO) declared COVID-19 a pandemic, on 3 March 2020, social distancing was the recommended public-health measure to control the spread of the coronavirus pandemic. This entailed a set of measures including isolation at home, remote working, suspension of in-person school classes and even restrictions on freedom of movement. These measures affected the supply side of the economy, by restricting workers' mobility and access to the workplace and, at the same time, the demand side, partly paralysed by the restrictions imposed by the public-health crisis, which affected household consumption directly and investment decisions indirectly. In particular, the coronavirus crisis hit economic sectors unevenly, the most adversely affected being service and trade. The social consequences of the economic crisis, from loss of income and employment, are extreme.

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[**] Professor of Economics at the Federal University of Rio de Janeiro (IE/UFRJ, Brazil), Voluntary Professor at the University of the State of Rio de Janeiro (IESP-UERJ, Brazil) and CNPq and FAPERJ researcher; email: luiz.fpaula@ie.ufrj.br; ORCID: https://orcid.org/0000-0001-9770-516X.

Brazil has been applying orthodox economic (monetary and fiscal) policies since 2015, and since 2016 has begun to introduce a set of liberal reforms, including: (i) a constitutional ceiling on public spending, effective from 2017, which (in real terms) freezes government spending for 20 years, since public spending is adjusted only by the previous year's inflation, a type of fiscal rigidity that exists only in Brazil;[1] (ii) a labour reform, effective as of November 2017, to make the labour market more flexible by allowing, among other things, temporary contracts, intermittent work and the possibility of a 12-hour working day; and (iii) a pension reform, approved in November 2019, which raised the minimum retirement age, extended the minimum contribution period and made other changes.

During this period, the governments of both Temer (2016–2018) and Bolsonaro (2019 to date) promised to restore growth by pushing through liberal reforms on the hypothesis of expansionary fiscal contraction – fiscal adjustment achieved by cutting public spending to increase the confidence of agents and stimulate private spending by firms and households (Alesina/Ardagna 2010) – and on the 'confidence fairy' argument, according to which liberal policies help unshackle entrepreneurial animal spirits from the State. Economic performance has been disappointing, however, with the economy semi-stagnant in 2017–2019 (GDP growth averaging 1.5 per cent per year), while unemployment has remained high and the labour market continued to be precarious, as informal and partial work have expanded. Social inequality worsened in this period: between 2015 and 2019, the Gini Index increased from 0.525 to 0.543, mainly due to the decline in labour income (Barbosa et al. 2020). The main problem of the Brazilian economy lay not on the supply side, but in insufficient aggregate demand to support growth (Oreiro/Paula 2021: ch. 4).

This paper examines the Brazilian economy during the coronavirus pandemic and the economic policies introduced in 2020 in response to the economic and social crisis. The analysis differs from other heterodox analyses by Brazilian economists who find that State action to address the economic effects of the pandemic was 'weak and inconsistent,

[1] Constitutional Amendment 95, imposing the spending cap, prevents any fiscal policy management, which is a fundamental tool for smoothing out the economic cycle: if the economy grows faster than expected, government revenues will rise more than forecast, but it will be unable to spend the surplus, because its expenditures are limited by the rule just introduced; on the other hand, as the spending cap rule requires zero real growth in total spending, any real increase in mandatory expenditures entails reducing discretionary spending in the same amount, so that total primary expenditures remain constant and do not exceed the target (Barbosa 2019).

as fundamental policies were not implemented' (Araújo et al. 2020: 31) and that the combination of measures taken in Brazil was 'timid, slow and uncoordinated' (Paludetto et al. 2020: 28).

In this article, it is argued that counter-cyclical actions, in particular those relating to emergency aid transfers, had strong counter-cyclical effects on the Brazilian economy and contributed to reducing poverty and social inequality during the coronavirus crisis. This occurred despite the lack of any prior coordinated strategy by the Brazilian federal government to meet the economic and social crisis: the measures were often taken due to pressure from public opinion and/or at the initiative of Congress.

This paper is divided into four sections, in addition to this introduction. Section 2 considers the effects of the coronavirus crisis on the Brazilian economy and Section 3 examines the measures taken in Brazil to tackle the effects of the COVID-19 pandemic. Section 4 analyses the impacts of the measures implemented in Brazil and Section 5 concludes the article.

EFFECTS OF THE CORONAVIRUS CRISIS ON THE BRAZILIAN ECONOMY

The coronavirus crisis affected the Brazilian economy immediately and made itself felt through two channels: one external and the other domestic.

In March 2020, the external channel saw intensive capital flight in both debt portfolio and equity portfolio. Capital flight was led by non-residents with positions in assets denominated in Brazilian currency, which created a new form of external vulnerability, which Bank for International Settlements (BIS) economists labelled 'original sin redux', where capital outflows from non-residents, in addition to contributing to deflating domestic financial asset prices, generate strong exchange-rate devaluation (Carsten/Shin 2019). Capital outflows reached record levels in emerging economies during the peak of the coronavirus crisis in March 2020 and, in the case of Brazil, were driven mainly by investments in debt securities (cf. Figure 1).

In comparison with other emerging economies, Brazil experienced major currency devaluation (27.2 per cent from 11 March to 14 May 2020), followed by huge exchange-rate volatility (cf. Figure 2). As can be seen in Figure 3, the pass-through of exchange-rate devaluation to domestic prices was low until August 2020: the consumer price index (IPCA) stayed well below 4.0 per cent per year, the official inflation target for 2020.

<Place Figures 1 and 2 about here>

In Brazil, the shock to economic activity resulting from the outbreak of the COVID-19 pandemic was immediately transmitted to the financial system ‘in terms of liquidity needs, among which disbursements of daily mark-to-market settlements and margin calls for derivative transactions in [B]3 – due to the market volatility –, drop in the availability of external funding, high withdrawals from open credit lines and households and companies credit operations restructuring and renegotiation process’ (BCB 2020: 13). On the other hand, in March and April 2020, agents rapidly reallocated portfolios towards more liquid financial assets (especially government bonds with shorter maturities or repo operations), particularly on the fixed income markets, with a huge fall in financial asset prices and a sharp decrease in liquidity in the financial market (Martins et al. 2020).

The impact of the coronavirus crisis on Brazil’s GDP was very strong and immediate, as of March 2020, but particularly in the second quarter, although rates continued to be negative throughout the year, except for a slight recovery in industry in the fourth quarter. The fall in GDP growth reflected the contraction in services and industry, while agriculture maintained its initial high growth due to commodity exports (cf. Figure 4).

<Place Figures 3 and 4 about here>

The level of idleness in the Brazilian economy was high in the period before the coronavirus pandemic. As can be seen in Figure 5, utilization of installed industrial capacity, which had been below 80 per cent since mid 2015, fell to 66.5 per cent in April 2020 and recovered only in July. Unemployment increased from 11.0 per cent in the fourth quarter of 2019 to 14.6 per cent in the third quarter of 2020, while the percentage of ‘discouraged’ – including those who do not seek work immediately because they think they will not get a suitable job – in the total of the economically active population increased from 4.2 per cent to 5.4 per cent in the same period. In fact, many unemployed workers decided to stop looking for work during the coronavirus pandemic. Thus, the sum of the unemployed and discouraged increased to 20 per cent of the economically active population in the third quarter of 2020 (cf. Figure 6).

<Place Figures 5 and 6 about here>

In particular, informality (workers without a formal contract) reached 41.1 per cent of the employed population in 2019, showing the duality of the Brazilian labour market, where a significant portion of the population works informally, some of them pursuing their activities on the street. It should be added that formal employees work largely in commerce and home services, have little or elementary schooling and with little (or reduced) possibility of working remotely and thus maintaining income during the pandemic (Pero et al. 2020: 92). Accordingly, when the coronavirus pandemic started in Brazil, large numbers of people were in situations of potential vulnerability. This posed a major challenge for policymakers in that emergency programmes had to be directed to both formal and informal workers.

With regard to the bank credit market, the contraction in credit granting occurred in March 2020 for households and in April for corporations (cf. Figure 7). In the case of corporate credit, the growth in March is due to loans to large companies, which sought resources to strengthen their liquidity, to finance the production chain and to protect themselves from exchange-rate variations (BCB 2020: 6); however, the credit-growth rate fell sharply from April to June for both large and small and medium-sized companies (cf. Figure 8). Debt renegotiation to extend time-frames – as favoured by the National Monetary Council (CMN[2]) regulations allowing financial institutions to extend repayment terms for credits previously granted – was an influence in improving problematic asset ratios for companies of all sizes. In credits granted to households, the greatest slowdowns occurred in vehicle financing and credit cards, where recovery resulted partly from renegotiation of previous operations (BCB 2020: 7).

<Place Figures 7 and 8 about here>

[2] The CMN is a government council that sets inflation targets and formulates exchange-rate, monetary and credit policy rules in Brazil.

MEASURES TAKEN TO COUNTER THE EFFECTS OF THE CORONAVIRUS CRISIS

First measures

International experience has shown that, in order to respond to the economic and social consequences of the coronavirus crisis, four kinds of measures are necessary: (i) aid for the people worst affected by the crisis, through either direct income transfers, expansion of unemployment insurance, compensation for workload reduction, etc.; (ii) maintenance of cash flow for companies losing revenue as a result of the total or partial paralysis of economic activity, which calls for a set of relief measures, including financing working capital (especially for small and medium-sized companies), postponing tax payments, reducing working hours, etc.; (iii) financial support for state and municipal governments to offset lost tax revenues, especially in countries like Brazil where these sub-national entities are prohibited from issuing public debt; and (iv) expansion of the public-health system to cope with the public-health crisis.

The Brazilian government's initial response to the economic and social crisis that resulted from the coronavirus pandemic was ambiguous. The first reaction to the public-health crisis from Economy Minister Paulo Guedes, an economist known for his Chicago School training – he gained his PhD in Economics from the University of Chicago in 1978 – was that 'reforms are the best answer to the coronavirus crisis'. In March 2020, the federal government implemented a set of counter-cyclical measures with no fiscal impact, which included: (i) postponing payment of company tax contributions; (ii) postponing and/or reducing by up to 95 per cent employers' social security contributions for companies with up to 100 employees affected by the pandemic; and (iii) anticipating wage bonuses for workers and 13th wage payments to retirees. It also redeployed resources to the Unified Health System (SUS) and took steps to reduce the queue for the '*Bolsa Família*' conditional cash transfer programme (to include more than 1 million beneficiaries) and initially provided a total of R$16 billion in financial aid to states and municipalities. These measures proved clearly insufficient to deal with the economic and social crisis. This forced the federal government, after a strong civil society campaign and at the initiative of the National Congress, to implement an emergency cash transfer programme for the most vulnerable, as a huge portion of the population are informal workers, as well as an emergency programme for maintaining formal employment. As pointed out by Blofield et al. (2021: 5), 'Like Argentina, Brazil moved quickly to alleviate the economic fallout from COVID-19 … , although unlike in Brazil, a share of the impetus came from civil society and the opposition rather than the executive itself'.

One fundamental step towards meeting the economic crisis that resulted from the public-health crisis was the state of public calamity decreed by Congress (Legislative Decree No 6, of 20 March 2020) until 31 December 2020, which allowed the Brazilian government to miss fiscal targets set by the Fiscal Responsibility Law and the Budget Guidelines Law and increase spending to address the effects of the coronavirus crisis, despite the context of strongly falling tax revenues.

A second step was Congress's approval of the so-called 'War Budget' (Proposal of Constitutional Amendment No 10/2020, of 17 April 2020, later approved by Congress as Constitutional Amendment No 106, of 8 May 2020), exclusively for expenditures to combat the coronavirus-pandemic-related crisis and free from the constraints of the now-constitutional cap on federal government spending and the so-called 'golden rule', which prohibits public debt issues to cover current expenses.[3] The 'War Budget' amendment also authorized the Central Bank of Brazil (BCB) to purchase public and private securities on the secondary securities market (in the case of private securities only those classified at least as 'BB-' by international rating agencies). That permission would allow the BCB to engage in 'twist operations', that is, to exchange long-term government bonds for short-term bonds in order to flatten the interest curve, affecting in particular the longest maturities of the yield curve.

In order to support state and municipal governments, as only the federal government is able to issue public debt in Brazil, there was a need not only to mitigate the fall in local tax revenues, but also – since competence for healthcare is shared between the union, states and municipalities – to finance measures for coping with the public-

[3] The golden rule was created by the 1988 Constitution and establishes that the government can only issue debt to finance investments or roll over the payment of amortization of past debts. The logic of this rule is that the current generation could only issue debt to be paid by future generations if this was done to finance investments that also benefit future generations. The problems of this rule arise in its application, as there are several expenditures that are not investment, but still benefit future generations. For example, if there are insufficient tax resources, the government may have to cut spending on education, which are current expenses, but by definition benefit future generations. In the same sense, if real interest payments come in higher than expected, the government may have to cancel vaccination programmes to comply with the golden rule, since health costs are also current expenditures. Of special concern in Brazil is the existence of overlapping fiscal rules, which are sometimes contradictory to each other. For more on this, see Barbosa (2019).

health effects of COVID-19. Initially, Provisional Measure No 939, of 2 April 2020, allowed an extraordinary credit line of R$16 billion to be opened. On 2 May 2020, the Senate approved provision of R$60 billion in financial assistance from the union to states and municipalities and suspended approximately R$50 billion in sub-national entities' debts to the union, with R$10 billion to be used exclusively for health and social assistance and the other R$50 billion to combat the COVID-19 pandemic and mitigate its financial impacts.

Measures related to social assistance and the labour market

As already noted, the government was under strong social and political pressure to implement an emergency income transfer programme for informal and unemployed workers. Initially reluctant to implement such a programme, the federal government ended up proposing a R$200 voucher for three months, while Congress was pushing for approval of a minimum R$500. This pressure led to the enactment of Law 13.982, of 2 April 2020, under which an emergency programme would transfer monthly aid of R$600 (about half the official minimum wage and about US$107)) to around 65.9 million beneficiaries[4] (approximately one-third of the Brazilian population), initially for three months, then extended due to legislative pressure for two further months. The programme focused on the unemployed, the self-employed and informal workers, and those registered with other social programmes such as Bolsa Familia, in all cases only for families with an income up to three minimum wages. After these five instalments had been paid, debate arose as to whether or not to continue the programme, leading the federal government to institute Provisional Measure No 1.000, establishing four more monthly instalments of R$300 until December 2020.

As regards preserving formal employment, once again the measures taken by the federal government were clearly ambiguous. To begin with, President Bolsonaro proposed suspending employment contracts and reducing the working day without any payment of wages. Under strong political pressure from Congress, he subsequently proposed some income compensation for reduced working hours and wages.

[4] Just for comparison, cash transfer programmes reached 13.3 million people in Argentina and 4.7 million in Colombia. According to Blofield et al. (2021: 6), 'Auxilio Emergencial [Emergency Aid] is by far the largest social protection program to mitigate the social effects of COVID-19 in Latin America'.

Accordingly, Provisional Measure 936/20 (1 April 2020) instituted the Emergency Employment and Income Maintenance Programme, authorising employers to reduce wages and working hours temporarily or suspend employment contracts for up to 60 days, while assuring employees they would be retained during that period and receive emergency benefit payments from the Brazilian government. Working hours and wages could be reduced by 25 per cent, 50 per cent or 75 per cent, for a maximum of 90 days, by individual or collective agreement, or by any percentage (including 100 per cent), by collective agreement alone. For companies with revenues of less than R$4.8 million, the federal government paid the equivalent of 100 per cent of the unemployment insurance the employee would be entitled to receive. For companies with revenues of more than R$4.8 million, the employer paid 30 per cent of the employee's wages as compensatory aid and the federal government the equivalent of 70 per cent of the unemployment insurance due. The programme was extended three times in 2020 and ended in December. The estimated tax cost of this programme was R$51.2 billion, but as can be seen from Table 1, the final expense was much less, that is, R$33.5 billion.

Table 1 shows that total federal government expenditures in response to the COVID-19 crisis amounted R$415 billion in 2020. For the most part (R$230 billion or 55.4 per cent of the total), these took the form of emergency aid to protect the vulnerable, followed by financial assistance to states and municipalities (18.9 per cent) and for coping with the public-health emergency (10.6 per cent), in addition to emergency employment and income maintenance benefits (8.1 per cent). Credit guarantee fund quota payments by the National Treasury (FGI and FGO) responded for only 4.8 per cent of total funding, but – as will be shown below – were important in unlocking corporate credit for small and medium-sized businesses.

<Place Table 1 about here>

To give an idea of federal government spending in response to the coronavirus crisis, it is useful to compare between countries, even though each country has its own specificities. According to IMF figures, as percentages of GDP, additional spending and revenue forgone, as well as loans and guarantees, by the Brazilian government were both well above the average for emerging economies, at 8.3 per cent and 6.2 per cent, respectively, as compared with 3.6 per cent and 2.5 per cent for EMEs (cf. Figure 9).

<Place Figure 9 about here>

onetary and credit stimulus measures

As for monetary stimulus measures, the BCB reduced the Selic (policy) interest rate – which had been falling since September 2019 – from 4.25 per cent in February 2020 to a historic low of 2.0 per cent in August 2020, where it remained until March 2021 (cf. Figure 10). The immediate effect of easing monetary policy, for both banks and companies, was to reduce the costs of liabilities indexed to short-term interest rates. At the Monetary Policy Committee (COPOM) meeting in August 2020, 'forward guidance' was issued for the first time in Brazil; through this mechanism, the BCB publicly committed itself to keeping short-term interest rates constant as long as the inflation rate failed to converge with the target in the relevant period. By January 2021, the BCB was no longer using this mechanism.

<Place Figures 10 and 11 about here>

Measures implemented by the BCB to assure the stability of the financial system and the functioning of the credit system included: (i) injecting liquidity into the financial system to reverse the process of falling public and private security prices and to provide resources for banks to be able to offer credit, thus creating conditions in which liquidity risk was not a factor limiting banking sector operations; and (ii), through guarantee funds, ensuring the functioning of the credit market, particularly for small and medium-sized businesses (Vilella et al. 2020).

The measures taken in the second half of March and early April 2020 to increase financial system liquidity included a set of changes in regulatory requirements and in capital conservation coefficients, as well as temporary relaxation of provisioning rules for financial institutions. The Brazilian government also subsequently launched specific programmes of non-earmarked loans designed for small and medium-sized companies.

Monetary authorities' measures to stimulate and facilitate the fundraising by financial institutions included: (i) setting up two Special Temporary Liquidity Lines (LTELs), one backed by Guaranteed Financial Letter and the other by debentures, so as to restore liquidity conditions for financial institutions and avert problems in their financing of their active operations, as well as in investment fund portfolios; and (ii) increasing the scope of the Deposit Insurance Fund (FGC) in relation to the Time Deposit with Special Guarantee (DPGE), expanding the guarantee of FGC coverage from up to R$250<ts>000 to R$20 million per bank client, so as to enable financial institutions to raise more funds.

In the former case, the aim was to reduce banks' capital costs and, at the same time, to free up resources on their balance sheets in order to be able to expand lending operations. In this connection, the CMN reduced the reserve requirement on time deposits from 31 per cent to 17 per cent; reduced banks' capital requirement from 2.5 per cent to 1.25 per cent by March 2021; and expanded leverage limits on own resources and risk that banks can carry over on net worth. The Countercyclical Capital Buffer (ACCP) alone, an extra cushion of resources that banks must maintain, allowed the immediate release of R$637 billion. The CMN also exempted banks from deducting capital from tax assets due to over-hedging of overseas investments by financial institutions. According to the BCB, this would generate capital relief of R$46 billion, leveraging credit by approximately R$520 billion, which was in fact the case (Table 2).

From Table 2, it can be seen that the reduction in the reserve ratio requirement and enhanced regulation on the liquidity coverage ratio (LCR) had an immediate impact, injecting R$135 billion into the banking sector, while an additional reduction of reserve requirements injected R$70 billion. Loans backed by financial letter guaranteed by credit operations and the expanded DPGE had the potential, respectively, to release funds in the order of R$670 billion and R$200 billion, but in practice only generated R$41.3 billion and R$23.2 billion.

<Place Table 2 about here>

The Brazilian government's measures intended directly for the credit market involved injecting National Treasury funds to implement new lines of earmarked credit with a view to mitigating banks' credit risk. The main measures were: (i) the Emergency Employment Support Programme (PESE), operated by the BNDES and designed to finance payrolls of small and medium-sized businesses (with annual revenues of R$360<ts>000 to R$50 million). Loans were offered under special conditions (an interest rate of 3.75 per cent p.a. and a six-month grace period) for an initial period of two months, which was later extended to four months, providing the company retained its employees for the same period after the end of the loan period; the Treasury provided 85 per cent of the programme funding (R$34 billion), the rest coming from financial institutions; (ii) the National Programme in Support of Micro and Small Businesses (PRONAMPE), to support small and micro businesses with annual revenues of up to R$4.8 million. Here, the Treasury injected R$15.9 billion in May 2020 in the Operation Guarantee Fund (FGO); in August it made a further contribution of R$12 million. Operated by Banco do Brasil, this programme safeguarded against default by offering 100 per cent guarantees. The operation had to be limited to 85 per cent of the financial institution's portfolio and companies were required to maintain all workers' employment relationships for 60 days after receiving the credit; and (iii) the Emergency Credit Access Programme (PEAC), managed by the BNDES with up to R$20 billion of Treasury resources in an Investment Guarantee Fund (FGI). This credit programme, aimed at small and medium-sized companies with annual revenues between R$360<ts>000 and R$300 million, made no requirement to maintain levels of employment. The FGI covered the risk of default to up to 80 per cent of credit operations and up to 30 per cent of the total value of the credit offered by the financial institution.[5]

These programmes were designed to avert widespread insolvency in Brazilian companies, particularly micro and small businesses, resulting from partial or total loss of revenues. As shown in Figure 11, requests for receivership particularly affected micro and small enterprises, particularly in the service sector, which was the most strongly affected by the COVID-19 crisis, and peaked between April and August 2020. In contexts of extreme uncertainty, banks have difficulty calculating the risk of default by such firms, a problem that leads to strong credit rationing, which particularly impacts small businesses with few guarantees to offer (Martins et al. 2020). Although targeted credit programmes were thus essential for smaller firms to be able to finance their debts, actual implementation did not begin until July 2020.

SOME POLICY OUTCOMES

[5] In addition to the PEAC–FGI, the programme also featured a receivables guarantee modality, the PEAC–Maquininhas, using resources from the National Treasury. Intended for individual micro-entrepreneurs, micro and small businesses, that is, companies with gross revenues of up to R$4.8 million in 2019, it offered non-earmarked credits.

Effects on social indicators and economic performance

As shown above, the emergency aid (EA) programme for vulnerable individuals accounted for more than 50 per cent of the federal government's expenditures and contributed to rapid improvement in income distribution, offsetting low-income families' loss of income, particularly for those earning less than half of the minimum wage. Using data from the November 2020 PNAD/Covid19 survey, Table 3 divides the population equally into ten groups in ascending order of average effective income. The table then compares average effective income with and without EA, and calculates the percentage difference between them. When EA is included in the total income, the first and second deciles show average gains of 76 per cent and 32 per cent respectively, demonstrating the strong distributional impact of EA for low-income groups. In the other deciles, gain declines with increasing income. Gonçalves et al. (2021) calculated the Gini Index without EA (0.5429) and with EA (0.4972), and found a significant variation of 8.4 per cent in a very short period.

<Place Table 3 about here>

In addition to reducing social inequality, the EA programme also strongly relieved poverty and extreme poverty: the percentage of the population below the poverty line decreased from 23.7 per cent in May to 18.4 per cent in August 2020, while the percentage in extreme poverty was almost halved, from 4.18 per cent to 2.29 per cent[6] (cf. Table 4). In the same direction, Lustig et al. (2020) calculated that, in the absence of any mitigating measures, the incidence of poverty measured with the international of US$5.5 per day (in purchasing power parity) would have increased from around 25 per cent to around 28 per cent, and the number of poor could have risen from 53 million to 58.8 million.

<Place Table 4 about here>

[6] Menezes-Filho et al. (2021) found that the poverty rate declined from 12 per cent in 2019 to 8 per cent during the pandemic, while extreme poverty decreased from 3 per cent to about 1 per cent. Furthermore, the poverty gap between blacks and whites also closed significantly.

Sanches et al. (2021) estimated the multiplier effect of EA, that is, the factors that attenuated the depth of the recession in the first year of the pandemic.[7] Their simulations show that, with spending equivalent to 4.1 per cent of GDP in 2020, EA was responsible for mitigating contraction of the Brazilian economy by between 8.4 per cent and 14.8 per cent in 2020. In the absence of this benefit, household consumption would have decreased between 11 per cent and 14.7 per cent, instead of falling by 6 per cent.

The BCB's economic activity index shows that the public-health crisis and the social isolation imposed by the pandemic led to a sharp drop in economic activity between April and June 2020. The economy would recover partly from August on, when the pandemic slowed somewhat in Brazil and the counter-cyclical impact of emergency aid was felt (cf. Figure 12). In January 2021, there was a further fall in economic activity due to the second (strong) wave of the COVID-19 pandemic, which resulted in partial shutdowns in several Brazilian states and cities, and the adverse effects on income of rising inflation resulting from supply shocks (caused by rising commodity prices and currency devaluation). The IMF's projection was for Brazil's GDP to fall by 9.1 per cent in 2020, according to the World Economic Outlook of June, when in fact the real GDP growth rate was –5.3 per cent in 2020, a far better performance than the average for Latin America (–7.7 per cent) and for the region's major economies, according to preliminary Economic Commission for Latin America and the Caribbean (ECLAC) estimates (cf. Figure 13).

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Effects on credit supply and the financial market

Among the measures taken by the BCB to ensure the functioning of the credit market, liquidity measures were successful both in averting a liquidity crisis in the banking sector and in partly reversing the fall in public and private – particularly short and pre-fixed – bond prices (Martins et al. 2020). The funds released by reducing reserve requirements and capital conservation coefficients and the temporary relaxation of bank provisioning

[7] For this purpose, they used the fiscal multiplier methodology, which measures the impact of changes in fiscal policy (public expenditure or revenue) on GDP over a certain period of time.

rules migrated largely to BCB repo operations,[8] highly liquid applications that grew strongly from April to September 2020 (cf. Figure 14). This suggests that these measures averted a liquidity crisis, but had limited effects on bank credit supply, even though they did prevent a credit crunch.[9]

<Place Figures 14 and 15 about here>

Figure 7 showed that, after bank credit granting slowed in April and June 2020, credit supply recovered, more for individuals than for companies, the former favoured by loans renegotiated with longer maturities and lower rates. Corporate credit for small and medium-sized companies saw credit rationing from April to June 2020, showing that the measures initially implemented by the BCB to expand liquidity in the banking sector had little effect on stimulating the supply of credit in this segment. In fact, the PESE employment support programme stalled, having financed a total of R$7.9 billion, well below the R$34 billion the Treasury provided for the programme. PESE’s problems related mainly to the conditionalities (funds had to be credited directly to employees’ accounts) and the fact that banks had to provide 15 per cent of loan amounts. It was only by using guarantee funds (FGI and FGO) that credit flowed to small and medium-sized companies, and then with some delay. By 31 December 2020 PRONAMPE and PEAC-FGI had financed R$37.5 billion and R$92.4 billion, in 516<ts>790 and 35<ts>959 operations, respectively (BCB 2021b). As shown in Figure 8, credit for small and medium-sized companies grew strongly from July to September 2020.

The impact of the coronavirus crisis on the financial market in Brazil can be seen in Figure 15. Interest rates for terms of more than three years rose sharply in March 2020 and remained high until May, then fell until July following the reduction in the (one-day) Selic rate. From August onwards, there was a gradual increase on all maturities including one-year interest rates, as a result of agents’ intensifying perception of risk relating to uncertainty about the future of the Brazilian economy, how economic policy was being conducted and the perpetual political crisis, which eventually caused problems in public-debt management by the Treasury. Although in 2020 the BCB was authorised to purchase

[8] Repurchase agreements (or repo operations) are transactions involving the purchase (with a resale commitment) and/or sale (with a repurchase commitment) of public securities on the market, which allows the BCB to control liquidity in the economy for monetary policy purposes.
[9] A credit crunch is a situation in which the supply of bank credit is reduced suddenly and sharply, which may result in a banking crisis.

public and private securities on the secondary market to flatten the interest curve, it did not avail itself of this facility.

CONCLUSION: THE RETURN TO THE 'OLD NORMAL'

This article considered the Brazilian economy during the coronavirus pandemic and examined the economic policies implemented in 2020 in response to that crisis. It sought to show, unlike other analyses by heterodox economists, that – despite the lack of any strategy previously coordinated by the federal government to address the economic and social crisis – the counter-cyclical actions, especially those relating to emergency aid, had a strong counter-cyclical effect on the economy and also reduced poverty and social inequality in a significant way during the coronavirus crisis. Compared to other major Latin American economies, Brazil performed better in both economic and social indicators. The political economy of the Brazilian government's counter-cyclical actions during the coronavirus pandemic deserves future and careful studies.

The problems facing the Brazilian economy in 2021 relate to two issues: (i) economic recovery in 2021 has been compromised and performance will probably be well below those of most other economies (OECD 2021), largely because of President Bolsonaro's strategy of denial in response to the coronavirus pandemic, which led to an increase in the number of COVID-19-related cases and deaths as of January 2021 and to enormous delay in the vaccination programme; and (ii) the Brazilian government's return to a liberal agenda and orthodox economic policies, in the form of implementation of a new round of reforms – which included the approval by law (24 February 2021) of the Central Bank of Brazil independency[10] and of the Emergency Proposal of Constitutional Amendment, approved in 14 March 2021, which implemented new types of restrictions on public expenses for the Union and the sub-national entities, with respective prohibitions that must be activated in case certain limits are not complied with (mandatory primary expenditure greater than 95 per cent of total primary expenditure), such as the increase or readjustment of the wages of public servants and the hiring of personnel.

[10] The law established, among other issues, that the positions of directors and the President of the BCB (who continue to be appointed by the President of the Republic and must be approved by the Federal Senate) will have fixed terms. According to the official document, the directors and the President of the BCB will have four-year terms of office, with most of them, including that of the President, extending beyond the electoral term of the BCB would take office in the third year of the President's term.

As for the economic policies, the return to a spending cap, which has frozen public spending in real terms, prevented the government from implementing counter-cyclical fiscal policies, as we have already pointed out. Due to such a restriction, Carneiro/Moretti (2021) suggest the monetary financing of an expanded emergency aid, making use of the asset valuation of international reserves, a possible way to guarantee income to households in the context of a renewed outbreak of the pandemic, which could be done through an extraordinary change in the law that governs the relationship between the Treasury and the BCB in Brazil.

For 2021, different estimates have calculated the reduction in total workers' income (a concept that includes government income transfers) at between 3.8 per cent (Tendências Consultancy) and 7.0 per cent (IBRE/FGV). That decline is related to the high level of unemployment (14.2 per cent in January 2021), high inflation (5.2 per cent p.a. accumulated in February 2021) and the now-downsized emergency aid programme.[11] This income gap, together with high levels of household indebtedness,[12] results in a typical 'balance-sheet recession' situation.

In conclusion, the main problem for the Brazilian economy is that the federal government has no coherent economic recovery strategy for 2021 and beyond, especially after the pandemic is controlled. For example, there is no sign of a government programme to boost investments in infrastructure. In particular, President Bolsonaro's view that the coronavirus pandemic could not be combated by social isolation, because workers need to work to survive, has proven to be a huge mistake, not only because the pandemic is out of control in 2021, but also because it has compromised economic recovery, with adverse social effects on poverty and income distribution, as expected by most analysts.

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[11] On 11 March 2021 Congress approved the government's proposal of a new EA programme providing R$250 per family for four months beginning in April. The total amount approved for this benefit was R$44 billion (by comparison, the 2020 emergency aid programme totalled R$230 billion). It was not until 19 April 2021 that the federal government announced an agreement with Congress that included the allocation of R$10 billion to the Emergency Employment and Income Maintenance Programme (allowing agreements to reduce wages and working hours or suspend employment contracts to avoid lay-offs) and R$5 billion for two targeted credit programmes (for micro and small businesses), PRONAMPE and PEAC–Maquininhas.
[12] Total household debt to income accumulated in 12 months was 56.4 per cent in December 2020 (BCB 2021).

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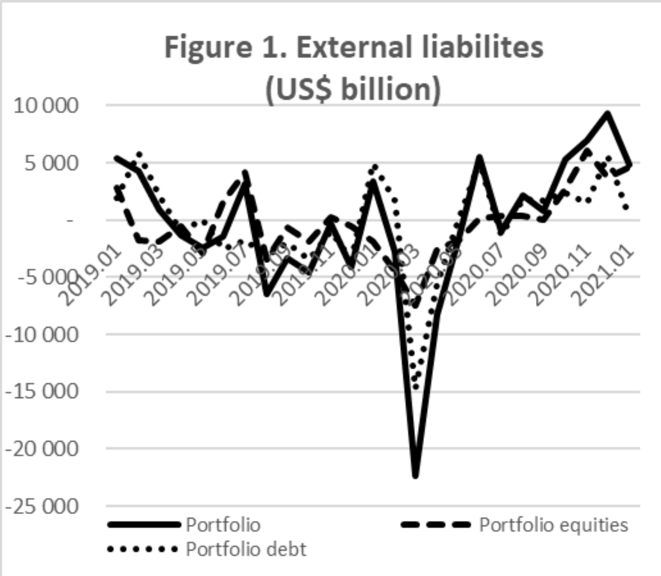
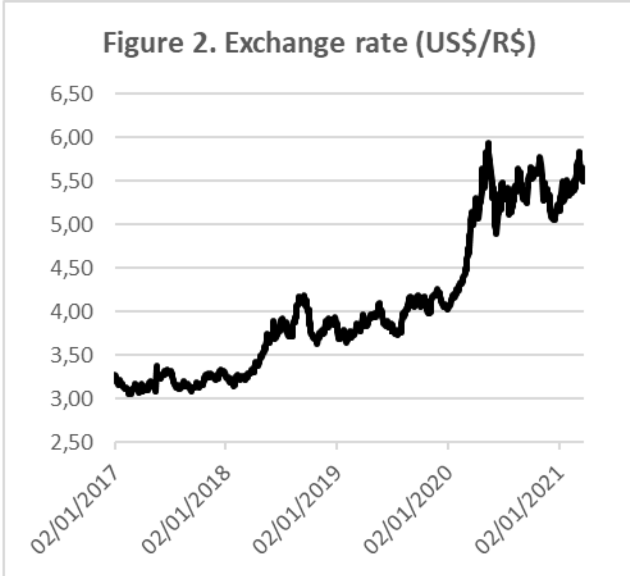
<Figures and Tables>





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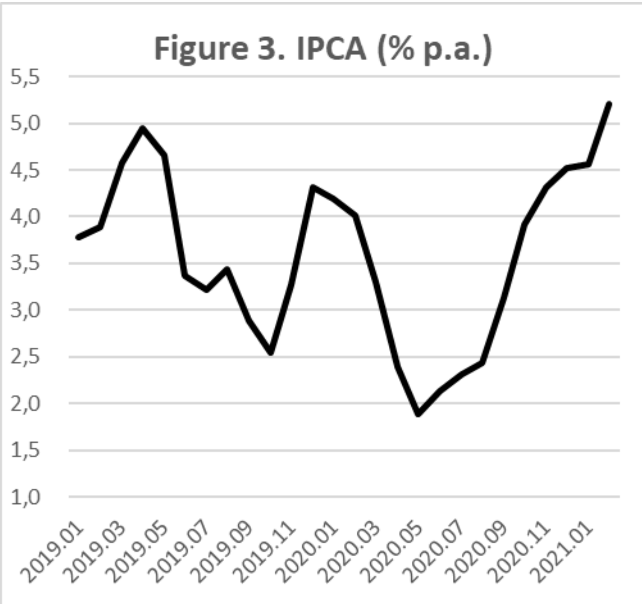

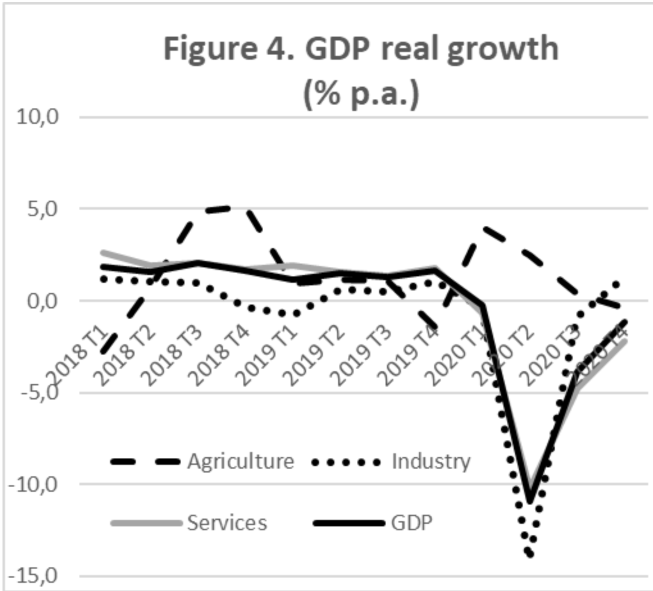

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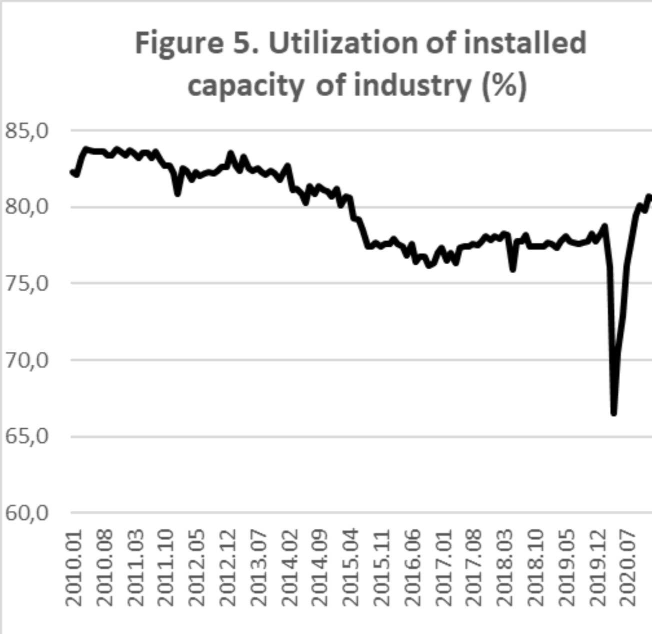

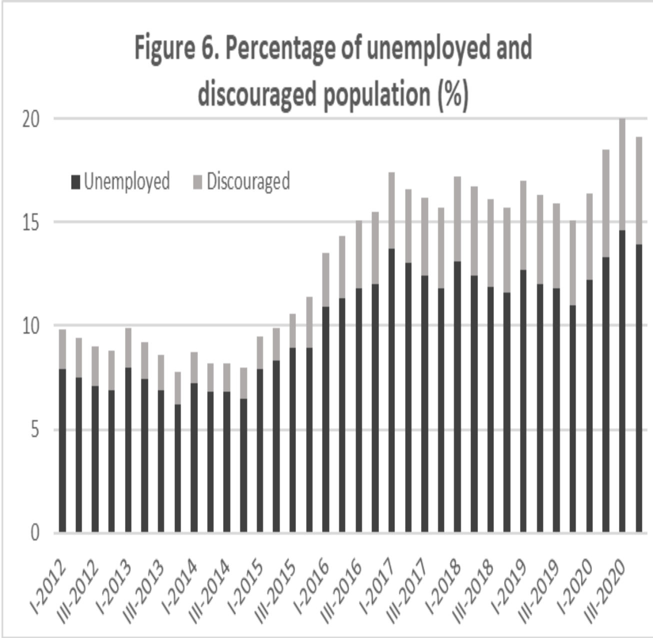

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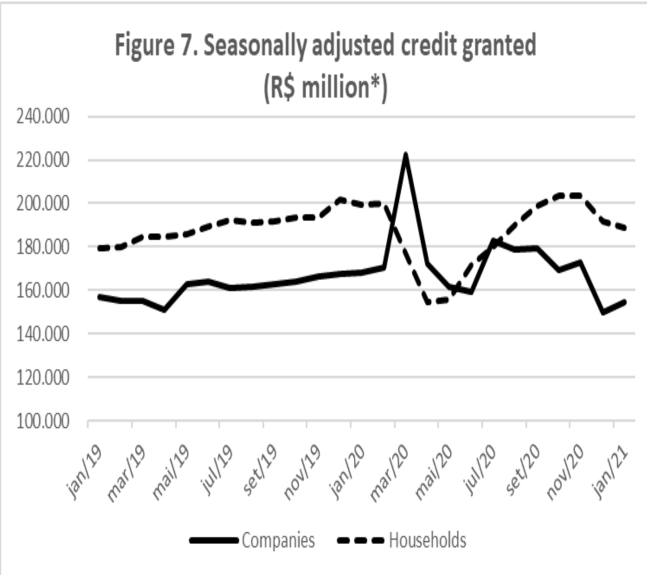
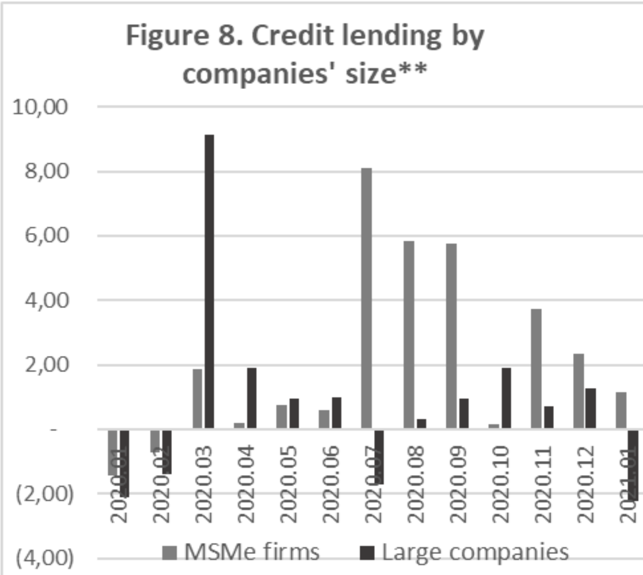


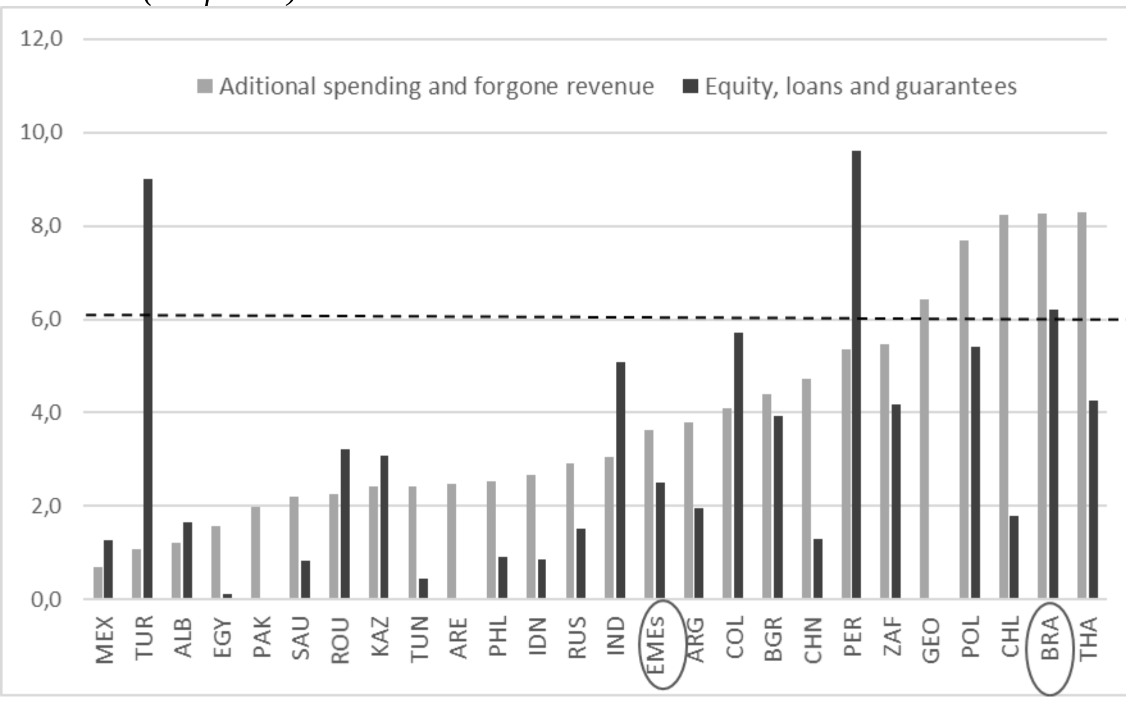


Notes: a. Data deflated by IPCA of February 2021.

b. Monthly variation of credit volume; MSMe: micro, small and medium-sized firms.

Source: Prepared by the author from BCB (2021).

Figure 9<em>Discretionary fiscal response to the COVID-19 crisis in selected economies (% of GDP)



Source: IMF (2020).

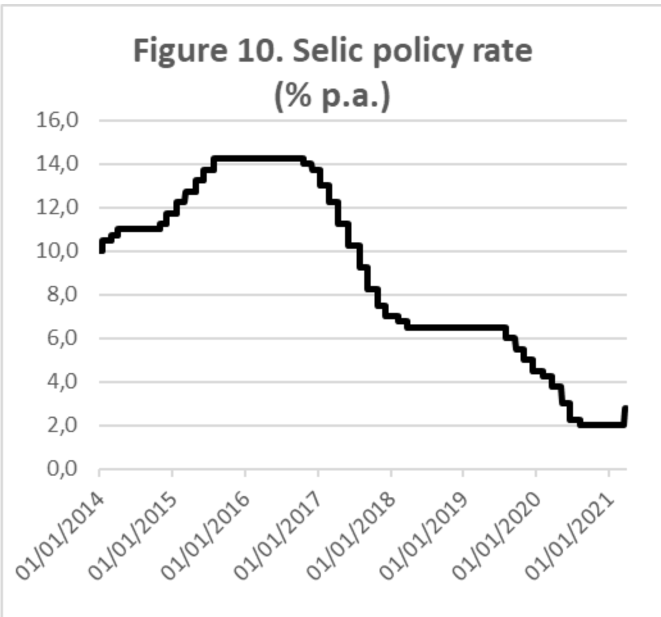


Figure 10. Selic policy rate (% p.a.)

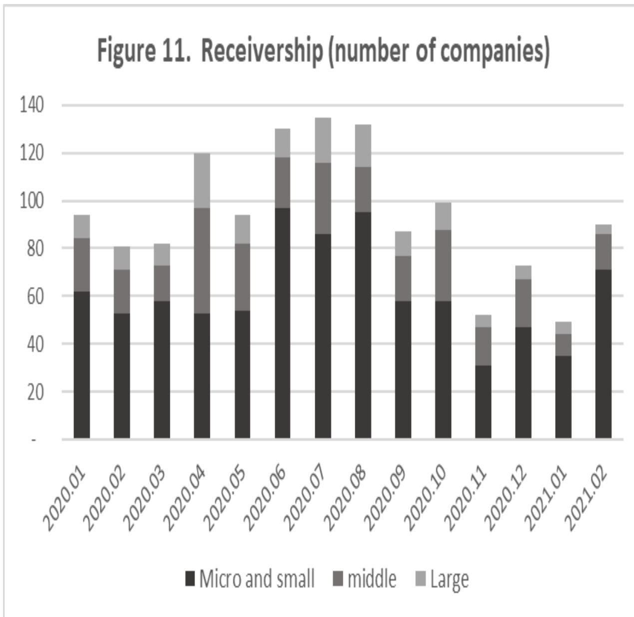
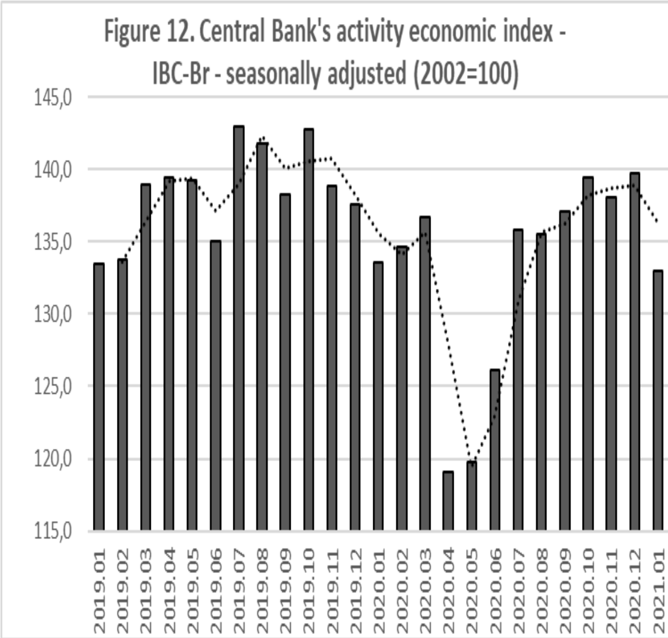
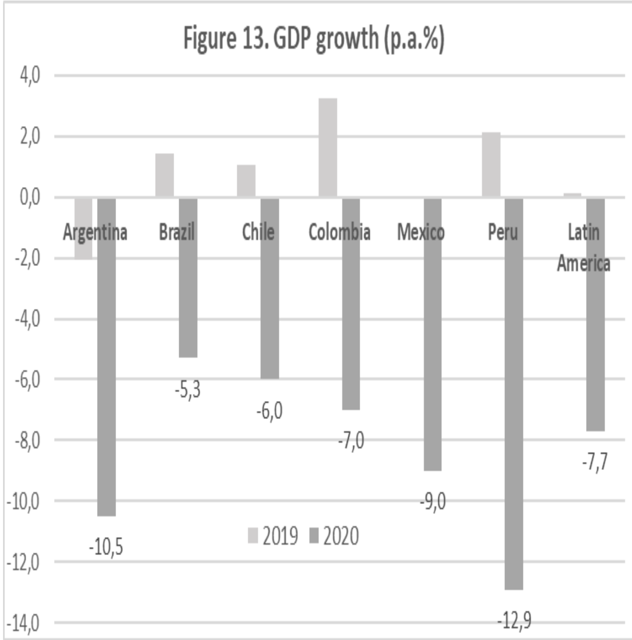


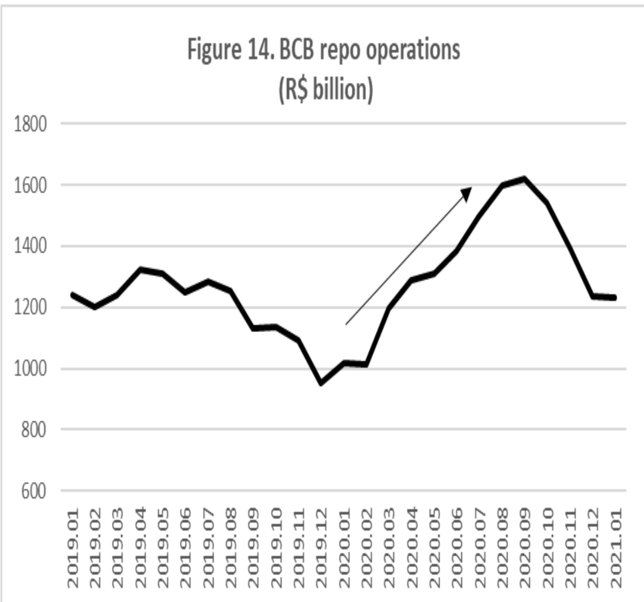
Figure 11. Receivership (number of companies)

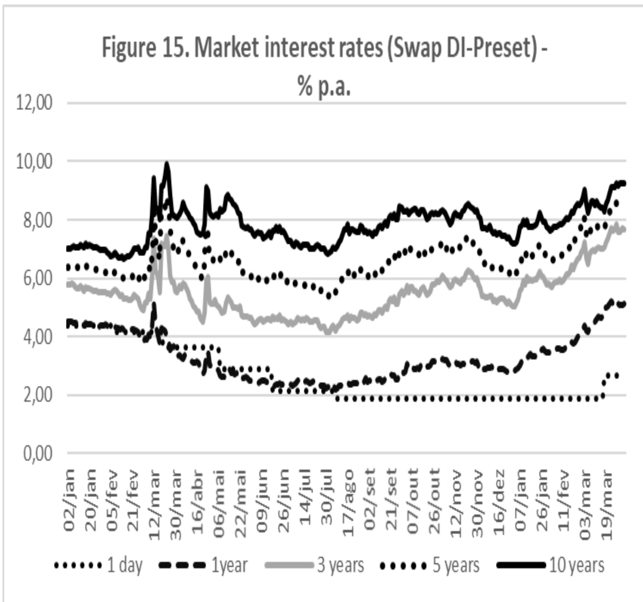
Source: BCB (2021) and Serasa (2021).





Source: BCB (2021) and ECLAC (2021).





Notes: OBS: The DI X PRESET rate corresponds to the yield curve constructed from the adjustment prices of the maturities of the one-day Interbank Deposit Average Rate Futures Contract traded on the B3 exchange.
Source: BCB (2021) and [B][3].

Table 1<em>Expenditures incurred due to the public-health emergency in 2020 (R$ billion)

Type of expenditure	Amount	Percentage
Emergency aid programme	229,906	55.4
Assistance to states and municipalities[a]	78,247	18.9
Coping with the public-health emergency	43,903	10.6
Emergency benefit to maintain employment and income	33,497	8.1
Payment of credit guarantee fund quotas	20,000	4.8
Emergency Employment Support Programme	6,807	1.6
Other expenditures	2,374	0.6
Total	*414,734*	*100.0*

Note: a. Includes Federative Programme to Address COVID-19 and compensation from the Participation Fund and support to the cultural sector.
Source: Ministério da Economia (2021).

Table 2<em>Main measures implemented by the BCB (R$ billion)

Measures implemented	Potential	Implemented
Liquidity support		
Reduction in reserve ratio requirement on time deposits and Enhanced Liquidity Coverage Regulation – LCR	135	135
Additional reduction of reserve requirements on term deposits	70	70
Loans backed by LF guaranteed by credit operations	670	41,3
New Term Deposit with Special Guarantees – DPGE	200	23,2
Loans backed by debentures	91	15,7
Release from savings deposits reserve requirement	56	25
Total	*1222*	*310*
Capital relief		
Over-hedging	520	520
Reduction of Conservation and Counter-cyclical Additional Principal Capital – ACCP	637	637
Reduction in capital requirement for SME credit	35	35
Total	*1192*	*1192*

Source: Campos Neto (2020).

Table 3<em>Average household income per capita of total effective income, by decile with and without emergency aid (EA) (R$)

Decile	Average effective income without EA	Average effective income with EA	Percentage variation
1	36.47	153.19	76.2
2	227.40	332.98	31.7
3	369.07	474.48	22.2
4	512.06	607.33	15.7
5	665.12	755.29	11.9
6	853.64	943.82	9.6
7	1,059.72	1,110.46	4.6
8	1,360.16	1,420.79	4.3
9	1,969.81	2,017.75	2.4
10	4,898.67	4,933.30	0.7

Source: Gonçalves et al. (2021: 7), with data from PNAD COVID-19.

Table 4<em>Percentage of the population below the poverty line

	Poverty[a]	Extreme poverty[b]
May 2020	23.72	4.18
June 2020	21.78	3.28
July 2020	19.58	2.54
August 2020	18.41	2.29

Notes: a. US$5.50 per day.

b. US$1.90 per day.

Source: Duque (2020), with data from PNAD COVID-19.