Independent Fiscal Institution

Fiscal Follow-Up Report

MARCH 22, 2021 • № 50

HIGHLIGHTS

- Consumption and investment contributed -5.2 p.p. to the change in GDP in 2020.
- A month of isolation would cause a deduction of 1.0 p.p. from GDP growth without compensatory measures.
- Unemployment rate would have reached 23.5% of the labor force if it included underemployed and discouraged persons.
- Local factors seem to be responsible for recent exchange rate depreciation.
- Current account deficit increased from USD 50.7 bn to USD 12.5 bn between 2019 and 2020.
- Central government had a primary deficit of BRL 744.1 bn in the 12 months up to January.
- Net revenue loss was BRL 154.1 bn in the comparison of 12 months between January 2020 and January 2021.
- Average rates of issuances of domestic debt bonds rose in January and February.
- Constitutional Amendment 109/21 authorizes up to BRL 44 bn in emergency aid over the spending ceiling.
- There is no provision for cutbacks in expenditures in EC 109/21 to offset the cost of emergency aid.
- Emergency aid, in 2021, will be paid from April, in four instalments, and the extension is not ruled out.
- Impact on the collection of measures contained in Provisional Presidential Decree no. 1,034/2021 is of BRL 4.0 bn.
- Risk of non-compliance with the ceiling becomes high before mandatory spending reaches the limit of 95%.
- The Executive Branch and the Labor Courts are the closest to the mandatory expenditure sub-ceiling.
- The Congress passed a law that allows the effective disbursement of conditioned expenditures prior to the publication of the Annual Budget Law.

FEDERAL SENATE
President of the Federal Senate
Senator Rodrigo Pacheco (DEM-MG)

INDEPENDENT FISCAL INSTITUTION
Executive Director
Felipe Scudeler Salto

Directors
Daniel Veloso Couri
Josué Alfredo Pellegrini

Analysts
Alessandro Ribeiro de Carvalho Casalecchi
Alexandre Augusto Seijas de Andrade
Luiza Muniz Navarro Mesquita
Pedro Henrique Oliveira de Souza
Rafael da Rocha Mendonça Bacciotti

Interns
Maria Vitória da Silva
Vinícius Quintanilha Nunes

TRANSLATION SERVICE - SETRIN/SGIDOC
Laerte Ferreira Morgado (translator)
Maria Iracema Lima Martin (editing translator)
Elder Loureiro de Barros Correia (translation coordinator)

REPORT LAYOUT
COMAP/SECOM and SEFPRO/SEGRAF

Summary

- Domestic absorption, composed of household consumption expenses, government consumption and investments, contributed -5.2 p.p. to the GDP change last year. Net exports (exports minus imports) exerted a positive influence, adding 1.1 percentage point to GDP. The negative impact on GDP resulting from the decline in consumption was mitigated by the effect of the Emergency Aid (BRL 293.1 bn between April and December last year).
- Reduction of the perception of fiscal risk, the effective and responsible management of the country in the pandemic, and the acceleration of a broad process of immunization of the population — reasons behind the uncertainty surrounding the domestic economic scenario — would help mitigate exchange rate pressures and the rate of interest increase needed to bring inflation expectations back to a level consistent with meeting the target.
- Deficits in the current account do not represent a concern when there are stable funding sources, such as the inflow of direct investments into the country. The figures from the Central Bank show that, in 2020, due to the effects of the pandemic on the economy, there was a significant decrease in the current account deficit in Brazil, from USD 50.7 bn to USD 12.5 bn, which was accompanied by a reduction, although relatively lower, of direct investments in the country, from USD 69.2 bn to USD 34.2 bn.
- The 12-month trajectory of public sector interest expenditure is favorable. As a proportion of GDP, the indicator showed a decrease over the last months, preventing even a more pronounced worsening of the nominal result. The start of a Selic[2] increase cycle in March is expected to worsen the dynamics of interest expenditure as the remuneration of federal government bonds is increased.
- The Emergency PEC was finally passed by the National Congress, as Constitutional Amendment No. 109, of March 15, 2021. The amendment contains several innovations, such as the one that changed the condition for activation of the Union's expense limitation triggers. In the case of subnational entities, a rule with the same provision has been created, but on an optional basis. The condition required for the adoption of measures will not be reached so soon. Among the other changes are the authorization for up to BRL 44 bn in emergency aid over the spending ceiling, a fiscal relaxation rule in case of a public calamity decree, a plan for gradual reduction of

Contact: ifi@senado.leg.br | +55 61 3303 2875
Social networks: /INSTITUICAOFISCALINDEPENDENTE @IFIBrasil @ifibrasil /instituiçãofiscalindependente
/company/instituição-fiscal-independente

[2] TN: the base internal rate of the Brazilian economy

tax expenditures and the inclusion of public debt sustainability as a criterion to guide fiscal policy.

- The 2021 Emergency Aid will be paid as of April. The programme, which had already been authorized by EC 109/2021, was established by Provisional Presidential Decree (MP, in the original acronym) No. 1,039 of March 18, 2021. Four monthly installments will be paid, and it should be noted that, according to the MP, the "period of four months (...) may be extended by act of the Federal Executive Branch". The manner of implementation of the aid will cause part of the expenditure provided for in the *Bolsa Família*[3] allocation to migrate to the aid allocation, generating a slack in the spending ceiling. However, judging by the 2020 TCU[4] recommendation, resources eventually saved with Bolsa Família should have a specific destination.

- Provisional Presidential Decree No. 1,034, dated March 1, 2021, provides for compensatory measures for the loss of revenue resulting from the reduction of federal taxes (PIS and Cofins) on diesel oil and cooking gas. According to impact calculations carried out by IFI, based on information received from the Federal Revenue of Brazil, the compensatory measures should bring a revenue gain of BRL 4.0 bn by the end of 2021.

- In 2020, mandatory spending corresponded to 92.6% of total expenditure and, in 2021, it should be equivalent to 93.4%. In the following years, the percentage should continue to grow, but at a slower pace. However, the risk of non-compliance with the ceiling becomes high before the mandatory spending reaches the 95% limit. In other words, for triggers to be activated, the amount of discretionary spending would have to be below the minimum level necessary for the operation of public services.

- In the breakdown by Government Branch or autonomous public body, the closest to the mandatory expenditure sub-ceiling are the Executive Branch and the Labor Courts. The forecast of mandatory spending in these two areas is 92.4% of total primary expenditure in 2021. To comply with the spending ceiling in 2020, the Labor Courts cut 36.3% of its discretionary expenditures. The high adjustment caused the ratio between mandatory expenditure and total expenditure to grow, making it more difficult to comply with the new EC 109 rule.

- Due to the imbalance in the so-called golden rule, 30% of the Union's primary expenditure planned for 2021 (BRL 453.7 bn) depends on the approval of the Annual Budget to be executed. With the delay in the processing of the PLOA[5], in some cases, the part of the expenditure that can be executed may be insufficient until April. The remuneration situation of the military members of the Armed Forces seems to be the most serious: 75% of the total expenditure allocated for the year are conditioned. PLN 1/2021[6], recently adopted by Congress, allows the execution of conditioned expenses prior to the publication of the LOA.

[3] TN: Family Grant program
[4] TN: Federal Court of Accounts
[5] TN: Annual Budget Bill
[6] TN: National Congress Bill

Independent Fiscal Institution

/INSTITUICAOFISCALINDEPENDENTE
@IFIBrasil
@ifibrasil
/company/instituição-fiscal-independente
/instituiçãofiscalindependente
github.com/ifibrasil

ifi@senado.leg.br / +55 (61) 3303-2875