Is there a Credit Crunch in Brazil?

By Barbara Cunha and Seynabou Sakho

The bankruptcy of Lehman Brothers triggered the contagion of the US sub-prime crisis to the rest of the world. Brazil was not spared. However it is unclear whether the crisis created a credit crunch in the country - a shortage in the credit market. To answer this question, we start by summarizing existing evidence in favor and against a credit crunch in Brazil and then move to a more formal test. Quite surprisingly, we find an excess of credit demand in Brazil (a credit crunch) during the entire period 2000 through 2008. However, during the current crisis the demand for credit dropped below the supply, refuting a credit crunch argument. The results also show a similar (albeit not as pronounced) pattern during the 2002 crisis, when credit demand dropped below supply levels. Countercyclical credit policy, implemented through public banks may explain this phenomenon.

Evidence in favor of a credit crunch

In September 2008, Lehman Brothers filed for bankruptcy. A worldwide panic in capital markets followed and the US sub-prime crisis spread to the rest of the world. Investors started pulling-out from emerging markets. Liquidity dried up as investors withdrew resources to rebalance their portfolios.

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A Blessing to Be? Statistical Carry-Over Effect on Brazilian GDP

By Jivago Ximenes

With the release of GDP growth figures for Q1 2009, Brazil is officially in a recession. GDP contracted for two quarters in a row, 3.7% in Q4 2008 and 0.8% in Q1 2009 (q-o-q). While the question of how long the recession will last is in the back of everybody’s mind, the politically hot question is whether Brazil will experience a positive or negative growth this year. In this note we argue that the answer to this question relies more on what happened last year than in what will happen in the next quarters. More precisely, this year Brazil is experiencing a negative statistical carry-over, which

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implies that positive rate of growth month to month of quarter to quarter are needed to reach zero growth. How can this be the case?

The carry-over effect is a consequence of taking composed averages between different periods and measures how the past economy growth profile influences future growth. Let us introduce a simple example to understand this tricky issue better. Consider an economy growing at about 10 percent in the first 3 quarters of year T and then, faced with a negative shock in Q4, retracting by 20 percent. In such case average GDP growth in year T is around 10 percent (actually a little bit more but let us not compound growth rates for the sake of simplicity). Suppose now GDP in year T+1 remains flat, on average it will be about 10 percent below the average growth in the past year. Because of such carry-over effect the country will face a negative growth rate of 10 percent to reach zero growth it should grow around 2.5 percent per quarter. This is the carry-over effect.

Let us now look at the case of Brazil (Figure 1). For the sake of simplicity let suppose there will be no growth at all from Q2 to Q4 2009, i.e., Brazilian GDP remains flat on its first quarter level, 2.5% below the average for 2008. Therefore, we can say that, for the whole year of 2009, GDP average will go down the very same 2.5% with respect to the previous year GDP average. Therefore, if the 2009 GDP average has to be the same as the 2008’s (which would correspond to a 0% GDP growth for 2009), the economy needs to grow considerably in the last three quarters of 2009. This is the curse of the statistical carry-over: poor performance in the past is transmitted into the future.

Considering the carry-over effect and assuming that GDP growth rates would be the same in the next three quarters, Brazil’s GDP would have to rise 1.69% in each quarter to reach zero growth in 2009. This means an average growth of 5.16% percent to counterbalance the 2.5% following Q1 and reach zero! We did the same exercise for GDP’s average growth rates in 2009 of +1% and -1% and found

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**Figure 1: Carry-over effect in GDP measuring**

![GDP Level](GDP.png)

2008’s GDP Avg

2009’s GDP Avg

2.5% difference

2008:01

2008:02

2008:03

2008:04

2009:01

2009:02

2009:03

2009:04
International experience tells us that broad fiscal reforms are often politically costly and difficult to implement. However, they might be the way for a country to raise its long term growth prospects. Brazil is not an exception. A consensus is finally emerging that the growth returns of fiscal reforms aiming at improving the taxation system, enhancing government expenditure efficiency, and creating fiscal space to increase investments, while consolidating fiscal discipline, may be very large.

These reforms are inextricably entwined with the system of fiscal federalism which, in turn, may influence the fiscal reform agenda in Brazil. First and foremost, the complexity of fiscal federalism arrangements regarding tax assignments and revenue sharing mechanisms may have led to a deterioration in the quality of the taxation system and to an excessive increase in the tax burden. Second, the improvement in the quality of public expenditures necessarily requires the enhancement of the efficiency of public expenditure management at the state and the municipal levels of government, which in turn are influenced by the system of intergovernmental transfers. Third, the consolidation of fiscal adjustment depends on the maintenance of fiscal discipline at lower levels of government, which implies the ability to transit from a culture of fiscal adjustment mandated by hierarchical controls to one encouraged by market incentives.

The first generation of fiscal federalism reforms, embedded in the 1988 Constitution, fostered the decentralization of fiscal revenues, mainly through the strengthening of the intergovernmental transfer system, and the enlargement of expenditure responsibilities to subnational governments. The second generation of reforms, in the late 1990s, focused on correcting deficiencies in laws and regulations that allowed subnationals’ fiscal laxity, unsustainable deficits, and mounting debt to threaten the stability of Brazil’s macro economy. With fiscal responsibility now entrenched and subnational deficits and debt levels under greater control, Brazil has the opportunity to implement a third generation of reforms that could enhance economic and government efficiencies, improving growth prospects both at the national and at regional levels.

The undergoing ESW entitled “Topics in Fiscal Federalism” examines the three ways by which subnational governments in Brazil finance their activities: (i) collecting taxes, (ii) receiving transfers, and (iii) borrowing; and discusses their implications on economic efficiency. In each area, the study proposes to identify progress, issues, and possibilities for change that could contribute to economic growth and development. Moreover, it discusses policy oriented issues from a fiscal federalism perspective that are part of the wider fiscal reform agenda in Brazil:

- the evaluation of tax reform options in terms of their impact on economic efficiency, overall tax burden and distribution of tax revenues among levels of government;
- the effect of intergovernmental transfers on the level and composition of expenditures by recipient units and the evaluation of new transfer mechanisms that would improve the efficiency of government expenditures; and
- the necessary conditions for the transition from the fiscal discipline induced by legislation and administrative devices to a market-based fiscal discipline that would guarantee the maintenance of fiscal responsibility at all levels of government.

More precisely, the introductory chapter provides background information on recent developments in the Brazilian federative system and defines the major issues for a reform agenda. Chapter 2 describes the evolution and structure of the taxation system in Brazil and assesses its impact on the efficiency and competitiveness of the Brazilian economy, concluding that reform is urgently needed. Following a discussion on the political economy of tax reform and international best practices, the ESW analyzes two comprehensive tax proposals before Congress. It

“A consensus is finally emerging in Brazil that the growth returns of fiscal reforms may be very large”
Awaiting for the Next Generation…

concludes that both proposals are very worthwhile and provide some advice on how to improve their chances of success.

Chapter 3 describes the evolution of fiscal transfers in Brazil and compares Brazil’s distribution and composition of fiscal revenues with those of other federal countries. It then assesses the performance of the major categories of intergovernmental transfers. It shows how the design of fiscal transfers has often created incentives that have led to perverse outcomes, but concludes that the recent tax reform proposals, with small modifications, could address most of the critical bulk of issues related to intergovernmental transfers.

Chapter 4 reviews the role subnational government debt played in Brazil’s macroeconomic instability prior to the introduction of hierarchical controls. It concludes that the hierarchical controls that restricted borrowing have served Brazil well, but it may be time to build upon them by allowing creditworthy states to borrow in capital markets under certain conditions. Drawing upon international experience in subnational debt markets, it outlines a specific proposal to allow a gradual and orderly transition to subnational debt markets.

Statistical Carry-Over… (Continued from page 2)

respectively 2.35% and 1.02% as the necessary growth rates in each of the next three quarters. These results can be seen in Figure 2.

The key message of this short note is that the annual GDP growth value is calculated from the variation of the sum of goods and services produced in a year against the sum of goods and services produced in the previous year. Since we are comparing averages, the starting point matters a lot. Indeed, in the case of Brazil, even if the Brazilian economy posts positive growth rates in the next quarters, the lower point of departure recorded in Q1 2009 could yield a smaller (average) annual production than the previous year. Of course, in a period of fast growth at the end of a year the statistical carry-over becomes positive. This means that what has been a curse (for politicians) in 2009 can become a blessing in 2010.

Figure 2: Necessary Brazilian GDP growth rates in coming three quarters

“What has been a curse in 2009 can become a blessing in 2010”
The Earlier the Better

By David Evans

Global Conference on Early Child Development presents innovative models and worldwide evidence

A recent interview with Economics Nobel Prize winner James Heckman * and an article by World Bank Vice President Pamela Cox ** have highlighted the importance of early child development (ECD) for Brazil. Despite evidence that high-quality early child interventions have the highest and longest-term payoffs, only 40% of Brazil’s children participate in early child education programs.

To call attention to this issue, the World Bank, Brazil’s Ministry of Education and the Municipality of Rio de Janeiro sponsored the “Global Conference on Early Child Development: Innovative Models and Global Evidence,” in Rio de Janeiro, in June. Brazil’s Government highlighted its commitment to this issue with the presence of the Minister of Education, the Minister of Health, and – representing the municipality of Rio de Janeiro – Education Secretary Cláudia Costin. The World Bank was similarly well represented with the presence of Country Director Makhtar Diop, LCR HD Director Evangeline Xavier and Elizabeth King, Education Sector Director.

Experts from different countries presented the impact of daycare and preschool programs promoting educational success. Steven Barnett, Co-Director of the National Institute for Early Education Research, displayed the array of evidence on the long-term impacts of early child interventions both from the United States and globally. Evidence from reliable studies indicates that children who participate in ECD programs do better in education, employment, in staying away from crime, and in an array of other outcomes. Fraser Mustard, a doctor and ECD researcher at the Founder’s Network, explained the science of early child development and the long-term cognitive impacts of early intervention.

The conference was attended by policymakers from all of Brazil as well as from Chile, Colombia, the Dominican Republic, Mexico, Jamaica, St. Lucia, and Sweden. Several of these policymakers explained the variety of early child development programs being implemented. Arturo Saenz, Director General of the Mexican National Council of Education Promotion (Conafe), shared the work being done through a low-cost community daycare program. Maureen Samms-Vaughan, Chairman of the Early Childhood Commission of Jamaica, discussed Jamaica’s national ECD policy and its implications for ECD center standards.

Furthermore, Brazilian researchers highlighted findings from the local context. Ricardo Paes de Barros, a researcher at the Institute of Applied Economic Research (IPEA), showed that traditional preschools and crèches have had measured impacts on outcomes for the adults of today. However, an exciting experimental study of crèches in Rio has already shown significant reductions in maternal stress, with findings on children’s cognitive development coming soon.

Donor partners, private foundations, and Brazilian policymakers at all levels of government (federal, state, and municipal) shared their current work, and the conference has initiated the launch of a Bank-sponsored Community of Practice, where ECD policymakers from around Latin America can share lessons through videoconferences, cooperative missions, and data exchanges. The conference also kicked off a major analytical program to fill key knowledge gaps about ECD in Brazil, sponsored by Brazil’s World Bank country management unit.

“The Earlier the Better

The materials presented by international specialist at the ECD Conference are available at www.bancomundial.org.br

* Published by Brazilian magazine “Veja” on June 10, 2009.

** Published by Brazilian newspaper “O Globo” on June 20, 2009.
Credit Crunch... (Continued from page 1)

answering margin calls, and flying for safety in the wake of new heights of risk aversion.

Brazil was not spared. Following Lehman, the overall volume of credit operations to the private sector in the financial system, (see Figure 1) decreased sharply. Such a behavior is consistent with a credit crunch story defined here as an excess demand of credit at the prevailing rates.

Capital market dynamics may support a similar story. Indeed, from September 2008 to March 2009, no IPOs took place in the market. Only public enterprises and governments were able to raise money in foreign capital markets. This suggests a sharp decline in the supply of credit in international markets for the private sector. Though domestic markets remained active during this period, the volume of operations to

Figure 1: Credit to the private sector slowed down (% change, y-o-y)

private firms was far below the average in the previous years (see Figure 2).

The impact of the crisis on the banking credit was less pronounced but still consistent with a credit crunch story. The overall credit balance and in particular the balance on operations in the private sector continued expanding during 2008, while net credit flows fell significantly after November 2008, becoming slightly negative in the beginning of 2009.

Figure 2: Equity, bonds and syndicated loans

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Haddad: Education is a High Yield Investment

By Mauro Azeredo

Minister Fernando Haddad, 46, is one of the most charismatic and dynamic members of President Lula’s cabinet. Since his nomination in 2005, he has instituted or helped strengthen important reforms and programs, such as the Basic Education Fund and the ProUni university scholarship program for low income and marginalized groups. At one point he was considered as a possible option for President Lula’s succession. Haddad has a PhD in Philosophy from the University of S. Paulo. His thesis was “From Marx to Habermas – Historical Materialism and its Adequate Paradigm.” Mauro Azeredo of the Brazil Economic Team interviewed him about the crisis, education and the relationship with the Bank during the recent Early Childhood Development global forum promoted by the Bank in Rio. Following are the highlights of the interview:

BET: What is the role of education in the context of the international financial crisis?

FH: The high return on education investments has been proved and highlighted numerous times in Brazil. It may be among the biggest in the world. So investments in the sector in Brazil have guaranteed returns. The other day I was surprised by a study of the Fundação Getúlio Vargas in the area of adult literacy. It was long thought that this type of work responded more to citizenship and inclusion demands than to development needs. But FGV discovered that an adult who becomes literate increases his or her income by about 20 percent. Thus, education results are so important in Brazil that a forty-year-old person who learns to read not only gets to participate more actively in the country’s social and political life, but also gets a significant boost in his or her material well being. From this example it is possible to see how education can help during the crisis. Investments in this area are the most effective, considering the internal rate of return.

BET: What are Brazil’s main education challenges?

FH: The ministry’s agenda focuses on four priority areas: early childhood education, secondary education, teacher development and scientific production and innovation. In all, I would say it is a good agenda for the next ten years.

BET: And in the secondary education area?

FH: We have extended all the benefits of the Fundef into Fundeb, and thus they are now available for secondary schools. Also, the Ministry made all the support programs previously restricted to fundamental education, such as transport, textbooks, school meals and direct cash transfers to schools, available for this important segment.

There are also many initiatives in the fundamental link to the university level. We are now introducing an innovative university admission mechanism, to substitute the traditional all-or-nothing entry test. The new instrument is a mix of the American SAT and the French BAC. It is an interesting innovation, and many universities have already begun using it. Finally, vocational education programs in the secondary level are being substantively strengthened, in coordination with existing schools and other partners.

BET: You mentioned teacher development as a third challenge of the country.

FH: Yes, the adoption of a national policy for teacher development and capacitation, with strong participation from the Federal government, is a difficult
challenge. We have launched the first national teacher development plan, which guarantees a university education for all public school teachers in activity, so that they may achieve their first diploma or continue their education. In parallel, we are doubling the number of public 2-year teaching courses in the country, so that students from private universities do not have to pay for the initial teaching course.

On the quality side, we are also filtering those who apply for teaching positions by requesting a minimum score in the national Secondary Teachers Test and also passing a specific exam to become a teacher.

**BET: What is the role of the Ministry of Education in the science and innovation agenda?**

**FH:** Brazil has already been experiencing a strong growth in scientific production, from a global perspective. The country ranks 13th in the world in number of published papers in indexed journals. But the challenge is to advance in translating this knowledge into applied technology. That is, increase labor productivity, add value to our production and exports. The Ministry is working with other ministries and partners in this fundamental agenda.

**BET: What is the role of the World Bank and other international organizations in supporting Brazil’s education agenda?**

**FH:** We have a long lasting partnership with the Bank, and also a permanent dialogue with the institution. I feel that, increasingly, international organizations in general and the World Bank in particular can and should disseminate good practices and innovation around the globe.

So, we welcome the global inputs and knowledge that the Bank is bringing to Brazil, but also its role in taking our experience to where it can be useful – Latin America, Africa, Asia. I encourage international organizations to work harder at this dissemination and also to establish a more intensive multilateral cooperation in the sector. For example, the poorest countries will be hard pressed to reach the Millennium Development Goals or the Dakar Goals without support from developing and developed countries. I can imagine an important role for the Bank and other institutions in doing this triangulation.

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**Credit Crunch…** (Continued from page 6)

It is plausible that part of the firms that were not able to raise resources in capital markets looked to banks as an alternative source of financing. In this case, the credit expansion observed in 2008 might not have been sufficient to meet this additional demand, leaving some players (possibly the smallest ones) out of the market.

**Evidence against a credit crunch**

If we found some evidence in favor of a credit crunch, the evidence hinting in the opposite direction is quite strong. Indeed, an important consideration left aside in the previous analysis of the credit supply is the fact that the credit market in Brazil is characterized by a relatively small participation of direct foreign financing.

In addition, as the crisis unfolded, public banks drastically increased their lending. As shown in **Figure 3**, the decrease in credit supply

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The First Conference of the Brazilian Network of Monitoring and Evaluation was held in Belo Horizonte, Minas Gerais on June 25th and 26th, and brought together over 220 professionals interested in monitoring and evaluation from the federal and state governments, universities, private foundations and think tanks.

The conference, hailed as a success by the audience, provided expert participants an opportunity to learn about other state of the art evaluations taking place in Brazil and also provided an opportunity for some state governments who were new to monitoring and evaluation to learn about setting up initial monitoring and evaluation plans for individual programs and for overall government programs.

The high level of participation in this conference followed a similarly high level of Brazilian participation in the 4th Annual Conference of the Latin American Network of Monitoring and Evaluation which was held in Minas Gerais in November, 2008. On the occasion, many of the Brazilian institutions and individuals attending the conference met informally and decided to create a Brazilian Chapter of the Network and to hold a conference.

The Fundação João Pinheiro of the Government of Minas Gerais took on the major responsibility of organizing the first conference, with support from FAPEMIG (Fundação de Amparo à Pesquisa do Estado de Minas Gerais), FUNDEP, (Fundação de Desenvolvimento de Pesquisa), and the World Bank

“Evaluation as an instrument to achieve better effectiveness of social policy: current status and challenges for the next decade” was the theme of the keynote speech at the conference delivered by Ricardo Paes de Barros from IPEA, the Brazilian Institute for Applied Economic Research. The subsequent presentations were organized around the following topics:

- Diagnosis and Monitoring of Social Problems
- Use of Ex-Ante Evaluation for the Identification and Design of Social Programs
- The use of Logical Frameworks and the Design of Evaluations of Social Programs
- Process Evaluation and Program Implementation
- Ex Post Evaluation

A second organizing session for the Brazilian Network was held at the end of the first day of the conference and agreement was reached to hold the second conference in either Fortaleza or São Paulo. Plans were made to create a web site for the network, post the Conference papers on the web site and arrange for publication of the papers. There was also discussion of the possibility of holding more intensive 2 to 3 day courses or exchanges around the specific topics listed above. These plans will be discussed by a small steering committee consisting of the Fundação João Pinheiro, SEADE of the Government of São Paulo, the Banco do Nordeste, the Agência Brasileira de Avaliação and the World Bank.

“State governments learned about setting up monitoring and evaluation plans for individual programs and for overall government programs”
Credit Crunch... (Continued from page 8)

from private and foreign banks and from international capital market was offset by increased lending from public banks.

The analysis so far did not consider changes in the demand for credit along with the changes in the supply.

Confidence and financial market strains from the global economy affected investment and consumption and thus the demand for credit, indicators of investment along with expectations about the economy declined. In the fourth quarter of 2008, firms drastically slashed production and decreased the imports of capital goods, indicating lower investment expectations for the future (see Figure 4).

**Figure 4: Investment indicators**

As such, one may argue that credit demand may have dropped in the face of expectation of weak domestic and external demand. While the evidence supporting a credit crunch in Brazil in the aftermath of Lehman is weak, it is difficult to reject it out without a more rigorous analysis. This is what we do in the next section where we test whether in Brazil the decline in the willingness to borrow was smaller or greater than the decline in the supply of credit.

**A Disequilibrium Model of Credit Crunch**

In order to empirically verify the existence of a credit crunch we have estimated a “disequilibrium” model for Brazilian credit markets. The model allows for a mismatch between quantity of credit supplied and quantity demanded, that is, for the existence of shortages and surpluses in the credit market. This implies that in the presence of rigidities, the competitive equilibrium interest rate cannot clear the credit market and the observed credit is determined by the minimum of credit demanded and credit supplied.

In the model, credit demand is expected to depend negatively on nominal lending rate, positively on expected inflation rate (i.e., higher expected inflation will decrease the burden of debt), positively on expected growth of production or expected investment (e.g., firms take future credit rationing into consideration), positively on lagged GDP (only after accumulating certain wealth, firms can access new credit lines).

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CONSAĐ: Strengthening the Public Management Agenda

By Evelyn Levy

As mentioned by Abrúcio & Gaetani (2006), perhaps the greatest challenge to improve Public Management is to build a coalition supporting the issue.

CONSAĐ conferences, organized by CONSAĐ in association with the World Bank and the IDB, are becoming an important tool for generating knowledge and learning processes; for exchange and networking between high ranks, middle management, academics and consultants and to build the political coalition in its support. As a consequence, during the 2008 conference, the Ministry of Planning and CONSAĐ state secretaries signed the "Carta de Brasília" on which they agree on several points conducive to Public Management improvement. Furthermore, in 2009, Public Management became one of the five long standing objectives of the Strategic Issues Secretariat, led by former Minister Mangabeira Unger.

This year's conference, held in May, in Brasilia, had two keynote speakers: Michael Barzelay, from the London School of Economics, who spoke on "Public Management and Control," and José Álvaro Moisés, from the University of São Paulo, who spoke on "Mistrust of Citizens and the Political Institutions in Brazil". The WB sponsored two of the four keynote speakers: Deborah Wetzel spoke on "Public Management and the Financial Crisis", and Barbara Nunberg compared the "Latin American and Asian Challenges in Public Management."

Over 400 papers were submitted by authors from all Brazilian states, from all levels of government, the Judiciary and the Legislative and universities. Papers and panels presented fit well under the headings created by Manning et al. (2008) as the five dimensions of Public Management Reform:

1. Public expenditure management and financial accountability:
   The majority of the panels can be classified in this group, covering a wide number of issues, from strategic planning to performance budgeting, results based management, procurement and cost management. Issues relating to internal and external audit were introduced this year, becoming a novelty if compared to last year.

2. Human resource management
   New issues treated this year relate to workforce planning and social dialogue, whereas the debate on meritocracy and responsiveness highlighted more mature solutions.

3. The structure of the public sector
   Intergovernmental issues, related to state-municipal relations, inter-municipal relations (consortia and metropolitan governance) were also present this year. Papers on regulatory agencies were also presented.

4. Alternative service delivery
   A significant number of the papers and panels were concentrated under this broad heading, within it sector initiatives (education, health, environment, culture, policing, prisons, social development) to improve management.

5. Demand-side reforms
   This group encompassed e-government initiatives as well as participatory planning and citizen participation.

Considering the assessment made by Manning et al. (2008) on public management reform patterns in Latin America, the conference indicated:

- that performance budgeting is starting to be discussed, but there is very little evidence of its implementation in Brazil;
- that procurement has been a constant preoccupation in Brazilian governments and that success is being achieved;
- that no progress has really been done on accrual accounting; and, agreeing with Abrucio & Gaetani (2006), there is a lack of integration of public management policies;
- that audit institutions are starting to participate in the debate and adjusting their agendas to involve citizens in social control and to look more on results;
- that the management of regulatory agencies starts to become an issue of concern although no centralized regulatory approach is being discussed;

"Perhaps the greatest challenge to improve Public Management is to build a coalition supporting the issue"
**Credit Crunch...** (Continued from page 10)

Credit supply is determined by a portfolio management approach and is expected to depend positively on lending rates and the banks' capacity to lend (e.g., total deposits plus banks' equity, banking sector's share price index). Other explanatory variables include: market capitalization of corporate equity (e.g., net worth of corporations or the collateral worth), the difference between the lending rate and the money market rate (as a proxy for the risk premium), expected inflation rate and expected industrial production.

The results of our analysis are summarized in Figure 5 and Figure 6 and, quite surprisingly, they indicate an excess of credit demand in Brazil (a credit crunch) during the entire period 2000 through 2008. However, during the current crisis the demand for credit dropped below the supply (no credit crunch). The results also show a similar (albeit not as pronounced) pattern

**Figure 5: Credit supply and demand**

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Brazil and the Crisis: The Beginning of the End or …

By Tito Cordella

Much has been said about how long the global financial crisis will last. The only common denominator so far is that there is no conclusive agreement. It is no coincidence that the workshop on "Trade and Finance: the Challenges of the World Crisis" (Comércio e Finanças: os Desafios da Crise Mundial) shared different and yet complementing views of the same issue. The event, held on June 2, in Rio de Janeiro, was co-sponsored by the World Bank and CEM “Centro de Economia Mundial” of the Fundação Getúlio Vargas (FGV).

Under the theme "Financial Challenges", the first panel focused on whether the worst of the financial crisis is over. According to the Director of CEM and former Brazil Central Bank President, Carlos Langoni, who chaired the panel, the worst has indeed passed and from now on leaders must think about post-crisis measures.

UCLA’s economist Sebastian Edwards, instead, believes we will see a few false lights (“dawns”) before seeing the light at the end of the tunnel. He also showed skepticism toward the effectiveness of the US stimulus package in jump starting the world economy because of the macroeconomic imbalances it is creating.

Eduardo Levy-Yeyati, Director and Head of Emerging Markets Strategy at Barclays Capital, in turn, said the world is already in a post-financial crisis mood. However, the convalescence will be painful and the global economy recovery will be slow, because global lenders might become more cautious in financing the US economy.

UBS Chief Economist for Latin American Eduardo Loyo stressed that the current situation is difficult to assess as the signals we are receiving are mixed. He also pointed out that the crisis is fostering a process of international convergence in which G7 countries look more like emerging economies and emerging economies more like G7 countries.

The topic of discussion for the second panel, which was chaired by the World Bank Senior Advisor and former PREM Vice President Danny Leipziger, centered on the trade Challenges.

World Bank Director Bernard Hoekman highlighted that while global trade flows fell significantly as a result of the crisis, trade in services continued to growth. On the policy response, he warned against the resurgence of protectionist pressures. However, in his view, the fact that countries are playing according to the rules of the game, using the WTO litigation system, is encouraging, and remarked that a successful conclusion of the Doha round would produce a much needed boost in confidence.

Gary Clyde Hufbauer, senior fellow at the Peterson Institute for International Economics, stressed that while the trade picture is grim, the protectionist measures undertaken since the crisis started have been large in number but pretty small in impact. Besides, the great majority of them seems consistent with countries’ WTO obligations.

Finally, Brazil Country Director Makhtar Diop closed the workshop, stressing the importance of this sort of events in which the World Bank partners with local institutions to present new research or just discuss highly relevant and controversial policy issues.

“The crisis is fostering a process of international convergence in which G7 countries look more like emerging economies and emerging economies more like G7 countries”
Credit Crunch… (Continued from page 10)

during the 2002 crisis when demand for credit dropped to almost meet the supply of credit.

It is also worthwhile to notice the sharp acceleration in the supply of credit before the 2008 crisis. The volume of credit operations increased more 25.8% between March 2008 and October 2008 and remained stable after October. The crisis had only a minor effect in the supply path, most of the movements in credit markets seem to be driven by the sharp fall on credit demand.

Summarizing our findings, Brazil appears to be a sort of an outlier with credit becoming less rationed during the crisis periods. One reason might be its ability to channel resources through public banks to prop up credit supply and for that very reason overcome the credit rationing characterizing normal times. Contrary to other countries, credit rationing eases up in crisis times whereas in normal times, when credit markets do not clear at the prevailing rates.

“Brazil seems to be an outlier, with credit becoming less rationed during the crisis periods”

Figure 6: Excess credit demand and the crises
In the Loop

Some of the quarter’s noteworthy events

Cost Benefit Analysis, Porto Alegre (Rio Grande do Sul), May 20 to 22

The Bank and the State Secretariat of Planning and Management of RGS sponsored a three-day training course on Cost Benefit Analysis for public infrastructure projects, which was carried out by Edgardo Mimica (University Adolfo Ibañez, Santiago de Chile). The course was delivered in four parts. The first consisted in a review of capital budgeting systems with emphasis on the Chilean model under the National System of Investment and governance issues regulating the decision making process. The second part described the different phases of the project design and implementation from the project profile, prefeasibility and feasibility assessments, financial and economic analysis. The third part consisted in a theoretical a session introducing the most important concepts of Cost Benefit Analysis (cash flows, net present value, benefit-cost ratio, internal rate of return, optimal scale, etc). The fourth session was a hands-on exercise to apply the concepts and methods learning in the previous sessions.

Subnational Debt Management, Porto Alegre, June 15 to 19

As part of the technical assistance activities under the supervision of the Rio Grande do Sul (RGS) Fiscal Sustainability for Growth DPL, the Bank and the state Secretariat of Finance of RGS organized a one week training course on the design and implementation of debt management strategies for subnational governments. The preparation of the material and the delivery of the workshop were carried out jointly by LCSPE, GCMSM (Global Capital Markets Development Department), and BDM (Banking and Debt Management Group). The course contained three main parts: financial mathematics fundamentals and the basic functioning of the financial system in Brazil; theoretical concepts behind the development of a strategy for managing government debt, and execution of liability management and funding strategies.

Project Management, Maceió (Alagoas), July 13 to 15

As part of the preparation activities for the Alagoas: Fiscal and Public Sector Reforms DPL, the Bank organized a three-day training course on project management for Alagoas state officers. The selection of a portfolio of priority projects for a better prioritization of government resources and their intensive management is one of the reform areas supported by the DPL. The workshop was carried out by the Institute of Managerial Development, which has been providing advisory services on improving the efficiency of governmental processes to the states of Minas Gerais, Rio Grande do Sul, and the Municipality of Rio de Janeiro, among others.
New Knowledge… (continued from page 1)

As the global financial crisis continues to take its toll, we analyze the impact of the global economic downturn in Brazil, and how the largest economy in Latin America was able to weather the storm effectively. On this launch edition, Barbara Cunha and Seynabou Sakho address the critical question of whether there is evidence of a credit crunch in Brazil in 2008-09. Jivago Ximenes drives us into the intricacies of statistical carry-over and explains why Brazil should show positive growth rates to be able to reach zero growth this year.

The front line of development in Brazil is increasingly shifting from the Federal government to the states, where a new generation of governors has innovative programs and a focus on results. Pursuing customized knowledge solutions for our partners, Fernando Blanco elucidates a pressing issue for Brazilian subnational governments to tackle: the next generation of fiscal reforms.

Cost efficiency is a cross-cutting issue that also informs the debate on education policies in Brazil. As a recent WB report warned regional policy makers, Early Childhood Development (ECD) programs provide a cost-effective way to reduce poverty and inequality in the region in the medium and long-term. To call attention to this issue, the World Bank, the Brazilian Ministry of Education and the Municipality of Rio de Janeiro sponsored the Global Conference on Early Child Development: Innovative Models and Global Evidence. David Evans brings us the highlights of the conference, while Mauro Azeredo shares an exclusive interview with Brazilian Education Minister Fernando Haddad. Enjoy your reading!

Makhtar Diop
Brazil Country Director

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Brazil Quarterly, Monthly, Daily – What are They?

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From Monday to Friday, our team selects the most important news about Brazilian economy on the leading national and international newspapers, and prepares a unique report on major economic indicators, data and surveys. We believe the "BET Daily Report" can provide you a concise and useful update on the Brazilian economy.

The BET team also produces:

The "Brazil Monthly Report", which provides updated information on economic developments, policy challenges, and keeps you ahead of the economic trends.

The "Quarterly Knowledge Report" which aims to bring you to speed on our analytical work (conferences, AAA, etc.), and offers short knowledge pieces on policy relevant questions.

If you do not receive these materials yet, just send us an email at betmail@worldbank.org. Your suggestions and feedback will also be very welcome.

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