

# Fiscal Follow-Up Report

JUL 13, 2022 • № 66

# HIGHLIGHTS

- Sectorial data from April and May enhance the perspective of GDP growth in the second quarter.
- IPCA estimate is revised from 8.6% to 7.4% in 2022 and from 4.2% to 4.8% in 2023
- Fiscal policy expansion and change in the ceiling rule in a disorganized manner compromise the policy's credibility.
- Information from Siga Brasil and Tesouro Gerencial indicates substantial improvement in the primary balance in June.
- In June, strong revenue growth occurred in income tax, grants, and dividends.

- Outstanding and issuances average cost of public securities continued to rise in May.
- The LDO, approved on July 12, now allows for an automatic change in the primary balance target and increases the transparency of parliamentary amendments.

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# **President of the Federal Senate**

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# **Covering letter**

The Fiscal Follow-Up Report (RAF) is the IFI's monthly conjuncture analysis and serves the purposes in art. 1 of Senate Resolution No. 42 of 2016. Periodically, usually in May and November, the RAF also presents a broad review of the fiscal scenario for ten years ahead. Starting in June of this year, we began updating the forecasts every month to capture the short-term dynamics of the economic variables in a timelier manner.

The first part of the RAF analyzes the macroeconomic context. We highlight that the performance of the activity remains positive. After a 1.0% advance in the first quarter compared to the previous quarter, the leading indicators suggest the GDP is still expanding in the second quarter. However, the economy should lose steam in the year's second half due to monetary tightening and less dynamic global growth. Our projection for the GDP remains at 1.4% for 2022 and drops slightly from 0.8% to 0.7% in 2023.

The labor market is on a recovery path. The unemployment rate went from 14.7% in May 2021 to 9.8% in May this year. The labor market participation rate reached 62.5%, better than a year ago, although still below the pre-pandemic period. Our expectation for the average unemployment rate has fallen from 11.0% to 10.7% in 2022.

Unemployment is falling, but so are incomes. Impacted by inflation, the average real income in the quarter ending in May fell by 7.9% compared to the same period in 2021. As a result, the overall wages – the product of the average earnings by the number of employed – advanced only 3.0% in real terms, in the same comparison, and remains below the pre-pandemic level.

Inflation is still facing an adverse picture. The IPCA-15 registered 0.69% in June and accumulated a twelve-month high of 12.04%. Nevertheless, our projection for the IPCA of 2022 moved from 8.6% to 7.4%, given the impact of the ICMS reduction promoted by Supplementary Law No. 194/2022.

The second part of the RAF deals with the fiscal environment. Since the approval of the so-called court-ordered debt PEC (Constitutional Amendments No. 113 and 114/2021), the measures adopted or being considered in Congress already represent a fiscal impact of about R\$ 166 billion in the Federal Budget for 2022. The most recent case is PEC No. 1/2022, which authorizes spending of up to R\$ 41.2 billion in the last months of this year.

To some extent, the performance of tax collection offsets fiscal expansion. From January to May, the real advance was 10.9% compared to the same period in 2021. Without considering non-recurring events, the increase remains high: 9.5%. The new macroeconomic forecasts, the realized revenue data until May, and the preliminary IFI figures for June raise our net primary revenue estimate from 17.9% to 18.4% in 2022.

The fiscal situation section also analyzes the Union's Budget for 2023, approved yesterday (12) by the National Congress. The primary deficit target was set at R\$ 65.9 billion, a result lower than the IFI's projection, which is a R\$ 1.4 billion surplus for next year. The difference in revenues is possibly due to the inflation and other macroeconomic parameters assumptions and positive surprises in the collection of 2022 that had not yet been considered in the PLDO scenario.

Daniel Veloso Couri IFI Executive Director Vilma da Conceição Pinto IFI Director



# Summary

- After having advanced 1.0% in the first quarter compared to the previous quarter, the highfrequency indicators from April and May suggest that the GDP should continue to expand in the second quarter. Positive data from industry, trade, and services and the labor market recovery sustain the activity's resilience in the first half of the year. During the second half of the year, on the other hand, the impact of the monetary tightening underway on aggregate demand and the less dynamic global growth should negatively impact the economy's performance. GDP is expected to advance 1.4% in 2022 and 0.7% in 2023. (Page 6)
- The projection for the IPCA in 2022 was revised from 8.6% to 7.4% with Supplementary Law 194/2022. The temporary reduction to zero federal taxes (Cide and PIS/Cofins) on gasoline and ethanol and the establishment of a permanent limit for ICMS rates on essential goods, including fuels, electricity, and telecommunications, should reduce current inflation. However, the 2023 estimate rose from 4.2% to 4.8% due to the recomposition of the federal tax rates in January next year. (Page 10)
- The recent measures in the fiscal area, which involve expansion of spending and revenue waivers, combined with the changes promoted in the spending ceiling, undermine the credibility of the main fiscal anchor of the country and may bring essential consequences in terms of future economic growth and equilibrium interest rates, which would penalize society as a whole. (Page 12)
- Preliminary data from the IFI show a solid primary balance for the central government in June. The surplus reached R\$ 53.9 billion in June and R\$ 72.4 billion in 12 months. Tax collection performance maintained robust growth in June, with income tax, CSLL, concessions/permissions, and dividends/participations as highlights. (Page 22)
- The central government's primary deficit target was set at R\$ 65.9 billion, but it may be higher, depending on the change in the spending ceiling. Considering the hypothesis that the spending ceiling should be higher than that estimated in the PLDO and that the budget will be allocated in such a way as to use all the space in the ceiling, the report approved by the CMO innovates by allowing the primary target to change according to the deviation between the spending ceiling estimated in the LDO and that which will be set in the 2023 Budget Law. (Page 27)

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# Table of contents

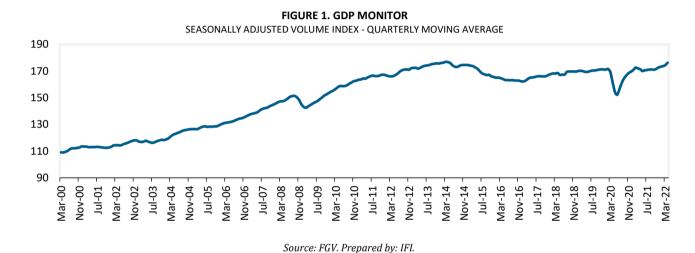
Covering letter	.3
Covering letterSummary	.4
Table of contents	.5
1. MACROECONOMIC CONTEXT	6
1.1 Economic activity	.6
1.2 Labor market	.7
1.3 Inflation and monetary policy	10
2. FISCAL SCENARIO	12
2.1 Fiscal risk1	12
2.2 Primary revenues and transfers1	15
2.3 Primary expenditures1	۱9
2.4 The central government and the consolidated public sector balance2	
2.5 Public sector indebtedness indicators2	24
2.6 The PLDO for 20232	
Fiscal tables3	34
IFI forecasts3	37



#### 1. MACROECONOMIC CONTEXT

#### 1.1 Economic activity

**GDP** should grow in the second quarter. After having advanced 1.0% in the first quarter of 2022, compared to the previous quarter on a seasonally adjusted basis, slightly above our expectation (0.6%), high-frequency indicators suggest that GDP should continue to expand in the second quarter. Positive data from the industrial, trade, and services sectors, in addition to the recovery underway in the labor market, sustain the picture of economic activity resilience in the year's first half. The Getulio Vargas Foundation's (FGV) GDP Monitor, an indicator that seeks to estimate the GDP monthly, registered a 0.3% expansion in April. Despite the lower growth rate compared to March (1.5%), there is a tendency for acceleration in the margin when the evolution of the quarterly moving average is observed (Figure 1).



**Expanded retail sales advanced 0.7% in April.** The sales volume (PMC – Monthly Retail Trade Survey) grew 0.7% between March and April in the expanded concept, including vehicles and construction materials. In the previous month, the index had increased by 0.1%. The survey's opening shows that April's performance was mainly sustained by the expansion in sales of furniture and appliances (up 2.3%) and clothing (1.7%). Considering the maintenance of the current level in May and June, the statistical carry-over of retail trade for the second quarter is estimated at 1.6%. Stimuli to disposable income, such as the anticipation of the 13th salary for retirees and pensioners of the INSS (National Institute of Social Security) and the release of FGTS (Severance Premium Reserve Fund) resources, tend to benefit consumers in the second quarter.

The service sector grew 0.2% in April. The volume of services rose 0.2% between March and April in the seasonally adjusted series, according to data from the IBGE's PMS (Monthly Services Survey). In the previous month, the index had grown 1.4%. The expansion in the volume of services in April largely followed the dynamics of services provided to households (up 1.9%). This component, hit during the pandemic, has benefited from the normalization of urban mobility. With this result, and considering the maintenance of the current level in May and June, the carry-over for the second quarter is estimated at 1.1%.

**Industrial production rose 0.3% in May.** According to the IBGE's PIM (Monthly Industrial Survey), general industry production rose 0.3% from April to May (seasonally adjusted series). In the previous month, the index had grown 0.2%. The month's result reflected the transformation industry's performance (up 0.8%), while the extractive industry

JULY 13.2022



shrank 5.6%. The industrial sector's advance in May was accompanied by three major economic categories, especially the capital goods sector (5.7%). Despite the positive dynamics of the capital goods sector, driven by the rise in commodity prices, industrial production continues at a lower level than before the pandemic, limited by the persistence of bottlenecks in global production chains. With the positive result for May, considering the maintenance of the current level of the general industry in June, the carry-over for the second quarter is estimated at 1.0%.

The inflow of resources (INSS and FGTS) reinforces the scenario of increased activity in the second quarter. IBGE's sectorial surveys point to GDP expansion in the second quarter, given the magnitude of the carry-over in trade, services, and industry (representative sectors in the GDP composition on the supply side). The expectation for GDP growth in the period is reinforced by the extraordinary withdrawal of up to R\$ 1,000 from the FGTS, even though a recent FGV<sup>2</sup> survey based on the Consumer Survey indicates a limited impact on consumption. In the survey, less than a quarter of those interviewed intend to consume goods and services with the funds, given the current high inflation and indebtedness levels.

The economy should lose steam in the second half of the year. Over the second half of the year, on the other hand, the economic activity is expected to slow down. The impact of the monetary tightening underway by the Central Bank on aggregate demand and the less dynamic global growth should harm the performance of the economy over the coming quarters. Faced with the advance of inflation – influenced by the disarray in global production chains and by the rise in commodity prices, intensified by the war – central banks are withdrawing the monetary stimulus adopted during the fight against the pandemic. The contractionary stance of monetary policy has affected the prospects for economic growth in the major economies.

Uncertainties surrounding the GDP estimates (1.4% in 2022 and 0.7% in 2023) remain high. This year's GDP growth remains at 1.4%, but we have slightly adjusted the 2023 estimate (from 0.8% to 0.7%) due to the base interest rate revision (13.75% in 2022 and 10.25% in 2023). The uncertainties surrounding the projections, however, remain high. The current measures of tax cuts (Supplementary Law No. 194/2022) and the expansion of social transfers (PEC No. 1/2022 – approved by the Federal Senate and under consideration by the Chamber of Deputies) like the increase in the benefit of the Auxílio Brasil program, may produce some positive effect on aggregate demand through the expansion of the income available for consumption. On the other hand, the increase in the perception of the risk associated with the sustainability of public accounts, which has already materialized in the shifting of the future interest curve and the increase in the country risk premium, tends to produce adverse lagged effects on economic activity. In practical terms, expectations of rising interest rates and inflation, embedded in the term structure, indicate an increase in the cost of loans and financing, discouraging consumption and investment.

#### 1.2 Labor market

**Labor market indicators maintain a recovery trajectory.** Data released by the IBGE in the Continuous National Household Sample Survey (PNAD Continuous) show a drop in the unemployment rate, an increase in the employed population, and a decrease in the level of discouragement. This positive dynamic reinforces the prospect of GDP growth in the second quarter of this year.

<sup>&</sup>lt;sup>2</sup> Available at: https://blogdoibre.fgv.br/posts/para-onde-vao-saques-do-fgts-e-antecipacao-do-13o-de-aposentados-e-pensionistas

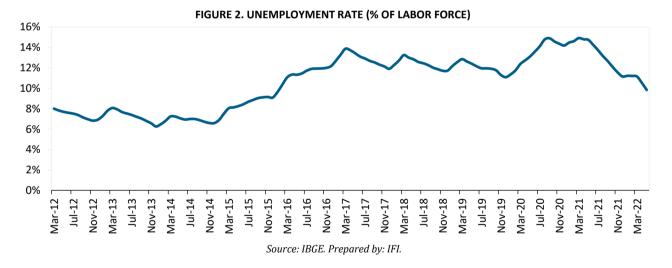


**TABLE 1. LABOR MARKET INDICATORS** 

Item	V	alues (millic	Quarter x last quarter			
	May/20	May/21	May/22	May/20	May/21	May/22
A – Working-age population	169.7	171.4	172.9	1.0%	1.0%	0.9%
A.1 – People outside the labor force	69.9	68.0	64.8	14.7%	-2.8%	-4.7%
A.2 – Labor force population	99.8	103.4	108.1	-6.8%	3.6%	4.6%
A.2.1 – Unemployment	13.1	15.2	10.6	-1.4%	16.3%	-30.2%
A.2.2 – Employment	86.7	88.2	97.5	-7.5%	1.7%	10.6%
Informal employment	32.2	34.8	39.1	-15.4%	7.9%	12.5%
Formal employment	54.5	53.4	58.4	-2.1%	-2.0%	9.4%
Unemployment rate (A.2.1/A.2)	13.1%	14.7%	9.8%	0.7 p.p.	1.6 p.p.	-4.9 p.p.
Employment rate (A.2.2/A)	51.1%	51.4%	56.4%	-4.7 p.p.	0.3 p.p.	4.9 p.p.
Participation rate (A.2/A)	58.8%	60.3%	62.5%	-4.9 p.p.	1.5 p.p.	2.2 p.p.

Source: IBGE. Prepared by: IFI.

The unemployment rate reached 9.8% of the labor force in the quarter ended in May, 4.9 percentage points (p.p.) below the rate recorded in the same period a year earlier (14.7%). The reduction in the unemployment rate is the result of the recovery in the employed population, which reached 97.5 million people (a 10.6% expansion compared with the same period in 2021), surpassing the growth in the labor force (up 4.6% in the same comparison), comprised of people who are employed or seeking employment.

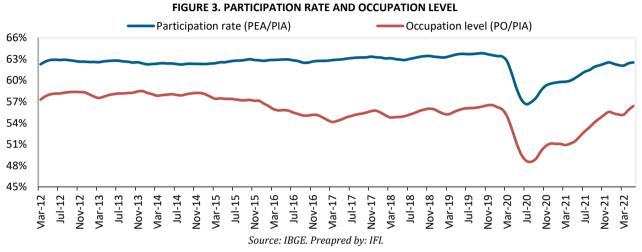


**Demand for labor: the increase in employment occurs in both the formal and informal markets.** The population employed in the informal segments of the economy (39.1 million people) grew 12.8% compared to the same period last year, while formal employment (58.4 million) rose 9.4%. The expansion of the employed population is positively impacting the occupation level (the ratio between the employed population and the working-age population). In May, the indicator rose to 56.4%, 4.9 p.p. above the same period in 2021 and 0.5 p.p. above February 2020 (before the pandemic).



confirming the recovery in labor market conditions.

**Labor supply: participation rate advances but remains below the pre-pandemic period.** Labor force growth drives the participation rate, which measures the inflow and outflow of working-age people into the labor market. The indicator, expressed as the ratio between the number of people in the labor force and the number of people of working age, reached 62.5% in the quarter ended in May (2.2 p.p. above the level of the same period a year earlier). The participation rate is evolving positively, indicating the return of people to the labor market, although it remains at a lower level than the months before the pandemic (63.4%).



The decrease in discouragement reinforces the picture of greater dynamism in the labor market. In the quarter ended in May, the number of people who are not willing to work – individuals who do not look for a job but would like one and are available for work – reached 4.3 million people, 22.6% lower than in the same period in 2021 (5.6 million),

**Expectations for the average unemployment rate are reduced from 11.0% to 10.7% in 2022.** Even with the increase in the labor force and the participation rate, reflecting the return of people who had not been previously active in the labor market, possibly due to the cooling of the pandemic and the recovery in activity, the IFI's projection for the average unemployment rate in 2022 was adjusted downwards, from 11.0% to 10.7%, due to the intense pace of expansion in hiring.

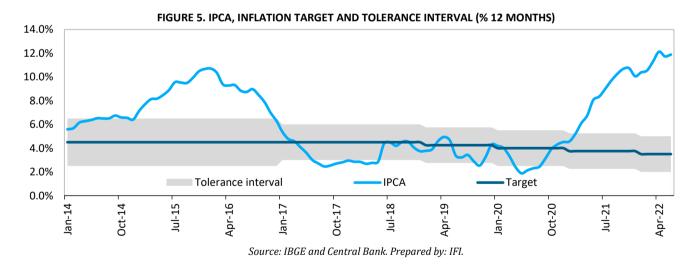
**Improvement in job creation contributes to the expansion of the overall labor earnings.** Also, according to data from PNAD Continuous, the average real income in the quarter ended in May dropped 7.9% compared to the same period last year, negatively impacted by high inflation. The overall labor earnings, on the other hand, an indicator that combines the evolution of income and the employed population, advanced 3.0% in real terms in the same comparison. Figure 4 shows an overall labor earnings recovery trajectory, although it remains far from the pre-pandemic level.





#### 1.3 Inflation and monetary policy

**Consumer inflation accelerated in June.** The IPCA in June raised by 0.67%, 0.2 p.p. above May (0.47%). In the last 12 months, the IPCA accumulated 11.89%, above the 11.73% registered in the immediately previous 12 months. Consumer inflation has been above 10% since September 2021 and exceeds the upper limit of the target defined by Copom (Monetary Policy Committee) of the Central Bank for 2022 (a reference of 3.5% with a tolerance interval of 1.5 p.p. above and below).



**The average of the cores accelerates, reaching 10.50% in June.** The diffusion index, which measures the proportion of goods and services with price increases compared to the total items surveyed by IBGE, slowed down from 72.4% to 66.6%, remaining at a high level. The average of the cores monitored by the Central Bank – measures that seek to remove the influence of more volatile items from total inflation – advanced from 10.11% to 10.50% in the accumulated figure for 12 months, revealing a still persistent inflation scenario.



TABLE 2. IPCA: MONTH % CHANGE AND 12-MONTH

Consumer inflation		onth % chan	ge	12-month			
Consumer initiation	Apr/22	May/22	Jun/22	Apr/22	May/22	Jun/22	
IPCA	1.06%	0.47%	0.67%	12.13%	11.73%	11.89%	
Administered prices	0.55%	-0.51%	0.48%	15.05%	12.09%	11.73%	
Market prices	1.25%	0.83%	0.74%	11.10%	11.60%	11.94%	
Food-at-home	2.59%	0.43%	0.63%	16.11%	16.35%	16.69%	
Services	0.66%	0.85%	0.90%	6.93%	8.00%	8.73%	
Industrial goods	1.22%	1.06%	0.58%	14.22%	13.97%	13.73%	
Average of inflation cores	0.95%	0.93%	0.89%	9.69%	10.11%	10.50%	

Source: IBGE and Central Bank. Prepared by: IFI.

June's IPCA acceleration reflected the administered prices, services, and food-at-home. Between May and June, the change in administered prices (or monitored prices), which account for approximately 25% of the total IPCA, went from -0.51% to 0.48% (accumulated variation of 11.73% over twelve months), impacted in large part by the hike in health plan prices resulting from the 15.50% readjustment authorized by the ANS (National Agency of Supplementary Health). On the other hand, free prices rose 0.74%, slowing down compared to April (0.83%). In 12 months, the variation in these prices rose from 11.60% to 11.94%. The existing opening for free prices shows that the most significant pressure in June came from services (0.90% variation in the month and 8.73% in 12 months). Food-at-home prices also advanced (0.63% and 16.69%), while industrial prices slowed down (0.58% and 13.73%).

Despite the still adverse scenario, the projection for the IPCA in 2022 was revised from 8.6% to 7.4%, considering the impact of the measures contained in Supplementary Law No. 194/2022. Among the initiatives contained in the law, aiming to mitigate the effect of the increase in fuel prices, the temporary reduction to zero of federal taxes (Cide and PIS/Cofins) on gasoline and ethanol and the establishment of a permanent limit for the ICMS rates on essential goods (at the level of 17%-18%, depending on the federative units), including fuel, electricity, and telecommunications, should reduce current inflation. The IPCA variation expected this year was revised from 8.6% to 7.4%, while the 2023 estimate rose from 4.2% to 4.8% due to the federal tax rates readjustment in January next year.

The Selic rate is expected to close at 13.75%, remaining at a high level in 2023. Recent data show resilient economic activity and high and still persistent inflation. In June, Copom decided to raise the base interest rate by 0.5 p.p. to 13.25%. Since the minutes published after the meeting indicate that there will be another increase of equal or lesser magnitude, we have revised the Selic rate estimate from 13.25% to 13.75%. The prospect of a still challenging inflationary picture and the displacement of inflationary pressures for next year resulting from the tax measures should affect the space for reducing the cuts. Our scenario envisions that the Selic at the end of 2023 will reach 10.25% (revised from 9.5%).

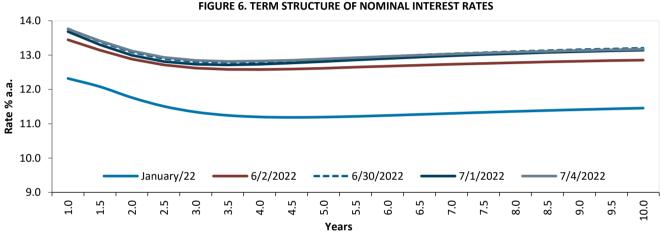
Copom's reference scenario inflation projections do not yet contemplate the effects of tax measures to mitigate the rise in fuel prices. In discussing the scenario update that justified its decision, Copom mentioned the deterioration of the external environment, marked by a sharp deceleration in the world growth outlook, the domestic economic activity indicators performance above expectations, and consumer inflation, as measured by the IPCA, higher and more persistent than anticipated. In the reference scenario, Copom's inflation projections are 8.8% for 2022 and 4.0% for 2023. These projections, in any case, do not incorporate the effects of the recently approved tax measures. Still, it was evaluated that they should significantly reduce inflation in the current year and raise, to a lesser extent, that of the following year.

Copom's balance of risks for future inflation includes concerns regarding the sustainability of the fiscal trajectory. In its analysis of the balance of risks for future inflation, Copom mentions the more remarkable persistence



of global inflationary pressures and uncertainty regarding the future of the country's fiscal framework and fiscal policies that imply the sustainability of aggregate demand among the upside factors. Among the downside risks, it emphasizes a possible reversal of the increase in international commodity prices in local currency and a sharper-than-projected slowdown in economic activity.

**Yield curve shifts after approval of PEC 1 in the Senate.** Figure 6 shows the term structure of interest rates calculated by Anbima (Brazilian Financial and Capital Markets Association) based on secondary trading in government bonds, the remuneration in nominal terms for a bond with one year at the beginning of July, one day after the approval of PEC No. 1/2022 in the Federal Senate, is higher in comparison to what was observed a month ago. At the same time, the longer part of the yield curve has shifted upward, reflecting, among other factors, the market's increased perception of fiscal risk.



#### Source: Anbima. Prepared by: IFI.

#### 2. FISCAL SCENARIO

#### 2.1 Fiscal risk

Recent measures affect the public accounts and increase the perception of risk in the fiscal policy conduction.

This section aims to discuss the perception of fiscal risk in the country resulting from the actions taken by the Executive and Legislative Branches as of the end of 2021 to increase expenditures and reduce primary federal revenues. These measures have led to revisions in economists' estimates for the main fiscal variables and may signal a deterioration in the fiscal picture of the federal entities in the medium and long term. Table 3 shows the list of the actions mentioned.

Constitutional Amendments 113 and 114 altered the Federal Government's spending ceiling to allow an increase in expenses. The main innovations brought by Constitutional Amendments (EC) No. 113 and 114 were the change in the rule for calculating the expenditures subject to the ceiling, moving the IPCA calculation window, an indicator used to limit the growth of primary expenses, from July to June to January to December; and the imposition of a limit for court-ordered payments of debt by the Federal Government. According to the IFI's calculations presented in RAF No. 60<sup>3</sup>, January 2022, the fiscal space opened in the fiscal year 2022 with the two amendments was R\$ 113.1

<sup>&</sup>lt;sup>3</sup> Available at: https://www12.senado.leg.br/ifi/publicacoes-1/relatorio/2022/janeiro.



billion. This space was filled with more expenses, such as Auxílio Brasil and the amendments of the general rapporteur, and left little room for new increases.

TABLE 3. MEASURES ADOPTED BY THE EXECUTIVE AND LEGISLATIVE BRANCHES WITH IMPACT ON THE UNION'S PRIMARY BALANCE\*

Legal instrument	Date	Summary	Impact on the 2022 primary balance (R\$ billion)
Constitutional Amendments No. 113 and 114 of 2021	December 8 and December 16, 2021	Open space in the ceiling due to the change in the indexer plus court-ordered debts expenses paid outside the ceiling (Fundef and agreements)	-81.70
Supplementary Law No. 192	March 11, 2022	Reduces to zero the PIS/COFINS rates on gas, diesel, and biodiesel until 12/31/2022	-17.60
Supplementary Law No. 193	March 17, 2022	Simples Nacional Refis	-1.20
Provisional Measure No. 1,115	April 28, 2022	Increase of CSLL for banks until 12/31/2022	0.40
Decree No. 11,055	April 28, 2022	Permanent reduction of IPI rates by 35%	-8.50
Import Tax Reduction	May 11, 2022	Import Tax reduction on some items	-0.70
Supplementary Law No. 194	June 23, 2022	Reduces to zero the rates of Cide and PIS/Cofins on gasoline and ethanol	-15.43
Constitutional Amendment Bill No. 1 of 202	Approved on June 30, 2022, by the Federal Senate and submitted to the Chamber of Deputies	State of emergency PEC. Creates some aid and extends others until 12/31/2022	-41.25
Total			-165.98

<sup>\*</sup> The R\$ 23.9 billion spent with the agreement between the Union and the Municipality of São Paulo about the ownership of Campo de Marte Airport (PLN No. 4, of 2022) was not considered because the expense resulted from a judicial decision.

Source: RFB and IFI.

The impact of R\$ 81.7 billion resulting from the enactment of ECs 113 and 114 can be divided as follows: (i) R\$ 69.6 billion refers to the recalculation of the ceiling with the change of the IPCA calculation window (from July to June to January to December); (ii) R\$ 4.2 billion, an amount authorized in the 2022 Budget Law (LOA), represent court-ordered payments of debt outside the ceiling, referring to agreements with the Union; and (iii) R\$ 7.9 billion configure court-ordered payments of debt under Fundef, to be paid outside the ceiling.

In other words, the impact of the two constitutional amendments on the central government's primary balance represents a difference between the new situation of primary expenses executed under a higher ceiling plus expenses included outside it and the expenses managed under the ceiling calculated by the previous methodology.

Federal tax cuts on diesel and gas will reduce federal tax revenues in 2022 by R\$ 17.6 billion. The Supplementary Law (LC) No. 192, of March 11, 2022, zeroed the rates of PIS/Cofins and Cide levied on cooking gas,

JULY 13.2022



diesel, and biodiesel until the end of 2022. In RAF No. 62<sup>4</sup> of March 2022, the IFI estimated that the impact on the primary revenue of the central government would be R\$ 17.6 billion.

The Simples Program of Fiscal Recovery (Refis) is expected to produce a revenue loss of R\$ 1.2 billion. On March 17, LC No. 193 was sanctioned, instituting the Program for Rescheduling the Payment of Debts within the scope of the Simples Nacional (Relp), also known as the Simples Program of Fiscal Recovery (Refis). According to the Federal Revenue Office, the estimated impact of the measure is R\$ 1.2 billion. To compensate for this loss of revenue, even if only partially, the government raised the CSLL rates for legal entities in the financial system until December 31, 2022, through Provisional Measure (MP) 1,115, of April 28, 2022. The IFI estimates a positive impact of R\$ 400 million<sup>5</sup> from this increase in the CSLL of banks on federal tax revenues.

The 35% reduction in the IPI tax will represent a revenue waiver of about R\$ 7.6 billion for the Federal Government in 2022. Decree No. 11,055, of April 28, 2022, increased from 25% to 35% the linear reduction of the IPI rates previously instituted by Decree No. 10,979, of February 25, 2022. In RAF No. 64, of May 2022, the IFI estimated R\$ 7.6 billion and R\$ 10.2 billion, reducing the Union's collection in 2022 and 2023, respectively. The decree did not stipulate a deadline for the end of the measure.

According to the government, the import tax reduction will impact R\$ 700 million. On May 11, the government promoted an import tax reduction on some items. As presented in RAF No. 64, the IFI used the estimate of the government's waiver due to the difficulty of calculating the impact on tax collection. According to the government, the measure would bring a loss of R\$ 700 million in 2022.

The reduction of PIS/Cofins and Cide in gasoline and ethanol will generate a loss of R\$ 15.4 billion in the second semester. LC No. 194, of June 23, 2022, among other innovations, zeroed PIS/Cofins and Cide rates levied on gasoline and ethanol until December 31, 2022. The IFI estimates a R\$ 15.4 billion tax waiver with this measure between July and December.

**PEC No. 1/2022 authorizes spending of up to R\$ 41.2 billion in 2022.** Finally, the Constitutional Amendment Bill (PEC) No. 1 of 2022, joined to PEC No. 16 of 2022, was approved on June 30 by the Federal Senate and sent to the Chamber of Deputies for analysis. The Proposal creates an extraordinary monthly benefit of R\$ 200.00 for the Brazil Aid, eliminating the program's queue and establishing financial aid for truckers and cab drivers, among other measures. In all, spending authorizations total R\$ 41.25 billion in 2022 alone, which would not be subject to the spending ceiling and other fiscal rules. IFI's Commentary No. 16, of July 6, analyzed the Proposal<sup>6</sup>.

Changes in the spending ceiling rule increase uncertainties regarding the conduction of fiscal policy. The demand for more spending, especially in the current economic and social context, is legitimate. However, changes in the spending cap rule without an in-depth discussion increase uncertainty regarding the long-term sustainability of public debt due to the possibility of an uncontrolled primary expenditure in the coming years, which would affect the expected trajectory for the primary balance. It is worth saying that, currently, the ceiling is the country's main fiscal anchor.

<sup>&</sup>lt;sup>4</sup> Available at: <a href="https://www12.senado.leg.br/ifi/publicacoes-1/relatorio/2022/marco">https://www12.senado.leg.br/ifi/publicacoes-1/relatorio/2022/marco</a>.

<sup>&</sup>lt;sup>5</sup> As presented in RAF No. 64, May 2022. Available at: https://www12.senado.leg.br/ifi/publicacoes-1/relatorio/2022/maio.

 $<sup>{}^6</sup> Available \quad at: \quad \underline{https://www12.senado.leg.br/ifi/publicacoes-1/comentarios-da-ifi/2022/julho/ci-comentario-da-ifi-no-16-a-pec-no-1-2022-e-o-aumento-do-risco-fiscal.}$ 



Previous experience suggests difficulty cutting budget expenditures, especially in an environment of uncertainty regarding the economy's behavior. Concerning the expenses created, such as the increase in the Brazil Aid and the aid to cab and truck drivers, previous experience indicates that it will be challenging to cut payments after including them in the budget, even more so in a context of a high probability of cooling economic activity in the coming months due to the monetary tightening, now uncompleted, conducted by the Central Bank.

**Increased risk perception will imply higher equilibrium interest rates.** It is crucial to weigh the consequences of an eventual increase in the country's fiscal risk perception. The first consequence would be a rise in the economy's neutral interest rate, an unobservable variable constructed by economists to reflect the real interest rate that would guarantee the economy's growth at the potential level (zero output gap) with stable inflation and within the target.

The Central Bank now considers the neutral interest rate for the Brazilian economy at 4.0% in the last Inflation Report. As an illustration, the neutral interest rate used by the Central Bank in future inflation scenarios is now considered a level of 4.0% in the June Quarterly Inflation Report (RTI), higher than the 3.5% rate used in the same publication in March 2022. The displacement of the real interest rate to a higher level would configure a shift towards a worse equilibrium, with effects on the financing conditions of the public and private sectors. Higher interest rates indicate a situation of greater distrust on the part of public debt financiers regarding the solvency conditions of the public sector, that is, regarding the trajectory of public debt as a proportion of GDP.

The IFI expects the gross debt to end in 2022 at 79.4% of GDP. The IFI's base scenario considers a gradual growth of the General Government Gross Debt (DBGG) as a proportion of GDP in the projection horizon from 2022 to 2031 when it would rise from 79.4% of GDP at the end of 2022 to 84.7% of GDP in 2031. This trajectory is supported by a consolidated public sector primary Balance of 0.3% of GDP from 2024 to 2031, an average GDP growth expectation of 2.1%, and an implicit real rate of the gross debt of 3.9% during the period.

In June, the IFI projected the DBGG at 78.7% of GDP. The upward revision in the projection in July occurred due to a change in the expectation for the economy's base interest rate (Selic) in 2022, which increased, and the downward revision in the IPCA projection, which raised the real interest rates expected for this year. In June, the IFI forecasted the Selic at 13.25% by the end of 2022. Now, the projection is 13.75%. For the IPCA, the prediction for 2022 moved from 8.6% to 7.4%. Thus, the IFI's forecast for the implicit rate of gross debt went from 2.8% in June to 4.4%. By comparison, the Ministry of Economy projects the DBGG at 78.3% at the end of 2022<sup>7</sup>, according to the Fiscal Projections Report for the first half of 2022, published on June 29.

The primary surplus required to stabilize the DBGG at 79.4% is 1.4% of GDP. Considering the debt sustainability equation, the level of primary surplus needed to stabilize the DBGG at the level of 79.4% of GDP (IFI's projection for the variable at the end of 2022) would be 1.4% of GDP, 1.1 p.p. of GDP higher than the current projection of the baseline scenario (0.3% of GDP).

## 2.2 Primary revenues and transfers

In May, the central government's primary revenue increased 5.6% above inflation compared to the same month in 2021. According to the Central Government Primary Balance (RTN) from the National Treasury Secretariat (STN), the central government's total primary revenue, which includes the federal government, the Central Bank, and the INSS, reached R\$ 172.9 billion in May 2022, R\$ 26.4 billion higher than the revenue recorded in the same month last

Link to acess the document: https://www.tesourotransparente.gov.br/publicacoes/relatorio-de-projecoes-fiscais/2022/20.

JULY 13.2022



year, a growth of 5.6% above inflation. Revenues collected by the Federal Revenue Office (R\$ 102.0 billion) grew 2.4%, while the net collection for the RGPS (R\$ 42.0 billion) rose 11.7%, and non-managed revenues (R\$ 28.8 billion) increased 9.1%.

In the year, the real growth in primary revenue was 10.9%. From January to May 2022, total revenue was R\$ 942.1 billion, an increase of 10.9% compared to 2021 (Table 4). The performance of the revenues continues to reflect the dynamics of the domestic economic activity, especially in the retail and service sectors, as well as inflation, which increases the tax bases.

**Growth occurred in the three main revenue groups.** From January to May, unmanaged revenues, which totaled R\$ 142.8 billion, were the ones that showed the most significant advance, 26.7% in real terms, compared to the same period in 2021. Revenues collected by the RFB, the largest group among federal revenues, reached R\$ 593.7 billion, an increase of 8.7%, while net revenue for the RGPS totaled R\$ 205.6 billion of 8.1% over the previous year (Table 4).

According to the Treasury, the following explains the performance of the central government's primary revenues from January through May:

- Income Tax (IR): a 16.1% increase, in real terms, from R\$ 222.5 billion in 2021 to R\$ 287.0 billion in 2022, due to higher collections in Corporate Income Tax (IRPJ) an increase of 23.6% in the period from January to May compared to 2021 and in Personal income tax (IRRF) an increase of 13.1% above inflation. The STN also highlights the growth of 83.2% in collecting adjustments to the IRPJ and CSLL from taxable events in 2021 and a 14.5% increase in the collection of monthly estimates, as well as growth in all forms of profit calculation. The STN also mentions an extraordinary collection of R\$ 20.0 billion by companies in the commodities sectors, compared to R\$ 16.0 billion collected in the first five months of 2021;
- Tax on Credit Operations, Exchange, and Insurance (IOF): an increase of R\$ 7.2 billion in collections, representing 29.0%. The explanation given by the STN for the performance of this tax was the credit operations of individuals and legal entities and the increase in operations with securities;
- **Social Contribution on Net Corporate Profits (CSLL):** revenue increase of R\$ 25.1 billion in nominal terms and an actual increase of 34.9% compared to the first five months of 2021. The explanation for the performance of this collection is the same provided for the IRPJ;
- **Net Social Security Revenues:** an increase of R\$ 34.6 billion in the first five months of 2022, compared to 2021, due to a real growth of 30.9% in the collection of Simples Nacional and the generation of 770.6 thousand formal jobs in the labor market, according to information from the General Register of Employed and Unemployed (Caged), of the Ministry of Labor and Employment (MTE);
- Concessions and Permissions: the increase of R\$ 12.3 billion in the collection in the first five months of 2022 compared to 2021 (+ 675.0%, in real terms) was due to the receipt by the Federal Government, in February 2022, of the signature bonuses related to the second round of the onerous cession, without counterpart in the period from January to May of the previous year; and
- **Exploration of natural resources:** nominal increase of R\$ 23.1 billion and real growth of 48.6% compared to 2021, driven by the combination of relatively high oil prices in the international market, the R\$/US\$ exchange rate, and domestic production.



TABLE 4. CENTRAL GOVERNMENT'S REVENUES – 2020 – 2022 – JAN – MAY (R\$ BILLION CURRENT, REAL % CHANGE, AND % OF GDP)

	Ja	an-May/20		J	an-May/21	Jan-May/22			
	R\$ B current	Real % change	% GDP	R\$ B current	Real % change	% GDP	R\$ B current	Real % change	% GDP
Total revenue	577.9	-14.2%	19.4%	764.2	24.7%	21.9%	942.1	10.9%	24.2%
Revenues Collected by RFB, except RGPS	369.1	-12.9%	12.4%	491.7	25.7%	14.1%	593.7	8.7%	15.2%
Fiscal incentives	0.0	-	0.0%	0.0	-	0.0%	0.0	-	0.0%
RGPS	140.6	-15.9%	4.7%	171.1	14.7%	4.9%	205.6	8.1%	5.3%
Revenues not collected by RFB	68.3	-17.4%	2.3%	101.5	39.7%	2.9%	142.8	26.7%	3.7%
Transfers	115.8	-6.8%	3.9%	142.6	16.1%	4.1%	193.7	22.1%	5.0%
Net revenue	462.1	-15.9%	15.5%	621.5	26.8%	17.8%	748.4	8.4%	19.2%
Total revenue without non-recurrent event*	637.8	-3.1%	21.5%	745.7	10.2%	21.4%	907.5	9.5%	23.3%
Net revenue without non-recurrent event *	522.0	-2.3%	17.6%	603.1	8.9%	17.3%	713.9	6.5%	18.3%
GDP (R\$ billion)			2,972.0			3,491.7			3,893.3

Source: National Treasury Secretariat, Tesouro Gerencial, Siga Brasil, and Central Bank. Prepared by: IFI. \* The non-recurrent events are presented and described in the IFI's EE No. 17, 2021.

After government measures, IPI and Cofins tax collections show a significant drop. Still, concerning the explanations provided by the STN for the behavior of primary revenues in the first five months of 2022, two facts should be highlighted regarding the reduction of taxes promoted by the Executive in the first months of the year: (i) IPI collection was reduced by 16.5%, in real terms, compared to the same period in 2021, influenced by the 30.9% drop in the effective average rate of IPI-Vinculado, by the 4.1% contraction in the industrial production between December 2021 and April 2022, and by the 25% decrease in IPI rates for all products; and (ii) the collection of the Contribution to Social Security Financing (Cofins) fell 7.1%, in real terms, a result influenced by the reduction to zero in the rates levied on the sale of diesel, biodiesel, aviation kerosene and liquefied petroleum gas (LPG), although the effect has been partially offset by collections from the fuel, retail, financial and service sectors.

**Growth in shared taxes and resources collected in the second round of the onerous cession boosted transfers to sub-national entities in 2022.** Table 4 also contains information regarding the transfers by revenue sharing to states and municipalities, which totaled R\$ 193.7 billion in the accumulated total for 2022 through May, an increase of 22.1% in real terms over 2021. This growth in transfers in the year to May reflects: (i) the increase in the collection of taxes shared by the Union with the sub-national entities, especially the income tax and revenues from the exploration of natural resources; and (ii) the transfer by the Union to the sub-national entities, in May, of R\$ 7.7 billion from the funds collected in the signing of the second round of the onerous transfer in February.

**Until May, the central government's net primary revenue grew 8.4% above inflation.** After discounting transfers by revenue sharing from the total primary revenue, the net revenue of the central government totaled R\$ 748.4 billion in the first five months of 2022, an amount 8.4% higher, in real terms, than in the same period of 2021, when there was an increase of 26.8% over 2020 (Table 4).

Recurring revenue recorded an increase of 9.5% in the accumulated five months in 2022. Excluding the effects of atypicality on revenues (Refis payments, concessions, and grants, anticipated dividends, operations with assets, and

JULY 13.2022



atypical collections reported by the Federal Revenue Service), the recurring primary revenue of the Union was R\$ 907.5 billion in the period from January to May, an increase of 9.5% above inflation compared to 2021, when an expansion of 10.2% had been recorded in the indicator. The recurring net revenue, in turn, totaled R\$ 713.9 billion between January and May, an amount 6.5% higher, in real terms, than the same period in 2021. The calculation of recurring revenues is based on the Special Study (EE) No. 17 of December 2021<sup>8</sup>.

**Discounting atypical factors in the collection reinforces the robustness of the results, which are driven by inflation, commodity prices, and the recovery of economic activity.** The isolation of atypical factors on primary revenues shows the robustness of the federal tax collection results in 2022, repeating what was observed last year. As highlighted in previous editions of this report, commodity prices, inflation, and the behavior of economic activity sustain this revenue performance. It is important to note, however, that the monetary tightening conducted by the Central Bank to reduce inflation and bring the IPCA to the target center will affect economic activity in the future.

Rising interest rates in several countries will slow global economic activity and reduce commodity prices. The monetary authorities in the leading developed countries have started to adopt restrictive monetary policies due to high inflation. This coordinated tightening of monetary policy will weaken economies, potentiating the effects on emerging markets such as Brazil. One of the channels of this transmission would be commodity prices, for which some reduction is expected in the coming months. This is, therefore, another risk factor for the tax collection scenario in Brazil, which the IFI is monitoring.

The central government's primary revenue increased by 15.7% in twelve months. According to the RTN, total revenue totaled R\$ 2,110.6 billion (23.2% of GDP) in the 12 months ending in May 2022, an increase of 15.7% in real terms compared to May 2021. On this basis of comparison, managed revenues totaled R\$ 1,297.7 billion (14.3% of GDP), an increase of 15.2% compared to 2021; the net collection for the RGPS reached R\$ 496.8 billion (5.5% of GDP), a rise of 3.3%; while unmanaged revenues reached R\$ 316.2 billion (3.5% of GDP), an increase of 45.7%.

The IFI's projection for total primary revenue in 2022 is R\$ 2,222.9 billion (22.9% of GDP). In July, the IFI changed the projection for primary revenue from R\$ 2,188.9 billion to R\$ 2,222.9 billion, an increase of R\$ 34.0 billion (Table 5). The revision was motivated by gains of R\$ 8.4 billion in net social securities revenue projection and R\$ 30.3 billion in unmanaged revenues. The projection for managed revenues was reduced by R\$ 4.6 billion due to the lower forecasts for inflation and nominal GDP for the year.

Concerning the RGPS revenue, the revision in the projection considered the higher realized values than those previously projected. Although the recovery of employment in the economy is more vigorous in the informal market, formal employment also shows growth, which boosts social security payments.

In non-managed revenues, the upward revision of R\$ 30.3 billion in the projection was due to a substantial collection in June, which IFI recorded in the Tesouro Gerencial and the Siga Brasil Portal. In the concessions and permissions item, there was an inflow of R\$ 26.8 billion from a signature bonus paid by Eletrobras on June 20, referring to new electricity generation concession contracts. This payment was informed to the market through a material fact<sup>9</sup>.

Table 5 compares the most recent IFI projections for central government primary revenues and transfers by revenue breakdown.

<sup>8</sup> Available at: https://www2.senado.leg.br/bdsf/bitstream/handle/id/594656/EE17 Resultado Estrutural.pdf.

<sup>&</sup>lt;sup>9</sup> Available at: https://ri.eletrobras.com/informacoes/fatos-relevantes/. See relevant facts of 06/17/2022 (privatization) and 06/20/2022 (grant bonus).



TABLE 5. IFI ESTIMATES FOR PRIMARY REVENUES AND TRANSFERS TO SUBNATIONAL ENTITIES IN 2022 (R\$ BILLION)

Baseline scenario	May/22	Jun/22	Jul/22	Dif. Jul/22- Jun/22	Var. % (Jul/22 over Jun/22)
1. Total Revenue	2,151.76	2,188.88	2,222.89	34.01	1.6%
Revenues Collected by RFB, except RGPS and fiscal incentives	1,338.85	1,348.17	1,343.52	-4.65	-0.3%
RGPS Revenues	511.27	525.17	533.55	8.38	1.6%
Revenues not Collected by RFB	301.64	315.54	345.81	30.28	9.6%
Fiscal Incentives	0.00	0.00	0.00	0.00	-
2. Transfers by revenue sharing	406.47	445.64	438.59	-7.05	-1.6%
3. Net revenue [(1)-(2)]	1,745.30	1,743.23	1,784.30	41.06	2.4%

Source: National Treasury Secretariat, Tesouro Gerencial. Prepared by: IFI.

By comparison, in July, the median projection of the economists participating in the Monthly Report from Prisma Fiscal <sup>10</sup> of the Ministry of the Economy was for a federal collection of R\$ 2,166.6 billion in 2022. The projection of the Executive Branch contained in the Primary Revenue and Expenditure Evaluation Report (RARDP) of the 2nd Bimester of 2022 May<sup>11</sup> and in the Fiscal Projections Report<sup>12</sup>, released on June 29, is total primary revenue of R\$ 2,167.1 billion (22.3% of GDP) this year.

**IFI's projection for the central government's net primary revenue in 2022 was changed to R\$ 1,784.3 billion (18.4% of GDP).** For the net revenue of the central government in 2022, the IFI projects the sum of R\$ 1,784.3 billion (18.4% of GDP), as shown in Table 5. The market consensus captured by the Prisma Fiscal contains the projection of R\$ 1,762.4 billion this year, while the Executive Branch projects R\$ 1,722.4 billion for the variable, according to the last Bimonthly Report of Revenue and Expenditure Evaluation. In the Fiscal Projections Report, the government projects net primary revenue at 17.7% of GDP by the end of 2022.

The projections for tax collection include the revenue waiver measures implemented during the year's first half. It is worth mentioning that the IFI's predictions for the total and net primary revenues of the central government contemplate, besides the measures already adopted by the government until last May and presented in the RAF No. 64 of May 2022 (reduction of the PIS/Cofins on diesel oil and cooking gas, Refis do Simples, an increase of the CSLL for banks, a decrease of the IPI and Import Tax rates), the drop to zero of the Cide and PIS/Cofins rates on gasoline and ethanol in June 2022.

#### 2.3 Primary expenditures

In May, the central government's primary expenditure increased, in real terms, by 7.9% to May 2021. According to the RTN, the central government's total primary expense was R\$ 161.4 billion in May 2022, R\$ 27.5 billion higher than in the same month of 2021, an increase of 7.9%. In this comparison, the expense with social security benefits, R\$

<sup>&</sup>lt;sup>10</sup> Available at: <a href="https://www.gov.br/fazenda/pt-br/centrais-de-conteudos/publicacoes/relatorios-do-prisma-fiscal/relatoriomensal/2022/relatoriomensal julho 2022-v2.pdf/view.">https://www.gov.br/fazenda/pt-br/centrais-de-conteudos/publicacoes/relatorios-do-prisma-fiscal/relatoriomensal/2022/relatoriomensal julho 2022-v2.pdf/view.</a>

<sup>&</sup>lt;sup>11</sup> Available at: https://www.tesourotransparente.gov.br/publicacoes/relatorio-de-avaliacao-de-receitas-e-despesas-primarias-rardp/2022/14.

<sup>&</sup>lt;sup>12</sup> Available at: https://www.tesourotransparente.gov.br/publicacoes/relatorio-de-projecoes-fiscais/2022/20.

JULY 13.2022



89.0 billion, grew 30.3%, while the expense with personnel and social charges totaled R\$ 25.2 billion, decreasing 8.6% in May.

**In the year, primary expenditures grew 6.0% to 2021.** Table 6 presents the Union's central primary spending in the accumulated year to May 2022. The total expenditure amounted to R\$ 709.2 billion, an increase of 6.0% by 2021. The STN highlighted events related to the following set of expenses in the five-month accumulated in 2022:

- Social security benefits: the strong growth in the year-to-date until May, 8.8%, in real terms, is related to the anticipation of the payment of the annual bonus (13th) to retirees and pensioners of the INSS for April, May, and June. In 2021, these payments were concentrated in May (R\$ 6.5 billion), June (R\$ 28.0 billion), and July (R\$ 21.6 billion). In 2022, the 13th bonus has already been paid, R\$ 6.4 billion in April and R\$ 28.2 billion in May;
- **Personnel and social security:** the drop of 8.2% registered in the year-to-date is due to the absence of salary readjustments for civil servants;
- **Salary Allowance and Unemployment Benefit:** the 37.0% real growth in expenses in the first five months of the year resulted from the concentration of salary bonus payments in the first four months of the year, under CODEFAT Resolution No. 934/2022, with no counterpart in the same period of 2021;
- Extraordinary credits (except PAC): the reduction in this expense (67.1%, in real terms) occurred with the decompression of expenditures made in the scope of the pandemic, such as emergency aid to people in vulnerable situations (R\$ 20.9 billion in 2021 and R\$ 3.2 billion in 2022), acquisition of vaccines (R\$ 7.2 billion in 2021 and R\$ 4.6 billion in 2022) and additional expenses of the Ministry of Health and other ministries (R\$ 9.8 billion in 2021 and R\$ 4.6 billion in 2022);
- **Compulsory expenditure with cash flow control:** the growth of 40.7% is explained by the variation of R\$ 25.4 billion in the item "Bolsa Família and Brazil Aid"; and
- **Discretionary spending by the Executive Branch:** the 24.5% increase is due to increased spending on the Health (+R\$ 1.9 billion) and Social Assistance (+R\$ 1.8 billion) functions.



TABLE 6. SELECTED CENTRAL GOVERNMENT'S EXPENDITURES – JAN-MAY (R\$ B CURRENT, REAL % CHANGE, AND % OF GDP)

	Jan-N	/lay/20		Jan-	May/21		Jai	n-May/22	:
	R\$ B current	Real % change	% GDP	R\$ B current	Real % change	% GDP	R\$ B current	Real % change	% GDP
Total expenditure	684.6	20.8%	23.0%	601.6	-17.3%	17.2%	709.2	6.0%	18.2%
Social Security Benefits (RGPS)	280.9	12.6%	9.5%	274.3	-8.0%	7.9%	332.4	8.8%	8.5%
Personnel (working and retired employees)	124.5	-3.6%	4.2%	126.2	-4.5%	3.6%	128.8	-8.2%	3.3%
Salary allowance and unemployment insurance	24.9	-1.8%	0.8%	26.0	-0.9%	0.7%	39.7	37.0%	1.0%
Continuous Cash Benefit (BPC)	26.1	2.4%	0.9%	27.9	0.4%	0.8%	31.3	1.0%	0.8%
Extraordinary Credits (except PAC)	9.4	3,572.0%	3.2%	36.0	-64.4%	1.0%	13.0	-67.1%	0.3%
Compensation to RGPS for Exemption of Payroll Taxes	4.8	-13.7%	0.2%	3.5	-30.3%	0.1%	3.1	-21.2%	0.1%
Fundeb	8.0	-1.1%	0.3%	8.6	2.2%	0.2%	14.0	45.5%	0.4%
Court Rulings and Court-Ordered Debts	1.0	-92.7%	0.0%	1.1	-2.4%	0.0%	1.3	6.0%	0.0%
Subsidies, Grants, and Proagro	20.8	28.,5%	0.7%	2.8	-87.1%	0.1%	7.2	130.1%	0.2%
Mandatory expenditure	646.4	21.9%	21.8%	573.6	-16.5%	16.4%	670.3	5.0%	17.2%
Mandatory spending with flow control	52.9	<i>-6.2%</i>	1.8%	57.4	2.2%	1.6%	89.8	40.7%	2.3%
Discretionary	38.2	5.2%	1.3%	28.0	-31.1%	0.8%	38.9	24.5%	1.0%
Total expenditure without non-recurrent events*	541.5	-4.5%	18.2%	559.6	-2.6%	16.0%	659.3	5.9%	16.9%
GDP (R\$ billion)		2,972.0	)		3,	491.7	3,893.3		

<sup>\*</sup> The non-recurrent events are presented and described in the IFI's EE No. 17, 2021. Source: National Treasury Secretariat and Central Bank. Prepared by: IFI.

Table 6 also presents the recurrent expenditure of the central government, calculated by the IFI based on the methodology published in EE No.17, December 2021. On the expenditure side, the calculation considers non-recurring expenses realized in the scope of the Covid-19 pandemic, expenses related to the onerous assignment of the pre-salt and the Brazil Sovereign Fund, and anticipations in the payment of the salary allowance and the RGPS 13th bonus.

The central government's recurrent primary expense grew 5.9% compared to 2021. In the year to May 2022, recurrent primary expenditure (excluding non-recurring events) totaled R\$ 659.3 billion, an increase of 5.9% over 2021. The difference of R\$ 49.9 billion between total primary expenditure (R\$ 709.2 billion) and recurrent primary expenditure (R\$ 659.3 billion) in the period is explained by: (i) R\$ 15.3 billion of expenses executed in the scope of the pandemic; and (ii) R\$ 34.6 billion paid as an anticipation of the 13th bonus to retirees and pensioners of the INSS.

The IFI's projection for primary expenditure in 2022 rose from R\$ 1,793.2 billion (18.4% of GDP) to R\$ 1,825.2 billion (18.8% of GDP) at the end of the year. In the 12-month comparison, total primary expenditure reached R\$ 1,721.7 billion (19.0% of GDP) in May, a reduction of 16.7% compared to the same month in 2021. The IFI's new projection for the variable is R\$ 1,825.2 billion (18.8% of GDP) in 2022. By comparison, the median of the projections compiled by the Prisma Fiscal, July 2022, is R\$ 1,792.6 billion, while the government's estimate from the latest Bimonthly Report on Primary Revenue and Expenditures is R\$ 1,787.9 billion.

A comparison between total and recurrent primary expenditures shows a downward trend as a proportion of GDP. Figure 7 presents the evolution in 12 months of the total realized primary spending and the recurrent



expenditure calculated by the IFI according to the methodology presented in EE No.17 of 2021. The total primary spending reached 20.0% of GDP in May (against 20.1% of GDP in April), while the spending without non-recurring events (or recurrent) reached 18.5% of GDP (against 18.6% of GDP in April). Both curves suggest that primary expenditure remains relatively under control.

The fiscal space opened up in 2022 with Constitutional Amendments No. 113 and No. 114, as well as Constitutional Amendment Bill (PEC) No. 1 of 2022, which will slow the pace of reduction in primary expenditure as a proportion of GDP. The IFI's projection is for primary spending at 18.8% of GDP by the end of 2022. The drop observed in recent months is explained to a greater extent by the substantial increase in nominal GDP and, to a lesser extent, by the absence of adjustments to public servants since 2019.

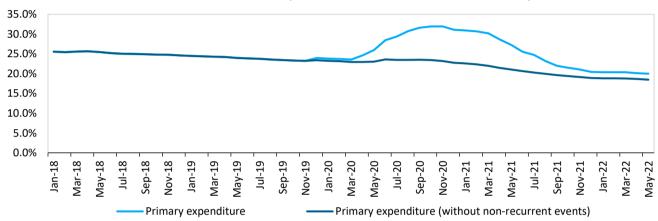


FIGURE 7. TOTAL PRIMARY EXPENDITURES (WITH AND WITHOUT NON-RECURRING EVENTS) - % OF GDP

Source: National Treasury Secretariat. Prepared by: IFI.

#### 2.4 The central government and the consolidated public sector balance<sup>13</sup>

**Despite the deficit observed in May, the central government's primary balance accumulates a surplus of R\$ 39.2 billion in the year.** Also, according to the information released by the Treasury in the RTN, the central government had a primary deficit of R\$ 39.4 billion in May 2022, R\$ 18.4 billion higher than the deficit recorded in the same month last year. In the five months of 2022, the central government has calculated a positive primary balance of R\$ 39.2 billion, determined by the behavior of tax collection, which continued to register a strong performance, as well as by the relative control of primary expenditure.

The IFI's projection for the primary deficit in 2022 went from R\$ 49.9 billion (0.5% of GDP) to R\$ 40.9 billion (0.4% of GDP). In the 12 months ending in May, the central government had a primary deficit of R\$ 15.8 billion (0.2% of GDP) against a deficit of R\$ 500.9 billion (6.3% of GDP) in the same month last year. The IFI's projection for the Union's primary balance in 2022 is a deficit of R\$ 40.9 billion (0.4% of GDP). The market consensus captured by the Prisma Fiscal of July was a primary deficit of R\$ 20.0 billion this year, while the Executive Branch expects a deficit of R\$ 65.5 billion, according to the Bimonthly Report of Revenues and Expenditures released in May.

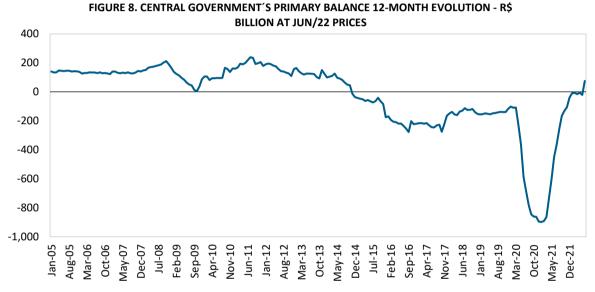
<sup>13</sup> Due to the Central Bank servers' strike, in this edition of the RAF, the information on the public sector borrowing requirements and indebtedness indicators, calculated using the Central Bank's below-the-line methodology, will not be analyzed.



#### Tesouro Gerencial and Siga Brasil's data indicate a primary surplus of R\$ 53.9 billion in the first half of 2022.

Based on information for June collected by the IFI in the Federal Senate's Siga Brasil and the Tesouro Gerencial, the central government had a primary surplus of R\$ 14.7 billion in June, reversing the R\$ 39.4 billion deficit recorded in May. With the June result, the Union's accumulated primary surplus for 2022 rose from R\$ 39.2 billion in May to R\$ 53.9 billion in June. In the 12-month comparison, the primary balance went from a R\$ 15.8 billion deficit in May to a R\$ 72.4 billion surplus in June.

Figure 8 presents the 12-month central government's primary balance trajectory at June 2022 prices, and it is possible to see the improvement from May to June, determined by the collection performance.



Source: National Treasury Secretariat, Siga Brasil and Tesouro Gerencial. Prepared by: IFI.

In the 12-month comparison, the central government's net revenue rose by R\$ 80.1 billion between May and June, while primary expenditure fell by R\$ 8.0 billion. In nominal values, net revenues rose from R\$ 1,705.9 billion in the 12 months ended in May to R\$ 1,786.0 billion in June, an increase of R\$ 80.1 billion. Primary expenditure fell from R\$ 1,721.7 billion in May to R\$ 1,713.7 billion in June, a negative variation of R\$ 8.0 billion.

**Income tax collections boosted the performance of managed revenues in June.** Still considering the 12-month comparison, Tesouro Gerencial and Siga Brasil's information shows an increase of R\$ 30.9 billion in collected revenues, in nominal values, from May to June. Of this amount, R\$ 23.3 billion (or 75.3% of the R\$ 30.9 billion total) corresponded to an increase in income tax collections, which maintained the same behavior as in previous months.

Concessions and permissions and dividends drive growth in non-managed revenues. In the 12 months, non-managed revenues grew by R\$ 49.8 billion from May to June, with the highlight going to collections from concessions and permissions (+ R\$ 26.6 billion in the 12-month comparison between May and June) and dividends (+ R\$ 25.9 billion).

This strong growth in tax collection in June, according to data from Siga Brasil and Tesouro Gerencial, led the IFI to revise the projection for primary revenue of the central government in 2022, even though the expectation for nominal GDP was reduced due to the downward change in the implicit deflator projection.



monetary tightening.

#### 2.5 Public sector indebtedness indicators<sup>14</sup>

The adoption of contractionary monetary policies amplifies uncertainties in the global economic environment. In May and June, risk premiums of emerging countries continued to rise due to the uncertain climate associated with the worldwide economy. Developed countries began to adopt contractionary monetary policies to curb inflationary pressures. The consequence of this synchronized movement may be a recession in several locations, with an increase in the flow of capital to advanced economies, particularly the United States, and a reduction in commodity prices. This combination of effects may further hurt emerging markets, such as Brazil, which are in a more advanced stage of

The context described in the previous paragraph increases the challenges faced by the Treasury in managing the public debt, intensified by the fiscal policy actions adopted in recent months, which may compromise the sustainability of public finances in the medium and long term. The risk associated with eventual increases in primary expenditures or tax waivers, whether permanent or transitory, will continue to be monitored by the IFI.

**Outstanding Federal Public Debt rose R\$ 112.3 billion in May, compared to April.** According to information published by the National Treasury (STN) in the Monthly Debt Report (RMD), the outstanding Federal Public Debt (DPF) rose from R\$ 5,590.0 billion in April to R\$ 5,702.2 billion in May, an increase of R\$ 112.3 billion. The Domestic Federal Public Debt (DPMFi) stock in the same period increased by R\$ 116.2 billion. Between April and May, the supply of fixed-rate securities increased by R\$ 44.6 billion, inflation-linked (+ R\$ 23.3 billion), and floating-rate securities (+ R\$ 49.2 billion). The stock of foreign exchange-indexed securities dropped R\$ 4.8 billion in the period, while the outstanding External Federal Public Debt (DPFe) dropped R\$ 3.9 billion.

In April, net redemptions of debt totaled R\$ 40.6 billion, while in May, there were net issuances of R\$ 69.2 billion. Total DPF net issuance (issuance minus redemptions) was negative at R\$ 40.6 billion in April and positive at R\$ 69.2 billion in May. In the DPMFi, net issuance was negative by R\$ 39.9 billion in April and positive by R\$ 65.4 billion in May. According to the Treasury, there was a large redemption of the National Treasury Bills (LTN), fixed-rate security maturing in April 2022. The net redemption of fixed-rate securities was R\$ 75.4 billion in April. In May, issuance was concentrated in fixed-rate securities (net issuance of R\$ 34.5 billion) and floating-rate securities (net issuance of R\$ 28.7 billion).

**Public debt liquidity reserve rose 6.8% between April and May 2022.** Also, according to the Treasury, the public debt liquidity reserve was R\$ 1,108.0 billion in May, a 6.8% increase in nominal terms compared to April (R\$ 1,037.0 billion). The liquidity reserve (also called debt cushion) is part of the Treasury's cash on hand deposited in the Single Account at the Central Bank. Over the next 12 months, DMPFi maturities of R\$ 1,310 billion are expected. In other words, the current liquidity reserve is insufficient to pay the Treasury's short-term commitments.

Average DPMFi issuance of fixed-rate securities continued to rise in May. The average issue rates of the DPMFi rose in May, according to information presented by the STN on the RMD. For 24-month fixed-rate securities (LTN), the average issue rate was 12.85% p.a. in May, against 12.60% p.a. in April. In 48-month fixed-rate bonds, the rate was 12.35% p.a. in May, compared to 12.13% p.a. in April. In the 10-year fixed-rate bond, with semi-annual interest payments, the average issue rate rose from 12.30% p.a. in April to 12.61% p.a. in May.

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<sup>&</sup>lt;sup>14</sup> Due to the strike by the Central Bank of Brazil's servers, responsible for calculating the statistics for the consolidated public sector balance by the below-the-line concept and gross and net debt, the May data have not yet been released. For this reason, this topic does not contain evaluations regarding these indicators, as traditionally occurs in the RAF. It is worth saying that this situation is worrying because it makes it difficult to monitor the overall public accounts condition.

JULY 13.2022



**In June, average issue rates continued to rise.** Information gathered by the IFI regarding auctions held by the Treasury<sup>15</sup> indicates new increases in the rates of the DPMFi auctions in June. For example, a fixed-rate bond maturing on April 1, 2023, had an average issuance rate of 13.55% p.a. in June. In May, the average rate for this security was 13.44% p.a. For the fixed-rate bond maturing on July 1, 2025, the average issue rate went from 12.33% p.a. in May to 12.55% p.a. in June. The securities (and their respective maturities) are communicated quarterly by the Treasury and may change over time.

The rising trend in public bond issue rates shows an increase in the perception of risk by agents that finance the Brazilian public debt. The rise in DPMFi bond issue rates in recent months characterizes an increase in the perception of risk by agents that fund the Brazilian public debt. Even though the global economic context is one of higher average interest rates in the medium term, the fiscal policy conducted in recent months may have contributed to a loss of credibility of the regime, encouraging higher premiums by debt financing agents in the auctions held by the Treasury.

The share of securities maturing in up to 12 months grew and reached 23.4% in May. Figure 9 contains information on the profile of Federal Public Debt (DPF) maturities made available in the Monthly Debt Report. In May, securities maturing in up to 12 months accounted for 23.4% of the DPF stock, 2.9 p.p. above that registered in April. By May 2021, this stock had a 0.4 p.p. increase.

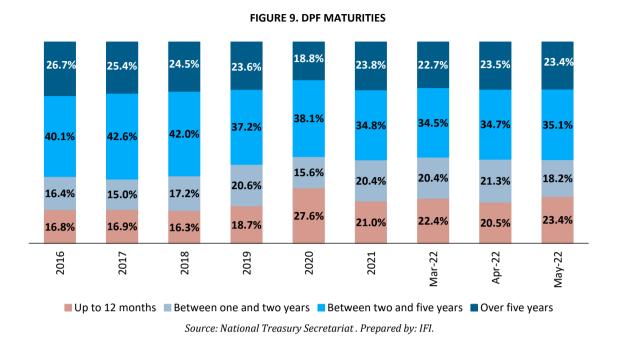
This increase in the percentage of debt maturing in the next 12 months in May, compared to April, is a result of the large volume of fixed-rate securities redeemed in April (LTN maturing in April 2022), as well as the entry of a large quantity of fixed-rate securities (LTN maturing in May 2023) into the next 12-month window, according to explanations given by the Treasury in the May RMD press conference.

**Securities with maturity above five years reached 23.4% of the stock.** Securities with maturity over five years reached 23.4% of the DPF stock in May 2022, a reduction of 0.1 p.p. in April and an increase of 3.4 p.p. in May 2021. The increased participation of longer maturity securities in the DPF stock reflects the increased issuance of long-term debt that the Treasury has achieved, particularly floating rate and inflation-linked bonds.

The maturity lengthening has been accompanied by an increase in the outstanding average cost. After the shortening observed in the federal debt profile in 2020 (increase in the relative share of securities with shorter maturities and reduction in those with longer maturities), the Treasury has managed to lengthen the maturity profile of public securities.

<sup>&</sup>lt;sup>15</sup> Available at: <a href="https://www12.senado.leg.br/ifi/dados/dados">https://www12.senado.leg.br/ifi/dados/dados</a>.





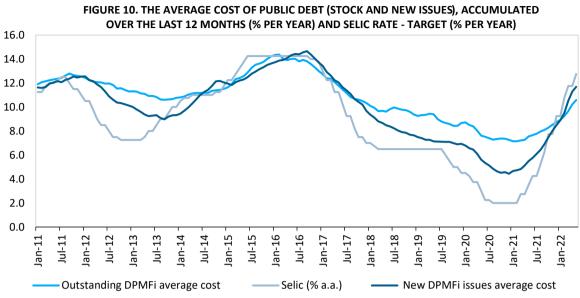
The outstanding DPMFi average cost in May is 3.03 p.p. above May 2021. To conclude the analysis of indebtedness indicators, the 12-month accumulated average cost of the DPMFi rose 0.37 p.p. in May, compared to April, to 10.58% p.a., the fifteenth consecutive increase in the monthly comparison. Compared to May 2021, the outstanding DPMFi average cost rose by 3.03 p.p. (Figure 10).

The average cost of DPMFi issuances rose 6.2 p.p. compared to May 2021. The average cost of DPMFi public offerings also rose in May to 11.69% p.a., compared to 11.29% p.a. in April (0.4 p.p. increase). By May 2021, the average cost of DPMFi issues grew by 6.20 p.p. (Figure 10). It is worth noting that, on this basis of comparison, the average cost of issues rises quickly and already exceeds the outstanding average cost, indicating that the latter will continue to grow in the coming months.

The rise in the base interest rate is one of the reasons for the increase in the average cost of public bonds. The increase in the outstanding average cost and new DPMFi issues as of March 2021 occurred, among other reasons, due to the contractionary monetary policy adopted by the Central Bank. This movement is evident considering the increase in net issuance of floating-rate securities, which is the Selic rate itself. In the last meeting of the Monetary Policy Committee (Copom), the Selic was raised to 12.75% p.a. The latest available release of the Central Bank's Focus Survey, with information updated up to July 1, 2022, indicated that the market consensus forecast the Selic at 13.75% at the end of 2022, the same projection as the IFI.

The outstanding DPMFi average cost and new issues are expected to continue to grow in the coming months. Additional hikes scheduled for the Selic in the coming months suggest that the average cost of the debt will continue to rise. Besides this, the risk calculated by economic agents in the forward yield curve will pressure the average cost of the debt, worsening the future scenario, which recently benefited from the increase in nominal GDP under the influence of high inflation.





#### Source: National Treasury Secretariat . Prepared by: IFI.

#### 2.6 The PLDO for 2023

The Federal Constitution determines that the National Congress must approve the Budget Guidelines Law Project (PLDO) by July 17 of the previous year. <sup>16</sup> The PLDO 2023 was sent by the Executive Branch on April 14, when it started to be discussed in the National Congress. On June 29, the Joint Committee on Planning, Public Budgets, and Oversight (CMO) approved Opinion No. 6 for 2022, referring to the PLDO. <sup>17</sup> On July 12, the project was approved by the National Congress. <sup>18</sup> The budget guidelines include projections for budget parameters, such as GDP, inflation, and interest rates; setting the primary balance target; and designing the rules that will guide the formulation of the budget. The figure below shows the timeline for processing the 2023 PLDO with evidence of the project's current status in the National Congress.

The addendum to CMO's Opinion No. 6 of 2022 is available at: <a href="https://legis.senado.leg.br/sdleg-getter/documento?dm=9185288&ts=1657656077465&disposition=inline">https://legis.senado.leg.br/sdleg-getter/documento?dm=9185288&ts=1657656077465&disposition=inline</a>;

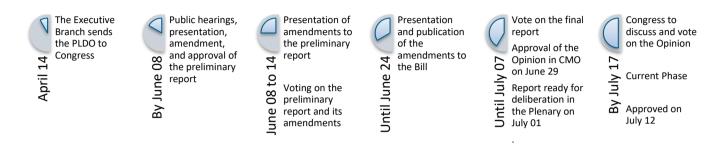
The list of the highlights voted is available at: <a href="https://legis.senado.leg.br/sdleg-getter/documento?dm=9185341&ts=1657656077200&disposition=inline">https://legis.senado.leg.br/sdleg-getter/documento?dm=9185341&ts=1657656077200&disposition=inline</a>;

<sup>16</sup> The legislative session cannot be interrupted if the PLDO is not approved by this date. See art. 57 § 2 of the 1988 Federal Constitution.

<sup>&</sup>lt;sup>17</sup> Available at: https://legis.senado.leg.br/sdleg-getter/documento?dm=9180388&ts=1657255298479&disposition=inline.

<sup>&</sup>lt;sup>18</sup> The analysis of this RAF was made based on Opinion No. 6, of 2022. Comments on the approval of the Opinion were inserted throughout the text, but until the end of the preparation of this RAF, the final text approved by Congress had not yet been released, considering the vote of the highlights.

#### FIGURE 1. SUMMARY TIMELINE OF THE 2023 PLDO



Source: CMO - National Congress19. Prepared by: IFI.

The primary deficit target in the 2023 PLDO is R\$ 65.9 billion. The 2023 PLDO <sup>20</sup> indicates a primary deficit target for the central government of R\$ 65.9 billion. In turn, the deficit target for the consolidated public sector, which includes states, municipalities, and state-owned companies, is R\$ 69.0 billion. As in previous years, the obligation is linked only to the central government's share. Total primary revenues for the central government are estimated at R\$ 2,230.3 billion, with revenues net of transfers to subnational entities at R\$ 1,800.9 billion and total primary expenditures at R\$ 1,866.8 billion.

Table 7 below presents the detailed fiscal framework of the 2023 PLDO compared to the IFI's baseline scenario for 2023. The table also shows the projections for GDP and inflation.

<sup>&</sup>lt;sup>19</sup> Figure 1 is a summary of the Joint Information Note of 05/18/2022 (available at: <a href="https://legis.senado.leg.br/sdleg-getter/documento?dm=9159606&ts=1657543661004&disposition=inline">https://legis.senado.leg.br/sdleg-getter/documento?dm=9159606&ts=1657543661004&disposition=inline</a>) and the CMO Schedule, as amended on 06/08/2022 (available at: <a href="https://www.camara.leg.br/internet/comissao/index/mista/orca/ldo/LD02023/crono/crono-v2.pdf">https://www.camara.leg.br/internet/comissao/index/mista/orca/ldo/LD02023/crono/crono-v2.pdf</a>)

 $<sup>^{20}</sup>$  Access here the Presidential Message, the text of the PLDO, and the attachments –  $\frac{https://www2.camara.leg.br/orcamento-da-uniao/leis-orcamentarias/ldo/2022/tramitacao/proposta-do-poder-executivo}.$ 



TABLE 7. REVENUES, EXPENSES, PRIMARY BALANCE, GDP, AND INFLATION - IFI AND PLDO 2023 (R\$ BILLION AND % OF GDP)

	PLDO 2	2023	IFI Jul/202	2 - 2023	D:f (1 11)
	R\$ B (I)	% GDP	R\$ B (II)	% GDP	Dif. (I - II)
Total revenue (A)	2,230.3	21.3	2,321.2	22.4	-90.9
Revenues Collected by RFB, except RGPS	1,392.3	13.3	1,467.3	14.2	-75.0
RGPS Revenues	552.1	5.3	566.6	5.5	-14.5
Revenues not Collected by RFB	286.0	2.7	287.3	2.8	-1.3
Transfers by revenue sharing	429.4	4.1	453.7	4.4	-24.2
Net revenue (C = A - B)	1,800.9	17.2	1,867.5	18.0	-66.6
Total expenditure (D)	1,866.8	17.8	1,866.2	18.0	0.7
Social Security (RGPS)	849.5	8.1	857.4	8.3	-7.8
Payroll	356.4	3.4	360.2	3.5	-3.8
Other mandatory	315.6**	3.0**	266.8	2.6	48.8
Expenses Subject to Financial Programming	345.2	3.3	381.8	3.7	-36.6
Mandatory spending with flow control	237.0	2.3	235.4	2.3	1.6
Discretionary	108.2*	1.0*	146.4	1.4	-38.1
Central gov. primary balance (E = C - D)	-65.9	-0.6	1.4	0.0	-67.3
National Treasury balance	231.6	2.2	292.1	2.8	-60.6
Social security balance	-297.5	-2.8	-290.8	-2.8	-6.7
Spending ceiling	1,781.0	17.0	1,807.8	17.4	-26.8
Nominal GDP (R\$ billion) e real GDP (%)	10,470.3	2.5	10,360.8	0.7	
IPCA % p.a.	3.3		4.8		

<sup>\*</sup> Without contingency reserve.

Source: CMO's Opinion No. 6, of 2022, to the PLDO 2023 and IFI. Prepared by: IFI.

The total primary revenues projected in the 2023 PLDO are R\$ 90.9 billion, lower than the IFI. The so-called managed revenues, which include taxes and contributions, are lower by R\$ 75.0 billion, while the unmanaged revenues are lower than the IFI estimates by only R\$ 1.3 billion. Finally, the PLDO's projection for the third component of total primary revenues, the RGPS collection, is R\$ 14.5 billion lower than the IFI's estimate.

**Inflation projections in the PLDO and the IFI may explain differences in the revenue scenarios.** The PLDO projection for transfers to states and municipalities is R\$ 24.2 billion, lower than the IFI's estimate for 2023. Thus, the projection for total net revenue in the PLDO is lower than that of the IFI by R\$ 66.6 billion. Since the main difference between the projections is in managed and RGPS revenues, it may be explained by the discrepancy between the values projected for inflation and other macroeconomic parameters in the PLDO and the IFI scenario.

**Positive surprises in the 2022 collection may also influence the differences in the projections.** At this point, the movement of collections from January to May is worth noting. The revenues collected by the RFB and the social security collection increased 7.5% in real terms from January to May 2022, compared to the same period in 2021. The positive

<sup>\*\*</sup> With contingency reserve, under the assumption that will become amendments.

JULY 13.2022



performance influenced this figure in the IRPJ/CSLL and social security revenues. Then, a higher short-term elasticity to GDP is expected for the 2023 period than initially forecasted in the PLDO. More recent projections by the National Treasury<sup>21</sup> also incorporate these factors so that the estimate by the STN for primary revenues net of transfers to subnationals is only R\$ 9.0 billion lower than that of the IFI for 2023.

**Turning to the expenditure side, the government projects R\$ 1,866.8 billion, while the IFI estimates R\$ 1,866.2 billion.** Although the difference is only R\$ 0.7 billion in the aggregate, there are differences between the expenditure components. In the expenses with personnel and social charges, the IFI's numbers are R\$ 3.8 billion higher than the PLDO's, while for the sum in discretionary expenditures with other mandatory expenses<sup>22</sup>, our projections are R\$ 10.7 billion lower than those of the PLDO. The trajectory of mandatory spending results from two factors: projection models and assumptions for inflation, minimum wage, salary mass, and GDP, among other macroeconomic indicators that index personnel, social security, and social security expenses. Next, we comment on the differences in the projections of the PLDO and the IFI for the main mandatory spending. Then, the case of discretionary expenditures is evaluated.

**IFI** scenario for INSS social security benefits is R\$ 7.8 billion above the forecast in the 2023 PLDO. The INPC assumption affects these expenses indirectly, through the increase in the minimum wage and directly, in the case of benefits above the minimum. According to the RARDP<sup>23</sup>, the government considers 6.7% for the INPC of 2022, while the IFI projects 7.3%. According to preliminary calculations, this difference of 0.6 p.p. can explain something like R\$ 4.8 billion of the R\$ 7.8 billion described above.

The issued benefits evolution suggests that the pandemic influenced the effects observed in 2020 and 2021. The country underwent a broad pension system reform at the end of 2019. After enacting Constitutional Amendment No. 103 of 2019, which, among other changes, began to provide for a minimum age for retirement, its results were expected to appear in the medium term. With the pandemic and the effects on the INSS operation<sup>24</sup>, the evolution of the issued benefits changed. With the normalization of these services, the pattern returned before the pandemic and the reform, reinforcing the thesis that the effects of the welfare reform on the evolution of benefits issued should occur more in the medium term. Figures 11 and 12 show the development and change of these benefits from December 2017 to May 2022.

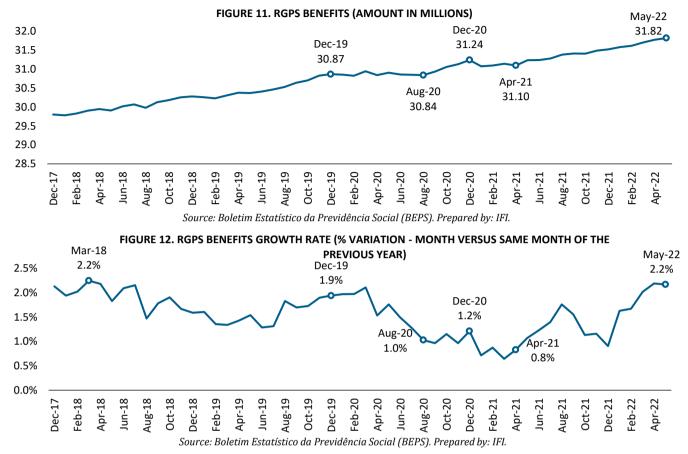
<sup>&</sup>lt;sup>21</sup> The National Treasury has started to publish a report on fiscal projections on a biannual basis. The predictions differ from the numbers presented in the budget documents (LDO and LOA) but can serve as more up-to-date parameters of government projections regarding fiscal statistics. It is worth mentioning that the predictions in the report are for the medium term, so it is possible to compare them with those of the IFI for a longer horizon. Available at: <a href="https://www.tesourotransparente.gov.br/publicacoes/relatorio-de-projecoes-fiscais/2022/20">https://www.tesourotransparente.gov.br/publicacoes/relatorio-de-projecoes-fiscais/2022/20</a>.

<sup>&</sup>lt;sup>22</sup> The comparative analysis is made by adding the mandatory and discretionary expenses since it assumes that the contingency reserve will be allocated to the parliamentary amendments classified as discretionary.

<sup>&</sup>lt;sup>23</sup> Report of the evaluation of the primary revenues and expenses of the Union. We used the RARDP because it is understood that the macroeconomic parameters have not been altered since the beginning of the process of approval of the PLDO.

<sup>&</sup>lt;sup>24</sup> Available at: https://g1.globo.com/economia/noticia/2022/07/04/inss-entram-em-vigor-novas-regras-no-atendimento-presencial.ghtml





The difference in the projection for personnel expenses reflects the effect of inflation and eventual salary adjustments. The IFI scenario for personnel expenses and social charges considers the possibility of salary increases. In the CMO report, on the other hand, there is only the indication as one of the priorities of the federal public administration (art. 4 of the PLDO). The Substitutive to the PLDO explains that for this priority to be fully effective, the proposals for salary increases and restructuring careers must be included in the specific annex (Annex V) of the LOA 2023. 26

In the IFI scenario, the spending ceiling should be R\$ 1,807.8 billion in 2023. The spending ceiling, instituted by EC 95 of 2016, and modified by ECs No. 102, 109, 113, and 114, should be higher than estimated in the PLDO due to inflation resilience. The federal spending limit is based on the previous year's limit adjusted by inflation observed in the last year.<sup>27</sup> The most recent projections indicate that inflation should be above the value projected in the PLDO, which would raise the federal spending limit to 2023. The IFI scenarios count on an IPCA inflation rate of 7.4% for 2022, which makes the spending ceiling for 2023 R\$ 1,807.8 billion.

projection made by the Executive Branch is used, and the differences are offset in the following year's ceiling.

<sup>&</sup>lt;sup>25</sup> The baseline scenario counts on vegetative growth of 0.3% (average growth from 2015 to 2019) plus a price effect compatible with inflation.

<sup>&</sup>lt;sup>26</sup> Item VIII was included in art. 115 of the PLDO to address this issue.

<sup>&</sup>lt;sup>27</sup> Besides inflation, the spending ceiling for 2023 should include the difference between the index used to correct the 2022 ceiling (10.18%) and the actual inflation (10.06%). This difference occurs because when the budget is prepared, the inflation for the entire year is not yet known. In this case, a



**Innovation in the PLDO's text allows for an automatic change in the primary balance target.** Considering the hypothesis that the spending ceiling must be higher than that estimated in the PLDO and that the budget will be allocated to use all the space in the ceiling, the report approved by the CMO innovates by allowing the primary balance target to be changed due to the deviation between the estimated spending ceiling and that which will be set in the 2023 Budget Law. The excerpt included in the PLDO states that:

(Art. 2, § 3) The primary balance target to which this article refers may be altered by an amount equivalent to the variation in the total amount of the individualized limits established by art. 107 of the "Ato das Disposições Constitucionais Transitórias" due to the application of projection for the Broad Consumer Price Index (IPCA) by the National Congress different from the one used in the preparation of the 2023 Budget Bill.

**During the vote on the PLDO in the National Congress plenary, the rapporteur deleted the section that made the amendments of the Rapporteur-General compulsory**. Another important innovation in the text of the Substitute to the PLDO presented in the form of CMO's Opinion No. 6 of 2022 refers to the general reporter amendments of the PLOA, which would now be considered impositive. The report approved by the CMO inserted art. 81-A in the text of the PLDO to state the impositive character of the programs classified as RP 9,<sup>28</sup> i.e., amendments by the general rapporteur, based on the provisions of § 10 of art. 165 of the Constitution states the duty of executing all programs related to effectively delivering public goods and services.

During the report discussed in the Plenary of the National Congress, the rapporteur deleted art. 81-A,<sup>29</sup> so that the approved text no longer considers this provision, the LDO will not provide for the amendments of the general rapporteur to be impositive.

Parliamentary amendments can assume four types of classification: (i) group amendments, (ii) individual amendments, (iii) committee amendments, and (iv) amendments of the general reporter of the PLOA. Currently, only the group and individual amendments are considered impositive (see ECs No. 86, 2015 and No. 100, 2019). To be clear, if the LDO was approved with Article 81-A, the rapporteur's amendments would also become taxable, thus increasing budgetary rigidity.

The approved text also innovates by increasing the transparency of the rapporteur-general amendments. The Substitutive to the PLDO agreed on July 12 to innovate by providing art. 77-A that the indication of beneficiaries will necessarily include the name of the requesting legislator, even when his or her plea is based on a demand presented to him or her by public agents or representatives of civil society.

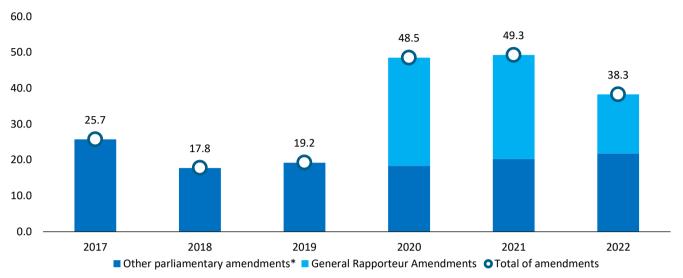
Parliamentary amendments are the instrument used by senators and deputies to make changes to the budget proposed by the Executive. In recent years, there has been a significant increase in these amendments, particularly those of the general rapporteur, causing the total amount approved in the LOA for 2022 to be R\$ 38.3 billion. As the committee and general rapporteur amendments are not binding, their value can be contingent throughout the fiscal year to comply with the fiscal rules. Figure 13 shows the evolution of the value authorized in the federal budget, year by year, for the total parliamentary amendments and those of the general rapporteur.

<sup>28</sup> RP stands for "Primary Balance Indicator." Its purpose is to assist in the classification/identification of the primary balance of the LDO and LOA. The classifications for RP can be consulted on page 85 of the Budget Technical Manual, available at:: <a href="https://www1.siop.planejamento.gov.br/mto/lib/exe/fetch.php/mto2023:mto2023-atual.pdf">https://www1.siop.planejamento.gov.br/mto/lib/exe/fetch.php/mto2023:mto2023-atual.pdf</a>

<sup>&</sup>lt;sup>29</sup> See addendum to the substitute to the Bill of Law No. 5, of 2022 (PLDO of 2023), available at: <a href="https://legis.senado.leg.br/sdleg-getter/documento?dm=9185288&ts=1657656077465&disposition=inline">https://legis.senado.leg.br/sdleg-getter/documento?dm=9185288&ts=1657656077465&disposition=inline</a>.



## FIGURE 13. AMENDMENTS PER YEAR OF PRESENTATION. AUTOGRAPH VALUES (R\$ BILLION)



Source: Siga Brasil (2020) and Technical Report No. 8/2021 - CONOF/Chamber of Deputies (2017 a 2021). Prepared by: IFI.

\* Includes amendments from state groups not classified with the primary balance identifier (PR) equal to 7.



## **Fiscal tables**

TABLE 8. IFI FORECASTS FOR THE CENTRAL GOVERNMENT PRIMARY BALANCE - BASELINE SCENARIO (% OF GDP)

	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
Gross Revenue	22.3	22.9	22.4	22.2	22.2	22.0	21.8	21.7	21.4	21.2	20.9
Transfers to States and Municipalities by Revenue Sharing	4.1	4.5	4.4	4.3	4.3	4.2	4.2	4.2	4.1	4.0	4.0
Net Revenue	18.2	18.4	18.0	17.9	17.9	17.8	17.6	17.5	17.3	17.2	16.9
Primary Expenditure	18.6	18.8	18.0	17.9	17.5	17.3	18.6	17.0	16.6	16.3	16.0
Mandatory Expenditure	17.2	17.2	16.6	16.5	16.2	16.0	17.3	15.8	15.4	15.1	14.8
Social security benefits	8.2	8.1	8.3	8.2	8.1	8.0	8.7	8.0	7.9	7.8	7.6
Personnel expenses and social contribution	3.8	3.5	3.5	3.4	3.3	3.3	3.5	3.2	3.1	3.0	2.9
Salary allowance and unemployment insurance	0.5	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.5
Salary Allowance	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Unemployment Insurance	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.3
BPC [Continuous Cash Benefit Program]	0.8	0.8	0.8	0.8	0.7	0.7	0.8	0.7	0.7	0.7	0.7
Compensation to RGPS for Exemption of Payroll Taxes	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Supplementation by the Federal Government to Fundeb	0.3	0.3	0.4	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Legislative, Judiciary, Prosecutor's Office, and Public Defender's Office	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Court Rulings and Court-Ordered Debts (current and capital expenditure)	0.2	0.2	0.2	0.2	0.2	0.2	0.7	0.3	0.3	0.3	0.3
Subsidies and Grants	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Other Mandatory Spending	3.1	3.2	2.4	2.4	2.3	2.3	2.2	2.1	2.0	2.0	1.9
without Flow Control	1.5	0.9	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1
with Flow Control	1.7	2.3	2.3	2.2	2.2	2.1	2.1	2.0	1.9	1.9	1.8
Of which Bolsa Família [Family Grant]	0.3	0.9	0.9	0.9	0.9	0.9	0.8	0.8	0.8	0.8	0.7
Discretionary of the Executive Branch	1.4	1.6	1.4	1.4	1.4	1.3	1.3	1.2	1.2	1.2	1.1
Primary Balance	-0.4	-0.4	0.0	0.0	0.3	0.5	-1.0	0.5	0.7	0.8	1.0
Note:											
Spending on Covid-19	1.4	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Nominal GDP (R\$ billion)	8,679.5	9,707.8	10,360.8	11,044.8	11,686.3	12,360.7	13,078.9	13,842.8	14,657.4	15,526.7	16,441.9



TABLE 9. IFI FORECASTS FOR THE CENTRAL GOVERNMENT PRIMARY BALANCE – OPTIMISTIC SCENARIO (% OF GDP)

	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
Gross Revenue	22.3	23.0	22.6	22.7	22.6	22.4	22.2	22.0	21.8	21.6	21.3
Transfers to States and Municipalities by Revenue Sharing	4.1	4.5	4.4	4.4	4.4	4.3	4.3	4.3	4.2	4.2	4.1
Net Revenue	18.2	18.5	18.2	18.2	18.2	18.1	17.9	17.7	17.6	17.4	17.2
Primary Expenditure	18.6	17.9	17.3	16.9	16.3	15.9	16.1	15.0	14.5	14.0	13.5
Mandatory Expenditure	17.2	16.3	15.7	15.3	14.8	14.4	14.7	13.6	13.1	12.7	12.3
Social security benefits	8.2	7.8	7.7	7.5	7.3	7.1	7.2	6.8	6.6	6.4	6.2
Personnel expenses and social contribution	3.8	3.4	3.4	3.3	3.2	3.1	3.1	2.9	2.8	2.7	2.6
Salary allowance and unemployment insurance	0.5	0.7	0.7	0.6	0.6	0.6	0.6	0.5	0.5	0.5	0.5
Salary Allowance	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Unemployment Insurance	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.3	0.3	0.3
BPC [Continuous Cash Benefit Program]	0.8	0.8	0.8	0.7	0.7	0.7	0.7	0.7	0.6	0.6	0.6
Compensation to RGPS for Exemption of Payroll Taxes	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Supplementation by the Federal Government to Fundeb	0.3	0.3	0.4	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Legislative, Judiciary, Prosecutor's Office, and Public Defender's Office	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Court Rulings and Court-Ordered Debts (current and capital expenditure)	0.2	0.2	0.2	0.2	0.2	0.2	0.4	0.2	0.2	0.2	0.2
Subsidies and Grants	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other Mandatory Spending	3.1	2.7	2.3	2.2	2.1	2.0	1.9	1.9	1.7	1.7	1.6
without Flow Control	1.5	0.5	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1
with Flow Control	1.7	2.3	2.2	2.1	2.0	1.9	1.8	1.7	1.6	1.6	1.5
Of which Bolsa Família [Family Grant]	0.3	0.9	0.9	0.8	0.7	0.7	0.7	0.6	0.6	0.5	0.5
Discretionary of the Executive Branch	1.4	1.7	1.6	1.6	1.5	1.5	1.4	1.4	1.3	1.3	1.2
Primary Balance	-0.4	0.6	0.9	1.3	1.9	2.1	1.8	2.7	3.1	3.4	3.7
Note:											
Spending on Covid-19	1.4	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0



TABLE 10. IFI FORECASTS FOR THE CENTRAL GOVERNMENT PRIMARY BALANCE - PESSIMISTIC SCENARIO (% OF GDP)

	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
Gross Revenue	22.3	22.5	21.5	21.2	21.0	20.7	20.4	20.2	20.0	19.7	19.5
Transfers to States and Municipalities by Revenue Sharing	4.1	4.5	4.3	4.2	4.1	4.1	4.0	4.0	3.9	3.8	3.8
Net Revenue	18.2	18.0	17.3	17.0	16.9	16.7	16.4	16.2	16.1	15.9	15.7
Primary Expenditure	18.6	18.5	18.1	18.2	18.2	18.3	20.7	18.7	18.6	18.7	18.6
Mandatory Expenditure	17.2	16.8	16.5	16.5	16.5	16.7	19.1	17.2	17.1	17.2	17.1
Social security benefits	8.2	8.0	8.1	8.1	8.1	8.1	9.3	8.4	8.4	8.4	8.4
Personnel expenses and social contribution	3.8	3.4	3.6	3.7	3.8	3.8	4.3	4.0	4.1	4.1	4.2
Salary allowance and unemployment insurance	0.5	0.7	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Salary Allowance	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Unemployment Insurance	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4
BPC [Continuous Cash Benefit Program]	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.7	0.7	0.7	0.7
Compensation to RGPS for Exemption of Payroll Taxes	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Supplementation by the Federal Government to Fundeb	0.3	0.3	0.4	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Legislative, Judiciary, Prosecutor's Office, and Public Defender's Office	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Court Rulings and Court-Ordered Debts (current and capital expenditure)	0.2	0.2	0.2	0.2	0.2	0.2	1.0	0.3	0.3	0.3	0.3
Subsidies and Grants	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other Mandatory Spending	3.1	3.2	2.4	2.5	2.4	2.4	2.3	2.3	2.3	2.3	2.2
without Flow Control	1.5	0.9	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1
with Flow Control	1.7	2.2	2.3	2.3	2.3	2.3	2.2	2.2	2.2	2.2	2.1
Of which Bolsa Família [Family Grant]	0.3	0.9	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Discretionary of the Executive Branch	1.4	1.6	1.7	1.7	1.6	1.6	1.6	1.5	1.5	1.5	1.5
Primary Balance	-0.4	-0.5	-0.9	-1.2	-1.3	-1.6	-4.3	-2.5	-2.6	-2.8	-2.9
Note:											
Spending on Covid-19	1.4	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Nominal GDP (R\$ billion)	8,679.5	9,753.6	10,416.3	11,142.3	11,833.4	12,559.4	13,331.4	14,153.5	15,029.0	15,954.6	16,950.1



# **IFI** forecasts

## SHORT-TERM

IFI forecasts		2022		2023			
iri forecasts	June	July	Comparison	June	July	Comparison	
GDP – real growth (% per year)	1.43	1.43	=	0.82	0.73	▼	
Nominal GDP (R\$ billion)	9,763.37	9,707.77	▼	10,464.93	10,360.76	▼	
IPCA (% in the year)	8.56	7.43	▼	4.24	4.78	<b>A</b>	
Exchange rate — end-of-period (R\$/US\$)	5.10	5.18	<b>A</b>	5.16	5.13	▼	
Employment – growth (%)	5.60	6.00	<b>A</b>	0.39	0.39	=	
Payroll – growth (%)	0.85	1.23	<b>A</b>	0.82	0.82	=	
Selic rate – end-of-period (% per year)	13.25	13.75	<b>A</b>	9.50	10.25	<b>A</b>	
Real Interest <i>ex-ante</i> (% per year)	5.68	6.06	<b>A</b>	4.49	4.83	<b>A</b>	
Public Sector Consolidated Primary Balance (% of GDP)	0.49	0.58	<b>A</b>	0.23	0.51	<b>A</b>	
of which Central Government	-0.51	-0.42	<b>A</b>	-0.27	0.01	<b>A</b>	
Net Nominal Interest (% of GDP)	6.68	5.18	▼	5.98	5.30	▼	
Nominal balance (% of GDP)	-5.94	-4.60	<b>A</b>	-5.75	-4.79	<b>A</b>	
General Government Gross Debt (% of GDP)	78.69	79.42	<b>A</b>	79.34	80.70	<b>A</b>	

## **MEDIUM-TERM**

MEDIONI TERM											
		Forecasts									
	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
GDP – real growth (% per year)	4.62	1.43	0.73	2.00	2.03	2.07	2.11	2.14	2.18	2.23	2.19
Nominal GDP (R\$ billion)	8,679	9,708	10,361	11,045	11,686	12,361	13,079	13,843	14,657	15,527	16,442
IPCA – accum. (% in the year)	10.06	7.43	4.78	3.18	3.00	3.00	3.00	3.00	3.00	3.00	3.00
Exchange rate — end-of-period (R\$/US\$)	5.58	5.18	5.13	5.18	5.21	5.25	5.29	5.32	5.36	5.40	5.44
Employment – growth (%)	4.99	6.00	0.39	0.96	0.97	0.99	1.01	1.03	1.05	1.07	1.05
Payroll – growth (%)	-2.36	1.23	0.82	2.00	2.03	2.07	2.11	2.14	2.18	2.22	2.19
Selic rate – end-of-period (% per year)	9.25	13.75	10.25	8.00	7.00	7.00	7.00	7.00	7.00	7.00	7.00
Real Interest <i>ex-ante</i> (% per year)	6.39	6.06	4.83	3.78	3.83	3.85	3.87	3.88	3.88	3.88	3.88
Public Sector Consolidated Primary Balance (% of GDP)	0.75	0.58	0.51	0.01	0.35	0.44	-0.94	0.48	0.67	0.79	0.96
of which Central Government	-0.39	-0.42	0.01	0.01	0.35	0.46	-0.98	0.50	0.70	0.82	0.99
Net Nominal Interest (% of GDP)	5.17	5.18	5.30	5.34	5.40	5.47	5.53	5.59	5.65	5.70	5.76
Nominal balance (% of GDP)	-4.42	-4.60	-4.79	-5.34	-5.05	-5.02	-6.47	-5.11	-4.98	-4.92	-4.81
General Government Gross Debt (% of GDP)	80.3	79.4	80.7	81.3	81.8	82.3	84.1	84.5	84.7	84.8	84.7



