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CAMPINAS SCHOOL OF POLITICAL ECONOMY

Selected Works on Brazilian Economy

Campinas School of Political Economy Book Series
Volume 2

Editora CRV
Instituto de Economia
UNICAMP

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FOREWORD

The Institute of Economics at the University of Campinas (Unicamp) is pleased to present to the international community the two volumes of "Campinas School of Political Economy", a careful selection of key translated manuscripts that contributed to the formation of our intellectual history over time.

The Institute was born in the late 1960s as the Department of Economic and Social Planning of the Institute of Philosophy and Human Sciences of the recently established University of Campinas at that time. Since its beginning, the Institute of Economics has represented an intellectual project rather than only an academic body. The departing point was the original perspective of the Latin American Structuralist School, which emerged in the late 1940s with the seminal work of Raúl Prebisch and represented an authentic and autonomous way of thinking about development in this region of the globe – an early preview of the current "decolonizing economics" trends. Two decades later, a group of young economists brought together in an infant university during the worst phase of the civil-military dictatorship in Brazil followed the same path, but adding novelties and criticisms to the ECLAC's approach.

Trying to understand the specificities of the origins and the development of capitalism in Brazil, those collective discussions were able to mobilize different theoretical inputs and tools, always with creativity, accuracy and independence. The result was an original interpretation, which throughout the following five decades was updated, renewed and transformed not only by the changes and challenges of the Brazilian economy but also by the evolution of both the international economy and the economic thinking in Brazil and worldwide.

For a long time, most of these contributions were written and published only in Portuguese, which is frequently a problem both for international students attending courses in Campinas and for the outward circulation of these ideas. Long awaited, these two volumes have tried to capture, organize and translate some of the most important chapters of what sometimes is referred to as "Campinas School". Each of the two volumes - whose division is thematic and follows a chronological sequence - has its own presentation and contextualization of choices. The list of manuscripts is neither exhaustive nor consensual, but the effort is, at least, a first step in spreading such key ideas.

Institutionally, we would like to thank all people involved in this project of translating original texts. Professors Alex Wilhans Antonio Palludeto and Mariano Francisco Laplane are the editors of the first volume, dedicated to contributions to theoretical and international topics. The second volume, whose texts focus on the formation and contemporary Brazilian economy, is organized by professors Pedro Paulo Zahluth Bastos and Denis Maracci Gimenez. Professor Roberto Alexandre Zanchetta Borghi assumed a fundamental organizing task at a later stage of the project, and professor Rosangela Ballini was also essential all the time. Professors Célio Hiratuka and Carolina Troncoso Baltar also made important contributions to this project. Our assistants Geisa Aguiari, Francisco Orlandini and Greisiane da Silva also played a fundamental role in different steps of the process. Finally, we thank all the authors of the texts for their collaboration.

More than an important step on the unavoidable path of academic internationalization, these books are an institutional invitation to the dialogue, collaboration, and "cross-fertilization" of ideas with other theoretical and empirical perspectives as well as researchers around the world.

Enjoy the books!

André Biancarelli
Director of the Institute of Economics - Unicamp
Campinas, Brazil, September 2022

INTRODUCTION

Pedro Paulo Zahluth Bastos
Denis Maracci

The book the reader has in hand is a collection of classic texts and more recent reflections from the Institute of Economics of the University of Campinas academic body. Slightly modifying Niklas Luhmann's (1982, p. 4) definition, a classic survives as a challenge or a guide because the way it poses problems serves to address other issues in the future, albeit with the necessary adaptations. The historical context in which a classic was written is relevant to understanding the problem it raises and marking its difference with the contexts of adaptation of the problem for the analysis of new concrete situations. On the other hand, it is the general theory or, in other cases, the analytical scheme that is relevant to new research and generations, in dialogue with new approaches, methods, and information arising since the origin of the classic. Hence, the classic text typically unfolds in new specialized branches of investigation that advance in traditional or innovative directions. In this sense, the survival of the problem and not necessarily of the specific answers defines the vitality and actuality of a body of classic texts.

What is the problem that characterized the origin of Unicamp's Institute of Economics? The characteristics of the origin, structural changes, and dynamics of capitalism in Brazil were the object of the first theses defended, in 1975, by the then Department of Economics and Economic Planning (Depe-Unicamp), created in 1968. As we will see, the proposed hypotheses required investigating the development of capitalism from its origins to understand the Latin American and Brazilian particularity in the world capitalist totality. Furthermore, the concern with contextualization and historical difference implied the effort to *historicize* theoretical concepts to reconstitute and explain specific contexts and processes rather than "applying" theories in particular case studies to "test" general hypotheses. This methodological characteristic is, in fact, one of the reasons why the school is currently a living tradition that still investigates structural changes and capitalist dynamics in Brazil and the world.

Such a preoccupation with history cannot mask the analytical and political preoccupation with the future. The Campinas School was created in the field of Critical Theory and not in the area of Problem-Solving Theory, to use Robert Cox's classic distinction (1996[1981], p. 88-90). On the one hand, Problem Solving Theory assumes social and political relations, and their institutions, as parameters of the problem identification and decision-making process in each area of academic specialization. On the other, Critical Theory asks about how such relations and institutions arose, who they serve, and how they can be changed in the name of emancipation. Therefore, it is concerned with the complex totality of relationships and not just with abstract parts. It sees the totality in the process of constitution and change, historicizing concepts in search of the potentialities for the future inscribed in the process of development of its object. At best, it is neither conservative nor utopian, rejecting both the conservation of order and implausible alternatives. In this case, the Campinas School was born with intellectuals committed to fighting for the redemocratization of the Brazilian State, reforming capitalism from the left, and debating with technocratic developmental economists and the Chicago-Boys who supported the military dictatorship instituted in 1964.

The first text of the collection is the introduction of the first doctoral thesis defended at DEPE in 1975, *O Capitalism Tardio [The Late Capitalism],* by João Manuel Cardoso de Mello. As the selected text is a small part of a large book, more space will be devoted to its presentation than to the following ones (generally full texts), which is also opportune to present the fundamental problem of the Campinas School. The controversial character of the introduction of *The Late capitalism* is mainly directed against the interpretation of the UN's Economic Commission for Latin America and the Caribbean (ECLAC) on the Central-Periphery System and the problems it poses for peripheral industrialization and overcoming underdevelopment. It is noteworthy that, like the other authors of the first generation of the Institute of Economics, Cardoso de Mello operates in the theoretical space opened up by ECLAC thought, to which he makes an "external" critique. A critique that questions the survival of neoclassical assumptions incoherent with the ECLAC thought, which is also censored because methodological nationalism would cover up the division of social classes.

The problem with the analyzes of Raul Prebisch and Celso Furtado was that they did not understand peripheral industrialization, and its difficulties, as a process associated with the development of capitalism in late historical conditions originating from pre-capitalist formations characterized by dependence, by the dominance of commercial capital, and, in the Brazilian case, slavery. Instead, industrialization was understood as a technical issue, not a political economy question. The solution to the technical problem, in turn, depended on an abstract conception of the State and, implicitly, on the belief in the adherence of the Latin American bourgeoisie to the technically proposed solutions. The technical problem would be the contradiction between imported, capital-intensive techniques and the endowment of local, capital-intensive, and labor-intensive "factors of production." The solution would be to limit the consumption of the bourgeoisie to generate the necessary savings and increase workers' wages through agrarian/urban reform and income policies to expand the market required by scale-intensive industrial techniques. The assumption was that capitalist industry served the *final consumption needs of* the population in the developed Core (the industrialized countries) rather than being a means of accumulating more capital by capital and producing the industrial reserve army necessary for that purpose without commitment to the well-being of the population.

In the proposed critical theory, Karl Marx's influence is explicit: industrialization consolidates capitalism through the "real subsumption" of labor to capital, largely dispensing with the extra-economic coercion of direct producers that had characterized the formal emergence of capitalism in the colonies of Latin America. Capitalism in the colonies, yes, because slavery is understood as the invasion of commercial capital into the terrain of production, formally subordinating compulsory labor with much more violence than the putting-out system and the manufacture at the time of the primitive accumulation of capital that gives meaning to the colonial economy: "...there is, formally, capitalism because slavery is slavery introduced by capital", in the words of Mello (1998 [1975], p. 43).

The similarity with the reflections of Jairus Banaji (1973) on India is striking. Still, the inspiration comes from three Brazilian Marxist historians and social scientists, Caio Prado Junior (2011[1942]), Maria Sylvia Carvalho Franco (1969[1964]), and Fernando Novais (1987[1968]). Inspired by Prado Jr., Andre Gunder Frank (2012[1964]) published a study on Brazilian agriculture while visiting the country, denying its feudal character, and defending its capitalist nature since colonization. Frank, however, is criticized by Mello as a mere radicalization of the ECLAC approach, which predicts the unfeasibility of the development of capitalism in Latin America. On the contrary, such development can occur without industrialization meeting the needs of the popular masses, producing a dynamic and exclusionary, unequal and combined model of capitalism, as Maria da Conceição Tavares and José Serra (1982[1970]) wrote in a text that anticipated the theoretical problematic of the Campinas School, but not its historical scope (Bastos, 2021). For heavy capitalist industrialization, what is fundamental is not the consumption of workers, but the overcoming of the requirements of financial centralization, technological control, and scales of inter-industry markets that can, as in Michal Kalecki, rely on investment and consumption by the capitalists themselves with state support.

Under the conditions of late capitalism, however, the state's and foreign capital's participation must be much more important than in earlier patterns of industrialization. This is because of capitalism's uneven and combined development on a world scale, as Barbosa de Oliveira (2003[1985]) would study later in detail. After all, competition with capitalisms that have followed the tendency of concentration and centralization of capital for a longer time and have surpassed the threshold of monopoly capitalism makes linearity and gradualism in late capitalisms unachievable, requiring a leap of stages. The ECLAC project of *national* capitalist industrialization that meets *popular needs* is an unrealizable utopia in Latin America, given the historical context in which it takes place, which cannot be reduced to the contradiction between "capitalistic" techniques and the labor-intensive endowment of factors.

The conception of uneven and combined development also distinguishes Mello from Wallerstein (1974), who, through Frank, is so close to the Brazilian Marxist reflection of Prado Jr. In the Campinas School, inspired by Cardoso & Faletto (1984[1970]), greater importance is given to internal determinants than in Wallerstein's hyper-structuralism, without, however, neglecting dependence. After all, the fate of each peripheral region or, for example, of the different capitalist models in Latin America is *ultimately conditioned* by the structural changes of capitalism worldwide. However, *in the first instance,* the struggle of local classes and fractions of classes, and the dynamics of capital accumulation in the local space, are essential to determine the conditions in which each region is inserted in the different phases of world capitalism, and in particular if the structural break or the *leap of stages* represented by heavy industrialization can occur, and how.

In the Brazilian case, capitalism in the strict sense – a mode of production based on the exploitation of a massive wage labor market – would have spread in the coffee plantations of the São Paulo plateau at the end of the 19th century, creating the necessary scale for the advancement of large-scale industry. Initially focused on light branches that served the coffee complex, such as textiles, clothing, food, beverages, and agricultural implements, as Silva (1976[1973]) defended and Cano (1990[1975]) would deepen in a thesis defended months after Mello. After all, for Cano, the low agricultural productivity, and the consumption pattern of enslaved people before the São Paulo coffee complex did not prevent the development of the internal market, urbanization, and the emergence of the transformation industry. Still, these factors structurally limited them much more than the capitalist coffee plantations did.

The structure and dynamics of the accumulation scheme between 1884 and 1930 are discussed in the chapter by Mello and Tavares (1984), whose examination is appropriate with the analysis of late capitalism. Tavares (1998[1975]) would defend an associate professor thesis shortly after Mello´s Ph.D. thesis, extending the discussion of industrialization to the period 1932-1962. Therefore, the joint chapter deals with the period covered by both theses. Regarding the period 1884-1930, for the authors, the critical point is that the primary conditions for industrialization (labor force, monetized domestic market, and available money capital) were created by the capitalist export economy within the coffee complex. However, there was a contradictory articulation expressed in the endogenous scheme of accumulation and its cyclical dynamics: the export boom would create financial accumulation in excess of agricultural investment needs, diverting funds for industrial investments when imports of production goods were cheapened by foreign currency abundance. However, the importation of competing manufacturing goods was also made cheaper and lessened the level of industrial capacity utilization. When the coffee export crisis occurred, the entire complex went into crisis. Still, the industry's profit rate increased with the protection brought about by the currency crisis, inducing import substitution with the utilization of installed capacity until a new cycle of export growth and exchange rate appreciation began. Between the currency crisis and the currency appreciation in each cycle, the balance of payments and the economic policy were subject to the power of external creditors. Between 1884 and 1930, capital accumulation in the coffee economy stimulated large-scale industry, but it imposed narrow limits on industrial accumulation.

As light industries advanced, the problem with heavy industrialization in the production goods sector (steel, electric energy, petrochemicals, internal combustion engine, etc.) is that it could not unfold from wage-earning consumption in late capitalism. In Brazil, there was no capital accumulation scheme and financial centralization mode that would enable local entrepreneurs to face the challenges of heavy industry, not to mention technological limitations and market scales. Therefore, the crisis of capitalism, the collapse of the liberal order, and multilateralism in the 1930s induced in Brazil, under government support, a process of *restricted industrialization* in which the manufacturing industry began to lead the pattern of accumulation and subordinated agriculture. However, neither the State nor local businesspeople gathered skills to promote heavy industrialization without new relations of international dependence. In the period, there would have been an *appearance of national autonomy* due to the lack of conditions and interest of foreign capital to invest in new industrial branches.

In the post-World War II period, the new international economic order under US hegemony enabled a new mode of internationalization of capital centered on foreign direct investment initially directed from the United States to Europe. The response of European and Japanese corporations to the "American challenge" involved FDI oriented to regions served by US exports, such as Brazil. For this to become feasible, however, it was necessary to expand state capabilities to offer inputs, infrastructure, incentives, foreign reserves, orient resources, and distribute coordinated investment tasks with foreign subsidiaries, which only occurred during the "Plano de Metas" – the national industrialization plan – in the JK government. Heavy industrialization, however, did not represent the "economic self-determination of the Nation" mentioned by Celso Furtado, but at most, the self-determination of capital, the consolidation of productive forces suited to capitalism in conjunction with what Tavares and Serra (1982[1970]) called "new dependency."

As a classic, Mello's work suggests a problematics for the Campinas School: it is necessary to be attentive, ultimately, to the structural changes in the patterns of competition, financial and productive internationalization in global capitalism, in which the peripheral economies are inserted in an unequal and combined form. However, in the first instance, local economic and political structures and dynamics, combined with the interests of foreign capital and states "from within," also matter to define the change in trajectory in the pattern of accumulation and international insertion of peripheral economies under the impact of global transformations. Hence, it´s necessary to understand capitalism in its economic, political and social dimensions. Then, based on the contradictory unity between external and internal determinants, the cases of capitalist development in the Periphery can be compared. Understanding without illusions the direction of the historical process, after all, is a condition for critically intervening in it.

The collection does not include the first systematic reflection on the comparative patterns of industrialization. Still, it is worthy of note: it is the thesis of Carlos Alonso Barbosa de Oliveira (2003[1985]). As we have seen, late capitalism designated the industrialization that took place at the time of monopoly capitalism in a country with a colonial past. There is a double determination to temporally classify the emergence of capitalism: the epoch of world capitalism and the structure of local pre-capitalist society in transition. This mark of origin has fundamental and long-lasting consequences on the design and dynamics of such capitalism. Barbosa de Oliveira extended the periodization of the industrialization processes to experiences before late capitalism, based on the double determination mentioned above. Thus, there would be three patterns of capitalism formation: 1) originary capitalism, at the time of primitive accumulation in a country with a feudal past (England); 2) backward, in the competitive stage of capitalism in countries with a feudal past (continental Europe) and an English colony (USA); 3) late, in the monopoly stage, in countries with a colonial past, with comprador and agrarian bourgeoisies as nationally dominant fractions, but subordinated to the world market.

Thus, W.W. Rostow's (1959; 1990[1960]) linear understanding of industrialization is rejected in favor of critically approaching Alexander

Gerschenkron (2015[1952]). This ex-Marxist author (Van der Linden, 2012) proposed a much less simplistic and anachronistic theoretical model to understand the institutional difference of late cases of industrialization that alluded to problems already addressed by Hilferding and Trotsky: the more significant the backwardness, the greater the institutional innovation needed to meet the challenge of industrialization. Therefore, it was not just a matter of imitating liberal Anglo-Saxon institutions, as proposed later by neo-institutionalism à la Douglass North, Daron Acemoglu, and James Robinson. The criticism made by Barbosa de Oliveira to Gerschenkron is that he did not qualify the degree of backwardness with a structural typology of backwardness situations. The degree of backwardness cannot be measured by linear physical time, as the historical time of capitalism is marked by structural breaks representing epochal ruptures. Thus, national backwardness is characterized by structural discontinuities depending on the historical epoch of world capitalism: is it the epoch of primitive capital accumulation, competitive capitalism, monopoly capitalism, or financialization with global corporations? In each era, the challenges are not only more significant; they are structurally different.

In turn, each case pertinent to the three patterns has unique particularities. For example, France and Germany do not reproduce the same institutional model of industrialization. However, the cases differ less within each pattern than between different patterns since problems, restrictions, and opportunities are typical of each historical epoch.

Table 1 – Capitalism: structural forms and historical constraints

Historical Structural form	Global moment of competition (advanced capitalism phase)	Local precapitalist structure
Originary capitalism	primitive accumulation	feudal past
Backward capitalism	competitive capitalism	feudal past
Late capitalism	monopoly capitalism	colonial past

Barbosa de Oliveira studies the cases of England, the USA, France, Germany, Russia, and Japan, emphasizing the specific form of coordination and centralization of resources, as well as the ideologies that animated and legitimized the coordination effort. The question of the political direction of national development projects is central, that is, their concrete socio-political bases. In the same direction as Gerschenkron, the importance of new forms of centralization of capital is identified in the backward experiences of the first wave (France and Germany), with national industrialization projects supported by universal and investment banks. In the case of the second wave, which still occurs at the time of competitive capitalism (Japan and Russia), there is greater direct participation of the State in enterprises and the control of mechanisms of coordination and centralization of capital. In all cases, the State assumes the historic role of supporting the formation of the wage labor market, overcoming barriers to the integration of the national market, and its international protection. In cases of the second wave, however, the State assumes a coordinating role in defining sectoral plans, negotiating the participation of foreign capital and/or taking foreign loans. In cases of late capitalism, as we have seen, the required participation is much higher, which poses major political obstacles to peripheral industrialization in addition to the difficulties associated with structural backwardness. Not surprisingly, countries with advanced industries are much the same as they were a century ago, with the addition of some Asian cases.

Historical backwardness thus assumes a more precise concept: it concerns the backwardness in the discontinuous time that marks the evolution of capitalist competition on a global scale. National forms of capital and state organizations are pressured to adapt to face the new challenges posed by institutional, technological, financial, and political innovations that characterize every leap in the centralization of capital, the technological revolution, and the coordination of decisions. Those who do not change will perish. This idea is valid for understanding the impact of the large US corporation, German finance capital, Japanese keiretsu, Korean chaebol, and the transformation of relations between State and companies operating in China in our historical epoch.

The second text of the collection goes back to thinking about the origins of late Latin American capitalism in the colonization process oriented towards the primitive accumulation of capital in European metropolises. It is by historian Fernando Novais, initially published in 1968. Novais inspired the first part of Mello's thesis, leading Prado Jr.'s reflection on the "meaning of colonization" to another level of academic rigor. Colonization was part of the Old Colonial System, which found meaning in the constitution of monarchical states in Europe, mercantilist politics, and commercial capitalism. The purpose that presided over colonization was to ensure tributes for the metropolis and monopolistic commercial profits for its traders, and this determined the structure assumed by the colonial economy and societies: in Spanish America, mineral extraction was based on native semi-slave labor; in Portuguese America, after the enslavement of the natives, the formation of specialized productive units exploited with slave labor, opening a new profitable branch for the European trade: the African slave trade. Novais starts from Eric Williams' approach to capitalism and slavery and Frederic Mauro's concept of commercial capitalism but articulates them to the more general determinations of the transition from feudalism to capitalism, in addition to comparing Portuguese, Spanish and English colonization. Unlike Mello, he does not propose that slavery in the Old Colonial System be considered capitalist, although it was subordinated to metropolitan commercial capital and contributed to the formation of capitalism.

The chapter by Mello and Tavares (1984) has already been commented on. Next, the text by Maria da Conceição Tavares (1971) anticipates the contemporary discussion of the financialization of capitalism for many years. It addresses the development of the financial system in Brazil after heavy industrialization and the reforms of the military dictatorship inaugurated in 1964. Instead of creating a financial system oriented towards long-term investment, the reforms promoted an institutional framework favorable to the speculative accumulation of fictitious capital for the benefit of large companies, financial institutions, and a small part of individuals (businessmen and middle classes) who received tax exemptions from participating in the waves of capital gains on the stock exchange. Given the transformations of competition and forms of company organization towards 'multinational' conglomerates that control technical progress in strategies of capital accumulation on a world scale, the institutional reforms of the military dictatorship were essentially about ensuring the dependent association between local groups and international financial capital, with a predominance of the latter. This process ended up leading to the financial crisis in the early 1980s. The pioneering nature of the discussion of fictitious capital and its systemic impact is undeniable: the new introduction of Josef Steindl's *Maturity and Stagnation in American Capitalism* articulates the issue in similar terms but is from 1976. Paul Davidson's *Money and the Real World* is from 1972, and *John Maynard Keynes* by Hyman Minsky is from 1975. Still, they did not develop an analysis of the combination between different forms of accumulation at different spatial scales, such as the article by Tavares, together with the already alluded Tavares & Serra (1982[1970]).

The following two chapters are assessments of the structure and dynamics of capitalism after heavy industrialization in Brazil, together with a critical diagnosis of the economic policy of the military dictatorship. First, the chapter by Tavares and Belluzzo (1978) mobilizes a Kaleckian-inspired model of sectoral relations, combined with an assessment of market structures influenced by Paolo Sylos-Labini and Josef Steindl, to explain the cyclical dynamics of capitalism in Brazil from the policy-induced recovery in the mid-1960s to the slowdown in the late 1970s. It also proposes an innovative postkeynesian reflection to elucidate why the cyclical deceleration was accompanied by inflation acceleration and heightened financial speculation. It is worth noting that, without abandoning the Marxist heritage, Luiz Gonzaga Belluzzo is a pioneer in the creative dialogue with the postkeynesian tradition consolidated in the 1970s.

Carlos Lessa's chapter (1977) assesses the political economy of the II National Development Plan (1975-1979), which proposed to shift the axis of industrialization to the national capital goods sector and make Brazil a great industrial power. Although the hypothesis that the II PND had already been abandoned in 1977 has been subject to criticism, the article correctly points out the causes of the partial failure of the II PND in economic obstacles – the limits to the demand for capital goods in an internationalized economy undergoing cyclical deceleration – and political constraints, such as the resistance of sectoral and regionally dominant business groups, hitherto favored by economic policy. Such limitations to the II PND would be at the root of the nationalization of the foreign debt, which would provoke a structural crisis in the pattern of capitalist development in Brazil instead of its elevation to the status of a great power.

The following four chapters are concerned with the extreme concentration of wealth and income inherent in the structure of capitalism in Brazil. Barbosa de Oliveira and Wilnês Henrique (1990) start with a critique of the distinction between developed and underdeveloped countries that explains income distribution in the labor market by the interaction between the type of (capital-intensive) industrial technology and the availability of "factors of production" (labor-scarce in developed countries and labor-abundant in underdeveloped ones). Instead, the determining variables were the agrarian question (degree of land concentration and rural unionization) and the social and labor question. These are related to the existence (or not) of grassroots movements that can support social-democratic reforms that increase wages, directly and indirectly, socialize risks to citizens with expanded social rights, increase public employment, regulate capital-labor relations, and finance social policies with progressive taxation on income and wealth. Thus, the reproduction of poverty in the Brazilian industrialization period is not explained by technological reasons but by how the agrarian question was addressed (land concentration, repression of rural unionization, and a large and rapid rural exodus that created a surplus urban population outside the formal labor market), and by regressive wage, labor, social and tax policies, especially after the post-1964 military dictatorship.

Given this analytical framework, the following three chapters address the agrarian, social, and labor questions throughout Brazilian industrialization. Romeiro's chapter (1992) compares how the agrarian question was addressed in developed and underdeveloped countries to show that the decentralization of land ownership and the political protection of rural workers' rights, unlike in Brazil and Indonesia, was fundamental to reducing poverty by controlling the rural exodus and lowering the urban cost of food. Considering the compared international experience, it justifies an agrarian reform in Brazil that involves less the expropriation of productive areas than the substantial taxation of rural wealth. The chapter by Liana Aureliano and Sonia Draibe (1989) is based on an assessment of the interpretations of the Welfare State according to the degree of universalism and depth of social coverage, institutional fragmentation, and progressive financing. Given this, the historical specificity of social policy in Brazil is characterized by the federal administration's political and financial centralization, institutional fragmentation and incoherence, low levels of universalization and popular participation, and little progressive funding. To effectively fight poverty and universalize social rights, it would be necessary to overcome the type of social protection of the authoritarian State that they saw being reproduced, in general terms, in the first government of redemocratization. As for the labor question, the chapter by Tavares and Souza (1981) empirically refutes Arthur Lewis' hypothesis reformulated by ECLAC authors, according to which the urban wage rate would be slightly higher than the subsistence wage due to the unlimited supply of workers. As a matter of fact, the rural masses expelled from the countryside are on the margins of the formal urban market – the one that guarantees contracts and labor rights – and cannot compete to the point of depressing the wages of formalized workers. Thus, the floor of the formal market is defined by the minimum wage policy, which in turn is the income ceiling and target in the informal urban market. Above this floor in the formal market, there is wide salary heterogeneity due to barriers between the internal labor markets in sectors of activity and even inside large companies, and the heterogeneity of union power in the various industries. Therefore, industrialization can contribute, but it is far from sufficient to raise the income of the urban poor, which depends on specific social, salary, and employment policies.

The following three chapters discuss the devastating effects of the foreign debt crisis on the Brazilian economy in the 1980s. Davidoff Cruz (1995) traces the origins of the problem in policies to stimulate external indebtedness as soon as the military dictatorship began, approaches the indebtedness process of state-owned companies during the execution of the II PND, and, finally, the possibility of transferring the private debt to the Treasury via the Central Bank since 1977. In the 1980s, subsidies to exporters reached 3% of GDP (or 60% of the value of FOB exports), being complemented by the real devaluation of public prices and tariffs, which contributed to facilitating the adjustment of the large private company to the detriment of the public sector budget and state-owned companies, leading to a significant reduction in public investment. Belluzzo and Almeida (1992) show how the socialization of large company losses was complemented by the macroeconomic policy monitored by the IMF. The rise in interest rates to provoke recession and increase tradable production surpluses (supported by currency devaluation and tax subsidies) also increased the rollover costs of domestic public debt and provided an advantageous alternative to productive private investment: rent-seeking with public debt securities. The instability of the exchange rate led to increases in inflation, while the daily maturity of public securities not only protected private wealth against inflation but also increased it with significant liquidity. Thus, rentiers and exporters assumed an almost monopolistic economic power over the management of monetary and exchange rate policy, determining favorable interest and exchange rates, which made inflation stabilization policies unfeasible without resolving the external and public financing crisis.

Carneiro (2002) demonstrates that the crisis in public investment and state-owned companies hampered productive private investment, which grew at lower and more unstable rates than in the post-war period. The increase in the trade balance that allowed the payment of foreign debt services depended more on the reduction in imports generated by the maturation of investments in the II PND and by the limitation of domestic demand than on the increase in exports. Export growth, in turn, depended mainly on the sectors that took advantage of idle capacity caused by investment decisions in the 1970s and by the contraction of domestic absorption in the 1980s rather than new investments induced by favorable relative prices for exports. When idle capacity declined with the recovery of the domestic market in the middle of the decade, the trade balance itself was harmed by the increase in imports and the reduction of exportable surpluses, instead of stimulating new investments oriented toward the external market. Therefore, the need to generate trade surpluses to pay the foreign debt represented an obstacle to the resumption of sustained economic growth, as the reduction in the trade balance led to the balance of payments crisis caused by the enormous and inflexible foreign debt services. In short, the foreign debt crisis and the fiscal crisis of the State and state-owned companies represented a strongly negative rupture in the structure and pattern of dynamism of capitalism in Brazil. Exports did not replace public investment as a stimulus to private investment and as sources of sustained growth.

The following two chapters resume the reflection on the structure of Brazilian capitalism considering its crisis in the 1980s and its redefinition in the 1990s. In dialogue with Celso Furtado, Mello (1997) redefines Core and Periphery in a three-dimensional hierarchy: technological innovation sustained by capitalist organizations with great financial power; international currency and finance backed by industrial power; political-military power. It explains the peripheral underdevelopment due to the growing discontinuities between the global tendency of centralization of capital, the initial conditions in the Periphery, and the obstacles to national development projects due to the interest of the ruling classes in imitating consumption styles without seeking to internalize a minimum capacity for autonomous financing and innovation. In this sense, the globalization process must be understood as a liberal-conservative counter-revolution that means, for the Periphery, productive regression, more social exclusion, and a redoubled return to external dependence. Sampaio Jr. (1999) seeks to explain the same processes using classics from the social sciences in Brazil. From the Marxist historian Caio Prado Jr., Sampaio Jr. highlights the contradiction between the possibility of forming a modern Nation and the colonial heritage manifested above all in the international control of the leading industrial sectors, limiting economic growth, technological development, and the balance of payments. From the Marxist-Weberian sociologist Florestan Fernandes, Sampaio Jr. emphasizes the bourgeoisie's realistic and pragmatic option for a subordinate alliance with international capital and with hegemonic nations to the detriment of organic solidarity with the popular classes, abandoning reformist, nationalist and democratic projects during industrialization and, in the epoch of neoliberal globalization, returning to the condition of the "comprador" bourgeoisie. From the historical-structuralist economist Celso Furtado, Sampaio Jr. emphasizes the interrupted construction of the project of formation of the Nation due to the submission of the Brazilian economy to the logic of global corporations in the neoliberal era. Faced with the diagnosis of neocolonial reversal, Sampaio Jr. proposes the alternative of the national revolution – a prelude to the socialist revolution – that tackles external dependence, social inequality, and cultural colonialism under the workers' leadership.

The following three chapters discuss the impact of Brazilian neoliberal reforms on the structure, dynamics, and insertion into global capitalism in the 1990s. Belluzzo and Almeida (2002) show that inflationary stabilization, with the Real Plan of 1994, occurred due to the exchange rate peg enabled by the first expansionary phase of the liquidity cycle of the global financial market in the early 1990s. Dependence on the global liquidity cycle made the exchange rate and foreign indebtedness very vulnerable to the cyclical reversal after 1997, despite a monetary policy free to pay the liquidity premium associated with currency devaluation risk. Sold as a condition for neoliberal reforms to allocate resources "correctly" under the impact of privatization and trade and financial opening, disinflation was accompanied by a high interest/overvalued currency mix that, on the contrary, contributed to limiting productive investment and exports, shrinking production chains, concentrating income, encouraging investments in bonds rather than in fixed capital, and promoting foreign investment in mergers and acquisitions rather than in new plants. Excessive interest rates and the issuance of exchange rate-indexed government bonds amplified public debt despite privatizations. Increased external fragility and the reversal of the global liquidity cycle led to balance-of-payments and financial crises, bringing a new period of submission to the IMF. The age of business cycles determined by the endogenous fluctuation of local autonomous spending, with the great importance of public investment, is in the past.

The chapter by José Graziano da Silva (2001) discusses the rural world in the 1990s. It shows how the centralization of capital and the technological modernization of large agricultural estates resulted in an expansion of production with a reduction in agricultural employment, tending to make small-size family farming impossible in traditional food cultures. However, this would not make the agrarian reform program unfeasible if it is associated with public policies for family farming (with popular participation and rural unionization) and for developing non-agricultural rural activities that ensure settlements and limit rural exodus. The chapter by Laplane and Sarti (2006) analyzes the manufacturing industry. It demonstrates that, in a scenario of low and unstable growth, trade opening with currency appreciation induced defensive strategies of employment reduction and modernization via the importation of capital goods, leading to the abandonment of activities that demand longer-term investments, particularly in technology-intensive sectors. Such “regressive specialization” made the manufacturing industry less dense, with a higher import coefficient and, contrary to what was expected by neoliberal reforms, an almost stagnant export coefficient in the 1990s. Foreign investment was concentrated in mergers and acquisitions without much expansion of productive capacity. Denationalization increased remittances of profits, which, together with the increase in imports, increased the demand for foreign exchange reserves in the manufacturing industry. Only in 2003 did the global recovery push industrial exports to the point of generating sectoral trade balances for a few years, but without significantly modifying the structural characteristics consolidated in the previous decade, despite the resumption of industrial policy. Between 1990 and 2003, the annual growth rate of the manufacturing industry in Brazil was almost half (1.6%) of GDP growth (2.6%) and lower than the Latin American average, indicating the degradation of the insertion of the Brazilian economy in the world capitalism and the failure of the declared goals of neoliberalism.

The following three chapters address some issues of Brazilian capitalism in the governments of Luis Inácio Lula da Silva (2003-2010) and Dilma Rousseff (2011-2015). The chapter by Cano (2014) discusses Brazilian deindustrialization in a broader temporal perspective that starts from the situation before neoliberalism and grasps the impact of the Chinese rise, the growth of the domestic market, and the industrial policies of the 2000s. Cano explains the importance of industrial diversification of the production goods industry to distinguish between development and underdevelopment. He differentiates *normal deindustrialization* due to increased industrial productivity, the advanced services sector's growth, and corporate-led relocation from developed countries against *premature deindustrialization,* affecting the underdeveloped economies that carry out neoliberal programs. In the second part, although it promises to discuss Brazilian deindustrialization, it delivers more. It presents a comprehensive overview, with a lot of data, of the main trends of the Brazilian economy in the period in question, concluding with the proposal of a National Development Program.

The chapter by Baltar and coauthors (2010) also delivers more than it promises, that is, the analysis of the world of work in the Lula administration. The first part addresses the macroeconomic dynamics of the 2000s, arguing that the initial impulse of exports was multiplied by an economic policy aimed at fighting poverty and increasing income and credit for low and middle-income workers with a great propensity to consume, encouraging private investment. The resulting growth in GDP and tax revenue led to the resumption of government and state-owned companies' investment. In the second part, the progress in the labor market is described: reduction of the unemployment rate, improvements in the occupational and income structure, increase in the proportion of occupations under the protection of labor legislation and rising minimum wage, and reduction of the enormous income inequalities between workers. The third part shows how the growth of employment was accompanied by social policies, a policy of raising the minimum wage, a greater inspection of compliance with labor legislation, and union participation in collective bargaining, contributing to the improvements described. Although for a relatively short period, the change in the correlation of social and political forces favored the expansion of the participation of wages in the functional distribution of income.

Carneiro (2018) proposes that the Brazilian economic crisis in 2015 is ultimately explained by the global conjuncture of aggravation of financial instability and industrial competition after 2008. In the first instance, though, the crisis is explained by the cyclical slowdown and the poor execution and fragile political support of social classes and interest groups for the economic policy of the Rousseff government. Financial instability manifested itself in the so-called *taper tantrum* of 2013, whose impact on currency depreciation was decisive in raising inflation. Given the globalization of value chains, the increase in idle capacity and the reduction in industrial prices in the world after the 2008 global crisis led to an intensification of market competition that resulted in the stagnation of Brazilian industrial production. Regarding the domestic demand cycle, the deceleration in consumption is explained by the limits to the expansion of the minimum wage, social spending, and credit, and the slowdown of investment induced by the leakage of demand due to production goods imports. The main economic policy mistakes were the difficulty of negotiating the program of infrastructure concessions to the private sector until 2014, the sudden reversion to fiscal and monetary austerity, and the adjustment of relative prices (exchange rate and administered prices) in 2015 and 2016.

Finally, Bastos and Belluzzo (2021) discuss the concepts of capitalism, freedom, democracy, citizenship, liberalism, social democracy, financialization, and neoliberalism to characterize, from a historical perspective, the neoliberal era and, within it, Bolsonarism. The project of the Jair Bolsonaro administration is understood as authoritarian neoliberal having as references the typology proposed by Nancy Fraser (2020), the contemporary context of contradictions between capitalism, neoliberalism, and democracy, and an international comparison with other right-wing leaders. After explaining the content of the policies implemented by the Bolsonaro administration in the context of the generalized failure of neoliberalism in the world, the authors urge young researchers to update the fundamental methodological principle of the Latin American structuralist tradition, which includes the Campinas School. In sum, researching how dependence is internalized in underdeveloped countries themselves and modifies their structure from within as it articulates their economies as part of the strategies of corporations and global investors and, thus, constrains economic policy itself. However, the economic policy also responds to the requirements of the capital accumulation model and to conflicts between different coalitions of local social groups and their international allies. The task is essential not only to understand Brazil's place in the world but to think of a new national strategy in the face of the challenges posed by the aggravation of inequalities after the Coronavirus pandemic and the ecological emergency.

It is noteworthy that the selected texts are a small sample of the vast academic production of the Campinas School. In this sense, the book is just an appetizer and an invitation for readers to seek to know more about the classic texts and the current production of Unicamp's Institute of Economics.

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CHAPTER 1

THE LATE CAPITALISM (INTRODUCTION)

João Manuel Cardoso de Mello

The *Estudio Economico de América Latina* - 1949 marks the birth of ECLAC's Political Economy due to a clear delineation of the problematics in which ECLAC thinking would move. After so many years, let us try to reread this work, which expresses one of the culminating moments of Latin American social thought.[1]

The entire analytical framework of the *Estudio* is based on the idea of **uneven development** of the world economy:

> The spread of technical progress from the countries where it had its source to the rest of the world has, from the point of view of each generation, been relatively slow and irregular. During the lengthy period which elapsed between the industrial revolution and the First World War, the new methods of production in which technique has constantly found its expression have reached only a small proportion of the world's population. The movement began in the United Kingdom, continued in varying degrees of intensity in Europe, received an extraordinary impulse in the United States and finally reached Japan, which strove to rapidly assimilate Western methods of production...Thus the great industrial cores of the world grew up, while the vast and heterogeneous peripheral areas of the new system shared only to a slight extent in the improvement of productivity. In these peripheral areas, technical progress only affected small sectors of the vast population, as it usually only penetrated where it was needed to produce foodstuffs and raw materials at low cost for delivery to the great industrial cores.
> [...] Carefully considered, the economic development of the peripheral countries is one more stage in the worldwide spread of the new forms of productive technique, or, if preferred, in the organic development of the world economy. ECLAC (1951: 3).

The uneven propagation of technical progress (seen as the essence of economic development) therefore translates into the configuration of a determined

1 Refer to ECLAC (1951). Our vision of this work follows the important *Estudio sobre el pensamiento de la CEPAL* (1948/1954) by Octavio Rodrigues, which is still unpublished.

structure of the world economy and a specific international division of labor: on the one hand, the Center, which comprises the set of industrialized economies, diversified and technically homogeneous production structures; on the other, the Periphery, composed of economies that export primary products - food and raw materials - to the core countries, highly specialized with dual production structures.

The character of primary products exporters gives the peripheral economies' dynamics its fundamental trait:

> There is, in fact, a dynamic element in the manufacturing industry that is not found to a comparable extent in primary production. As its name would imply, the latter covers the initial phases of the productive process, while the manufacturing industry accounts for subsequent stages. Because of this relative position of the two activities, the increase in industrial activity stimulates primary production, but the latter has not the power to generate industrial production. When industrial entrepreneurs, stimulated by the normal economic forces or extraordinary factors in times of war, undertake to increase output, demand for primary products increases; as profits are consequently greater, entrepreneurs in the periphery seek to increase primary production. The spontaneous increase of the latter, on the other hand, does not cause a similar rise in industrial demand, which would be capable of absorbing that increase [...] (ECLAC, 1951: 49-50).

Peripheral economies as primary products exporters (it would later be said: in the stage of **outward-looking development**) thus do not have control over their own growth, which, on the contrary, ultimately depends on the vigor of demand in the core.

The demand for primary products exerted by the core, after the rapid rise of international trade that goes from 1880 to 1914 and marks the birth of the peripheral economies, would have shown little dynamism for two reasons: the core countries' relatively slow economic growth and the drop in their global imports coefficient, resulting from the shift of the hegemony in the core from England to the United States.

The consequences of this slack in demand are more alarming when we recall that, in the *Estudio*, the slowness with which the industrial development of the core is absorbing the actual or potential excess of the active population dedicated to primary production (in the absence of international mobility of labor) is at the root of the **deterioration in the terms of trade** of the peripheral economies:

> "This is all the more necessary since we are dealing with a phenomenon which is closely related to how technical progress is spread throughout the world. [...] This phenomenon is **purely dynamic**, and we hope to prove that, ultimately, it can be explained by the relative slowness of the world's industrial development to absorb the real or potential surplus of population productively employed in primary occupations. [...] Thus, there is a relative abundance of potential labor in primary occupations, constantly tending to exert pressure upon wages and the prices of primary products, and preventing the periphery from sharing with the industrial cores the advantages of the technical progress attained by the latter. Furthermore, the periphery is unable to retain a part of the benefits of its own technical progress."[2]

The world economy dynamics, therefore, tends to deepen uneven development (whose immediate expression is the difference in average productivity and income between the core and the periphery) because the core is capable of maintaining its productivity increases and appropriating part of the results of technical progress introduced in the periphery. In other words, there is a tendency to concentrate the fruits of technological advancement in the core economies. The mechanism by which this happens is the deterioration in the terms of trade.

If the structural transformations in the core after 1914 seem to remove any hope of supporting Latin American development in the expansion of exports of primary products, the real movement of the world economy, at the same time, stimulates the rupture of the international division of labor. As a result, the Latin American economies enter a new stage - **inward-looking development**:

> "A few early signs of this new stage had already appeared in the primary producer countries before the First World War. But it was the war, with the consequent difficulties of maintaining imports, which revealed the industrial possibilities of those countries. Meanwhile, the great economic depression of the 1930's strengthened the conviction that those possibilities had to be used to offset, by means of internal development, the manifest failure of the external incentive which until then had stimulated the Latin American economy; this conviction was confirmed during the Second World War, when the Latin American manufacturing industry, with all its improvisations and difficulties, nevertheless became a source

2 Refer to ECLAC (1951: 46-7, emphasis added). It is clear, thus, that the attempt to give another conceptual aspect to the deterioration in the terms of trade as uneven exchange not only adds nothing to Prebisch's approach but actually represents a step backward, given its static formulation. Refer to Emmanuel (1972) and Charles Bettelheim's sharp *Remarques théoriques* that follow (p. 295-341) Emmanuel's work.

> of employment and consumption for a large and increasing part of the population" (ECLAC, 1951: 3-4).

What problems should this industrialization, which emerged as a spontaneous reaction by Latin American nations to the import difficulties of the World Wars and the Great Depression, have to face? The answer is quite simple: **the problems** and, at the same time, the **specificity** of Latin American industrialization come from its peripheral nature. Or better saying:

Latin American industrialization is problematic because it is peripheral

The uneven world development is reflected, first of all, in the mismatch between the core's "advanced" productive techniques and the periphery's savings capacity:

> "In the more highly developed countries, the productive technique requires a high capital investment per man employed. However, the gradual increase in productivity brought about by this technique enabled these countries to attain a high level of per capita income to assemble the savings required to create the needed capital. On the other hand, savings are low in most Latin American countries because of the low-income level. When the great modern industrial cores were in a position comparable to that of present-day peripheral areas, and the per capita income in these cores was relatively low, the productive technique also required only a relatively small capital investment per man. Careful study shows that savings are neither great nor small of themselves but only compared to capital density, determined by technical progress. In this sense, savings in Latin America are, on the whole, minimal in comparison with the requirements of modern techniques. [...] Consequently, countries that have recently begun their industrial development have, on the one hand, the advantage of finding a degree of technical advancement in the great cores which required time and sacrifice to acquire. Still, on the other hand, they encounter all the disadvantages inherent in lagging behind in the course of evolution" (ECLAC, 1951: 62-3).

Peripheral industrialization also bumps into the imbalance between imported techniques and the relative weakness of demand:

> "Another important consequence of the disparity between the degree of growth of income and that of production technique is the low level of demand which generally characterizes the greater part of the Latin American populations, despite their numerical size. Not only does lack of capital or of skill in managing it stand in the way of the adoption of advanced

> methods of technique, but, in addition, low demand makes it impossible to reap the benefits of mass production. Industrial development in the great cores cannot have been hindered by limitations of this kind. There, the initially low income coincided with production on a correspondingly small scale. This scale grew in time, as greater productivity raised incomes and, with them, demand, which in turn absorbed the larger, better, and more varied production. The situation is very different in the countries which are now adopting the modern industrial technique. Here the demand is low because productivity is low; this is so because weak demand in its turn impedes, along with other factors, the utilization of more advanced technique" (ECLAC, 1951: 63-4).

Finally, **inward-looking development** would manifest a tendency towards structural unemployment because technical progress brings unemployment, as in the cores. Still, the demand for capital goods inherent to it does not manifest itself in the periphery due to the lack of capital goods industries.

> "These unfavorable influences on employment and wages have often led to reactions adverse to technical progress in the development of the great industrial countries. Nevertheless, by requiring increasing capital investments, this same technological progress develops in these countries a powerful factor of absorption of unemployed workers through the development of capital goods industries. Thus we see that technical progress creates unemployment but at the same time tends to reabsorb the displaced workers by means of increased investments. […] The element of expansion, the effects of which are felt in all sectors of the economic activity of the great cores, is lacking in the peripheral countries; consequently, their exports are not sufficiently significant to offer productive employment to those unemployed due to technical improvements. Therefore, it is not surprising that the fear of unemployment is ever-present and that it sometimes takes the form of stubborn hostility to the use of more advanced capital equipment, the immediate consequence of which is to reduce the labor requirements of primary and industrial production. The absence of this spontaneous element of development does, in fact, lead to extraordinary conditions. In the periphery, technical progress is accompanied by unemployment as in the great cores. Still, the demand for capital goods inherent in such progress does not operate in the former as in the Core countries, since a capital-goods industry is lacking in the periphery.
>
> Consequently, instead of being reflected in the economy of the developing country, this demand transfers its effects to the industrial cores where such goods are produced" (ECLAC, 1951: 65).

ECLAC's Political Economy was thus born to explain the nature of the industrialization process that had taken place between 1914 and 1945 in several countries; reveal its possible trajectory; indicate the problems it would face if it wanted to succeed; and suggest economic policies that were able to overcome them. But it was born, at the same time, to say loud and clear to the Nations of *Nuestra América* that industrialization would be the only path to follow if they wished to become the masters of their own destiny and, at the same time, be freed from misery.

It is not difficult, therefore, to locate the problematics of ECLAC's Political Economy. **Every space in ECLAC's discourse is organized around the idea of the nation's economic independence. Better still: ECLAC's problematics is the problematics of national industrialization, based on a "peripheral situation."**

The core of the problem of industrialization resides in the antinomy between the full constitution of the Nation and certain international division of labor that had transformed it into a Periphery, that is, into an economy that was commanded by decisions taken at the Core, because its dynamics was ultimately stuck in external demand. Peripheral economies, while dependent, are a mere extension of the economic space of the core economies and could not be considered as **national economies**[3]. Moreover, as they continued to **grow outwards**, the Latin American economies would remain doomed to misery, since any effort they made to overcome it would be frustrating: is this not the deep meaning of the tendency to deterioration in the terms of trade? Therefore, dependence and poverty were two sides of the same coin, the "peripheral situation."

Industrialization appears as the crucial moment in the constitution of the Nation, as a way for the Nation to become a reality, ceasing to be what it was, a quasi-fiction. With it, a new stage begins, that of **inward-looking development**, because the dynamic center of the economy shifts **into the Nation**, which starts to command itself. The displacement of the dynamic center of the Latin American economies, that is, the replacement of the exogenous **external demand** variable by the endogenous **investment** variable as the economy's engine, is equivalent to the displacement of decision centers towards the interior of the Nation. As Prebisch said in another work, industrialization "is not an end in itself, but the only means that they (Latin American countries) have to capture the fruit of technical progress and progressively raise the masses' standard of living" (Prebisch, 1961).

In a word: building the economic bases of the Nation and eliminating poverty are also two aspects of the same process, that of industrialization.

3 No one expressed this idea better than H. Singer, whose influence on ECLAC thinking is well known. Refer to Singer (1950: 473-85), republished in: Okun & Richardson (1961: 170-80), especially pages 170 to 172.

The opposition Nation/international division of labor is renewed in the process of peripheral industrialization: the disparity between "advanced" productive techniques and the periphery's savings capacity, the imbalance between imported techniques and the relative fragility of peripheral demand, and the tendency to underemployment are precisely its new manifestations. In other words, Latin American industrialization, because it is peripheral, faces problems that give it specificity that, when you think about it, can be reduced to a single one: the absence of a production goods industry at a time when the Core formed an industrial structure permeated by highly advanced technology. Hence, the expansive effects of investment filter outward; thus, the imports of production goods contain inadequate technology to Latin American needs. Precisely because Latin American industrialization is problematic (and specific), the resolution of difficulties cannot be left to the free play of market forces but must be the object of a conscious intervention in reality, which is apprehended by the idea of **planning**.

As far as ECLAC's Political Economy sees industrialization as national industrialization, one dispenses with any endogenous accumulation scheme, which could reveal other oppositions (basically the wage/profit opposition). Instead, there are only "internal impacts" resulting from importing a certain technology, visualized from the perspective of the macroeconomic functions of production, opposed, in the final analysis, to the periphery's low savings capacity.

ECLAC's Political Economy was born with the *Estudio Econômico de América Latina* - 1949, and it was in the struggle for national industrialization that it has developed. In the battles over the orientations to be imprinted on economic policy, fought with knowledge and imagination by Prebisch, Furtado, Aníbal Pinto, and so many others, ECLAC thinking began to shape. The structuralist theory of inflation emerged from the fight against orthodox-inspired stabilization policies; the almost generalized failure of industrialization after 1955 led to the elaboration of the idea of structural obstacles, which ended up in the proposition of "structural reforms"; the isolated success of Brazilian industrialization has made it possible to reveal, in its entirety, the Latin American industrialization rationale (within, of course, ECLAC's problematics).[4]

And then we reach the mid-1960s, when the death of the national-developmentalist social movement became evident. Industrialization had either aborted itself or, when it had been successful, brought with it neither national liberation nor the elimination of poverty.

With this, a question remained in the air: why would history have taken another course, defrauding hopes that once seemed so well founded? At the theoretical level, the answer consisted, we all know, in the formulation

4 Refer especially to R. Prebisch (1952, 1959, 1961, 1963); Celso Furtado (1961, cap. 3-6, 1971 - 1. ed. 1959); Sunkel (1958); A. Pinto (1960); Seers (1962); M. C. Tavares (1964).

of the "Dependency Theories," which were born, thus, to face the **issue of national non-industrialization**.

ECLAC's influence in the idea of "external dependence" is clear, as it simply results from the concept of uneven development of the capitalist world economy, which is expressed in the Core/Periphery relationship. In this way, it would not be difficult to imagine Latin American History as a succession of "situations of dependency": colonial dependency, primary-export dependency, and technological-financial dependency.

From this point of view, the first dimension of Dependence - represented by A.G. Frank's works, centered on the idea of "development of underdevelopment," which is understood, in a nuclear manner, as a continuous re-articulation of an exploration relationship between Metropolises and Satellites - is, in a crystalline manner, a mere **radicalized reproduction of ECLAC's problematics,** and, for this reason, it presents no greater theoretical interest[5].

On the contrary, F. H. Cardoso and E. Faletto's formulation deserves careful analysis for its decisive importance.[6]

The starting point of **Dependence and Development** consists of a certain explanation for the failure of predictions arising from ECLAC's analyses:

> "At a first approach, therefore, the impression is that the interpretative scheme and the predictions that could be formulated in the light of purely economic factors at the end of the 1940s were not sufficient to explain the subsequent course of events" (Cardoso & Faletto, 1970: 13).

Therefore, the whole problem seemed to lie in the fact that ECLAC's Political Economy did not take due account of the social and political conditions of the economic process. But how to do it? After a reckoning with evolutionary and functionalist theories of development, the answer was readily given:

> "To acquire meaning, such an analysis (the global analysis of development) requires a double effort to redefine perspectives: on the one hand, consider in their entirety the 'particular historical conditions' - economic and social - underlying development processes, at the domestic and external levels; on the other hand, understand, in given structural situations, the objectives, and interests that provide meaning, guide and animate the conflict between groups and classes and social movements that 'set developing societies in motion'" (Cardoso & Faletto, 1970: 21).

5 Refer to Frank (1970) and the works *El desarrollo del subdesarrollo; Dependencia econômica, estrutura de clases y política del subdesarrollo en América Latina* e *Sociologia del desarrollo y subdesarrollo de la sociología*, all republished in Frank, Cockoft & Johnson (1970).

6 Refer to Cardoso, F. H. & Faletto (1970), and also Cardoso, F. H. (1971: 25-45).

The fundamental implications of this proposed style of analysis are pretty straightforward: 1) Latin American development is not just any development, but **capitalist development**; 2) capitalist development in Latin America is **specific because it takes place in a "peripheral national situation."** This is, in fact, what the concept of dependency was intended to account for:

> "The recognition of these differences (between 'original' capitalist development and Latin American capitalist development) led us to critique the concepts of underdevelopment and economic periphery and to value the concept of dependency, as a theoretical instrument to accentuate both the economic aspects of underdevelopment and the political processes of domination of some countries by others, of some classes over others, in a context of national dependence. Consequently, we emphasize the specificity of the establishment of a capitalist mode of production in social formations that find their peculiar historical trait in dependence" (Cardoso & Faletto, 1970: 139).

I think, therefore, that **Dependence and Development** represents an attempt to constitute new problematics, the problematics of "the establishment of a capitalist mode of production in social formations that find their peculiar historical trait in dependence," **the problematics of the formation and development of the mode of capitalist production in Latin America.** More than that, it brings, in my opinion, among others, a fundamental contribution: the idea that the Latin American social dynamics is determined, in the first instance, by "internal factors," and, ultimately, by "external factors," from the moment the National State was established (Cardoso & Faletto, 1970: 22 and the following).

It should be admitted, however, that the attempt could not be completed because, for this, it would be essential to critique ECLAC's Political Economy from its roots, and not from its results as it was proceeded: basically, from ECLAC's criterion of historical periodization (colonial economy/national economy, outward growth/imports substitution industrialization and extensive industrialization/intensive industrialization), which is reproduced taking into account "social and political factors" (Colonial Society/National Society, outward growth, consolidation of the internal market, internationalization of the internal market) and ECLAC's **explanations for the "economic passage" from one stage to another, from one period to another**. Finally, it would have been necessary not to locate the mistake in ECLAC thinking in the abstraction of the economic process's social and political - internal and external - conditions, but to think, to the last consequences, Latin American history as the formation and development of a certain capitalism. Not being able to start from a correct periodization, nor from a scheme that would concretely capture the economic movement of society, the integrative perspective was lost, to a large extent, giving the impression that it was only the introduction of social classes in ECLAC's theoretical body.[7]

This task - that of rethinking Latin American history as the formation and development of the capitalist mode of production - has advanced considerably in recent years. This work intends to make some contribution to this.

7 All the difficulties arising from the introduction of social classes in ECLAC's theoretical body appear, in full, in the concept of social marginality, which should retain the greater specificity of the Latin American class structure.

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CHAPTER 2

BRAZIL IN THE OLD COLONIAL SYSTEM[1]

Fernando A. Novais

Colonization as a System

Relations between the metropolises and their respective colonies during a particular period in our history is best understood as constituting a system of interrelated forces. For the early modern period — between the Renaissance and the French Revolution — it seems useful, in the tradition of many historians, to refer to these relationships as the Old Colonial System of the mercantilist era. Even this first, purely descriptive approach already allows us immediately to establish an early distinction of no small importance. Not all colonization occurred within the boundaries of this colonial system; the more general phenomena, the enlargement of the area of human settlement on the globe through the occupation, population, and development of "new" regions — in the words of geographer Maximilien Sorre, "the organization of the ecumenical"— has given rise to a wide variety of distinct historical situations, and it is only to one of them that we refer here.[1] In the early modern era, however, the unfolding of the process elaborated a specific set of relations, and this mercantilist system of colonization is the key to understanding all European colonization between the first maritime discoveries and the Industrial Revolution. In understanding it we can discern certain essential common denominators that persist as fundamental constants within a complex variety of particular historical circumstances — circumstances that varied from metropolis to metropolis as well as among the colonies —during the sixteenth, seventeenth, and eighteenth centuries.

These colonial relations can be understood on two levels: first, through the extensive colonial legislation imposed by the various colonizing powers (Portugal, Spain, Holland, France, and England); and, second, in the actual practice of trade and governance, that is, in the commercial arrangements and politico-administrative ties that involved all parties. The basic aim of colonial legislation was to discipline these political and, above all, economic

1 Translated by Richard Graham and Hank Philips.

relations. Still, for what we are undertaking at this early point in our analysis (defining the workings of European colonization during the Old Regime), our overriding concern is with the legal norms of the times, for these were the embodiment of the objectives of the colonizing entities, expressing their aims in the colonization process. Thus, the English Acts of Trade, the "laws that ban foreign ships... from Brazilian ports,"[2] Colbertian colonial legislation, charter company regulations, and so on, were all relevant examples of the immense body of European colonial laws that encompass the common denominators we seek here. Also, during the unfolding of the colonization process, the role and position of the colonies within the framework of European states' economic life was laid out theoretically by the pundits of mercantilist economics. The goals of colonial undertakings were thus specified, and the legislation of the times merely served as a vehicle for carrying into practice the principles formulated by mercantilist theory.

In order firmly to orient ourselves within the enormous framework of European colonial history, it seems useful, as we develop a tentative initial characterization, to begin with the typical model of the functioning and relations of the Colonial Pact as formulated by these theorists of mercantilist policy. One such theorist who formulated that policy with crystal clarity was [Malachy] Postlethwayt, who in 1747 wrote: "The colonies... should: first, provide the metropolis with a larger market for its products; second, provide employment for a larger number of its [the metropolis's] manufacturers, artisans and mariners; [and] third, furnish a greater quantity of needed articles."[3] To use a modern term, the colonies ought to constitute an essential factor in the development of the metropolis. So went the theory. To be sure, actual history runs along somewhat atypical and peculiar lines rather than along those contained within the framework of the models; and European colonization during the modern epoch offers a whole gamut of situations both approaching and differing from that scheme, varying in time and space and inexorably complicating reality. Yet to ignore that basic project that for several centuries gave form to European overseas policies, a project that forms thereby part of this same and complex reality, would mean not coming to know the deeper mechanisms inherent in the process and obtaining only a superficial view of each isolated event. Viewed as a whole and polarizing the European economies on one side and the peripheral colonies on the other, it cannot be denied that the colonial experience was fashioned according to that fundamental desideratum. Hence its relevance to this analysis.

It is important to emphasize at the outset, however, that mercantilist doctrine had as its immediate objective the formulation of economic policy. The development of theory had as its sole purpose justifying that agenda. These theorists did not proceed from grand explanatory theories logically developed in a deductive way, but worked almost in the opposite direction. By the same token these theorists concerned themselves with little outside the borders of their own nation; the move from "England's Treasure" (with which Thomas Mun concerned himself) to "The Wealth of Nations" (which would occupy Adam Smith) represented a broadening of intellectual horizons that betokened a different stage in the scientific formulation of economic theory, involving broader generalizations and expressly corresponding to distinct moments in the course of Western Europe's political and economic evolution.

Our interest here is merely to sketch the main outlines of the general doctrine in order to situate the role of mercantilist colonialism within it. Let us try to establish its essential features. The starting point, as we know, was the "metalist" idea—the identification of the level of wealth with the amount of gold and silver extant in each nation. Although the concept of wealth as identified with coinable metals was weighted disparately by the various thinkers who perfected the theory of mercantilism, the basic metalist idea oriented the political economy of each one. It involved a narrow conceptualization of the economic good and the supposition that profits are generated through the process of merchandise circulation, that is, that advantage necessarily results from losses suffered by one's trading partner. Not surprisingly, the mercantilist agenda tends directly toward maintaining a favorable balance—a favorable balance of contracts on the level of individual merchants and a favorable balance of trade on the level of international exchange. That was the means of promoting the entry of bullion that measured national wealth; hence, the adoption of a protectionist policy with primary emphasis on tariffs, and the stimulation of domestic production of those products most able to compete advantageously in the international market. Creating obstacles to the export of raw materials and boosting manufactured exports also followed; conversely, the policy fostered entry of raw materials and hindered or even banned imports of manufactures. The point of all of this was to lower the costs of internal production, with international competition as an end.

Mercantilism was not a political economy intent on social welfare. It aimed toward national development at all costs, legitimizing all manner of state stimuli and relying on state intervention to bring about lucrative conditions to enable enterprises to maximize the export of surpluses. This led to a policy fostering demographic expansion with an eye toward increasing the national labor force and impeding the rise of salaries.

Within this context one can easily view the position and significance of the colonies, their role being to constitute the metropoles' economic rear guard. While mercantilist policy, as practiced by the various modern states, took the form of unbridled competition with one another in Europe, there arose a need to reserve certain areas within which, by definition, mercantilist norms would be applicable. The colonies became guarantors of metropolitan self-sufficiency—which was the fundamental goal of mercantilist policy—thus permitting the colonizing state to compete advantageously with other powers.

The mercantilist notion, furthermore, did not emerge as an isolated element in the political and economic thought of theorists and statesmen. On the contrary, the belief was articulated in harmony with a body of ideas that developed and predominated in Europe during the period between the Discoveries and the Industrial Revolution. The colonizing project was tightly bound up, first of all, with the political principles of the absolutist era. The goal was clear. The powers' colonial politics sought to tailor colonial expansion to suit mercantilist aims; to cause relations between both poles of the system (metropolis-colony) to unfold in a manner consonant with the scheme. Even here, within this first description of the colonial system, we see that it reveals itself as a specific type of political relationship possessing two elements: a decision-making center (metropolis) and another area (the colony) that was subordinate. These political relations establish the institutional framework permitting the economic life of the metropolis to be fueled by colonial activities. If we are to plumb this long-term phenomenon more deeply, we will discover its connections with the very processes of modern colonization and other components of the totality. Such connections are not merely logically functional relations, but are constituted historically over time and in practice.

If overseas expansion and the colonization of the New World constitutes one of the most striking features of the sixteenth to the eighteenth centuries, one sees contemporaneously the predominance of absolutist systems in the political realm and, in the social sphere, the persistence of societies of "orders" founded upon juridical privileges. And within the universe of economic life, sometime between the gradual dissolution of feudal structures and the advent of capitalist production, there emerged (along with remnants of the former and elements peculiar to the latter) an intermediate stage that is commonly referred to as mercantile capitalism: For commercial capital, that is, capital generated most directly from the circulation of market goods, animated all economic life. The absolutist state, with its extreme centralization of royal power, which in certain ways unifies and disciplines a society organized into "orders," also executes a mercantilist policy encouraging the development of a market economy both internally and externally—externally by means of colonial development. Such were the parts of the whole that it behooves us to integrate. Truly, the relations between the unitary, centralized monarchy (or, earlier, between the *processes* of centralization and unification) and the adoption of mercantilist policies are clear. According to Eli F. Heckscher's formulation, mercantilism itself served as an instrument of that unification—albeit requiring a certain degree of national integration in order to emerge.[4] Their relations were, therefore, reversible, which leads us to believe that both emanate from a common source, namely, the critical process of transition out of the feudal structure. Similarly, overseas expansion allowed the breaching of those narrow limits that had constrained the movement of the mercantile economy up until the end of the Middle Ages.

It would be impractical, within the limits we've proposed, to attempt to include here an analysis of the crisis of feudalism. Let us simply state in passing, in agreement with the the analyses of Maurice Dobb, that on the whole, it arose not only from the commercial renaissance per se, but also from the manner in which the feudal structure reacted to the impact of the market economy.[5] The revival of commerce (i.eThe introduction of a strengthened mercantile sector into the economy and the development of an urban sector in the society) facilitated the gradual dissolution of servile bonds in some areas, while in others it furthered the entrenchment of servitude. We can note that first result in the areas adjacent to the large commercial routes, where the presence of the trader was a given. But in those areas where access to the market was limited to the upper strata of the feudal order, the reinforcement of servitude predominated. Thus, the development of the mercantile economy (with its correlated processes of division of labor and specialization of production) aggravated conditions of servitude—and in the end fostered peasant insurrections. Conversely, the enlargement of the market and increase of distances hastened the differentiating process within urban societies: The producer, no longer dominant in the marketplace, tended toward proletarianization—which in turn led ultimately to urban insurrections. Thus, the social crisis germinated in both rural and urban sectors.

To the extent that they disorganized production, the prolonged and persistent recurrence of these social crises tended in their turn to restrict the very development of commerce. These trends were even further aggravated by monetary depressions, for the European economies relied on the external supply of coinable metals. Such a situation led to a stiffening of competition among various commercial centers and a tendency to close off and dominate principal trade routes. As the principal commercial sector—the commerce in oriental products—was dominated by Italian merchants (mainly from Venice and Genoa), the other trading centers (Flemish, English, French, and Iberian) redoubled their efforts to open new routes.

It was within the general framework of these pressures and as a function of them, that the formation of nation-states took place. The advent of absolutist monarchies (with territorial unification and political centralization) was in fact a response to the crisis; or, better, the political redirection was brought on by multiple tensions. The centralized state, on the one hand, effectively promoted the stabilization of internal social order and, on the other, effectively stimulated transoceanic expansion designed to overcome the crises in the various sectors.

In any case, the opening up of new frontiers for mercantilist use and the establishment of new routes across uncharted seas involved unprecedented margins of risk and demanded, moreover, a previous accumulation of capital that would have been far beyond the organizational capabilities of the Middle Ages. The volume of resources to be mobilized, the uncertain profitability, the slow return of investment—all of these made inviable the tackling of the undertaking within medieval forms of mercantile associations. Only a centralized state could function as an organizing center to overcome such a crisis or crises, allowing the gathering of resources on a national and international scale. That was the only reason why a tiny, but precociously centralized Western European state—Portugal—was able to strike out across new routes, opening the way for Europe to circumvent these economic and social crises.

This point also illuminates the contours of European mercantile capitalism as it existed in Portugal during its early modern phase, and makes explicit the previous correspondence between the formation of nation-states and expansion across the seas. Portugal, Spain, the Netherlands, England, and France all sallied forth into the commercial and colonial contest in a measure proportional to their level of internal organization as unitary and centralized states. The rise of such states was an asynchronous process, the occurrence of which varied over both time and space, and each with its own form as a new player in the field of international relations. In its essentials and on the whole, however, this political process emerged from the tensions of feudalism indicated above. The leveling of all as subjects of the crown—which centralized all power in order to delegate it—allowed the disciplining and smoothing of tensions and social conflicts. This step coincided with the simultaneous prosecution of an active mercantilist economic policy, overcoming all impediments to the development of the market economy. Regaining the path toward economic expansion served, in its turn, to alleviate existing social tensions.

In truth, the modern state put in motion—with greater and lesser intensity, enjoying triumphs and suffering frustrations throughout its entire existence—a mercantilist economic policy. It simultaneously prescribed the abolition of internal custom duties and consequent integration of the national market, adopted rigidly protectionist foreign tariffs to promote a favorable balance of trade and the consequent influx of bullion, and established colonies to complement and autonomize the metropolitan economy. The consonance between this political economy and the phase of commercial capitalism subjacent to it was therefore perfect. Likewise, its application strengthened the absolutist state through royal fiscal policies that completed the network of interrelationships. That consonance, highlighted by W. Stark, substantially reduces the validity of the criticisms of mercantilism leveled by later theoreticians (beginning with the classical economists), who built on a conceptual system that largely ignored the historical place of mercantilist doctrine.[6] Absolutism, a society of orders, commercial capitalism, mercantilist policy, and overseas and colonial expansion were all parts of one whole—interacting within that complex that one could call, in keeping with the traditional term, the Old Regime.[7] These were, as a rule, correlated and interdependent processes, all of them products of the social tensions generated through the disintegration of feudalism and the gradual move toward a capitalist mode of production.

During this intermediate phase, in which expansion of mercantile relations tended to eclipse the manorial economy and foster the transition from a servile to a wage labor system, commercial capital commanded all economic transformations. But the mercantile bourgeoisie encountered all manner of obstacles to their maintenance of a rhythm of expanded activities and upward mobility. Thence arose the need for external supports—the colonial economies—to foster concentration in the economic sphere, and, in the sphere of politics, to aid the centralization of power that would unify the national market and mobilize developmental resources. In that sense, the political aspects of the Old Regime—that odd, apparent projection of state power above society—represented the mercantilist bourgeoisie's formula for securing conditions such as would guarantee their own upward mobility and create an institutional framework for the development of commercial capitalism. It meant, at root, simultaneously subordinating all to the king and redirecting royal policy to favor bourgeois progress so that, later, beginning with the French Revolution and from the nineteenth century on out, the bourgeoisie might become—as Charles Morazé would say—"all conquering," modeling society in its own image, according to its own interests, and in keeping with its own values. The strategy was not always explicit on the level of individual consciousness, and it was always fraught with countless difficulties. The history of the process is exceedingly tortuous, allowing Fernand Braudel to speak of the "betrayals" of the bourgeoisie.[8] But amid the contradictions surrounding the development of capitalist expansion and the rise of the bourgeoisie, that underlying mechanism—subjacent to the entire process—is too easily overlooked.

Within and inseparable from this context, one is able to focus on European transoceanic expansion and the formation of the New World colonies. Modern European colonization reveals itself in the first place as an intensification of a purely commercial expansion. The American lands were discovered during the course of opening up new trade routes for European mercantile capitalism, and the first activity undertaken was the barter for raw materials with the aborigines. Actual settlement was initially spurred by the need to guarantee possession in the face of disputes over the dividing up of the new continent. Production for European markets was a way of making these new domains viable. Almost imperceptibly, the shift from commerce to colonization was accomplished, although this development involved a new form of activity, a fact that did not escape the notice of the keener observers of the day.[9] In effect, during the transition from commerce to colonization there was a shift from the emphasis on commercializing goods produced by established societies toward the production of merchandise by a new society. So it was that the occupation, settling, and development of these new areas, as well as their integration into the European economy, were undertaken. In this way, economic activity eventually went beyond the field of circulation of merchandise to promote the implantation of complementary, extra-European economies; that is, it entered the orbit of production proper.

Notwithstanding such fundamental differences or the new dimensions that the colonizing activity acquired as it transcended its initial engagement in overseas trade, colonization kept within its essence that sense of commercial endeavor from which it emerged; only the nonexistence of marketable goods led to their production, and that, in turn, prompted colonizing activity. That was how the new areas adjusted themselves within the framework of European economic needs. Modern colonization, therefore, as incisively indicated by Caio Prado Júnior, has an essentially commercial nature: to produce for the foreign market and to furnish the European economies with tropical products and coinable metals—that, at root, was the "meaning of colonization."[10] If we combine this formulation—the commercial nature of early modern colonial endeavors—with the observations made earlier about the Old Regime—the intermediate stage between the disintegration of feudalism and the development of industrial capitalism—then our search for the real "meaning" of colonization will be well under way.

To summarize so far: The formation of a market economy in Europe began through the occasional sale of surpluses from premercantile production. To the extent that this commercialization became permanent, that sector of society dedicated to the acquisition of capital through the circulation of economic goods gained prominence. Bit by bit, and as a function of the same process, production exclusively for trade was introduced, as was specialization in production. Hence, the accumulation of commercial capital, the division of labor, mercantilization of economic goods, and specialization of production were all correlated processes involving a general raising of the economic level. The concentration of commercial capital and formation of the mercantile bourgeoisie were thus two facets of the same process.

Theoretically, the transformation was self-stimulating without limits. Historically, however, the launching of this process was connected to a concrete reality—the feudal system. From that reality derived the growth of social tensions beginning with the formation and expansion of a mercantile sector within the framework of the feudal economy; thence, also, the continuous political readjustments that channeled those tensions. The latter part of the Middle Ages represented a critical time because of these tensions and adjustments. The processes unleashed during the overcoming of this crisis included the creation of a unitary central state as executor of mercantilist policy, transoceanic and colonial expansion, and the creation of instruments to accelerate the development of a market economy, providing incentives for capital accumulation.

Eventually, capital was introduced into production. The expansion of the market economy, with its correlated processes of division of labor, specialization of production, and consequent raising of the level of productivity, only acquired a self-developing dynamic, however, with the emergence of mechanized industrial production. From artisanship to manufactures—where capital and labor were already dissociated—and on into the factory system there unfolds the process of forming capitalism, covering the entire period from the end of the Middle Ages through its completion with the Industrial Revolution.

As long as the last step remained to be taken, however, the commercial capitalist economy—and hence the rising mercantile bourgeoisie—still lacked sufficient internal growth capacity. The capitalism that resulted from the pure and simple workings of the market did not produce the transition to the decisive component—the mechanization of production. Hence arose the need for supports external to the system, inducing an accumulation that, because it was generated from outside the system, Marx referred to as original or primitive.[11] Hence also, toward the end of the eighteenth century, came the political and social tensions caused by the confluence of an entire complex of stimuli. Mercantilism was, in essence, the confirmation of the system's need, and the mercantilist colonial structure was one of the economy's fundamental parts; a lever for the emergence of modern capitalism. Contrary to what Max Weber believed, colonial exploration was among the decisive elements in the creation of the prerequisites for industrial capitalism.[12] In fact, the taking of that ultimate and decisive step in the transition to the capitalist order required, on the one hand, ample accumulation of capital on the part of the business class, and, on the other, a steady expansion of the consumer market for manufactured goods. To be sure, both of these prerequisites were generated by the process of developing a market economy proper. As we have seen, however, the pure form of this mechanism ran into immovable obstacles, the overcoming of which summoned forth the colonial system and mercantilist policy.

When examined in this context then, the colonization of the New World in early modern times reveals itself as a cog in a system, as the instrument of primitive accumulation within the era of merchant capitalism. That which, at the outset of these considerations, appeared to be merely a project, an idea, now presents itself as intimately consonant with the actual historical process of forming capitalism and bourgeois society. One also appreciates the deeper dimensions of colonization: both *commercial* and *capitalistic*—in the sense of being an essential formative element in modern industrial capitalism.

We can now finally comprehend the colonial system in its multiplicity of connections. This set of mechanisms—whether examined in the rules of political economy or in actual economic relations—integrates and links colonization with the central European economies, representing an immanent and subjacent reality underlying the colonizing process and constantly steering its outcome. It was not merely a common denominator present in all concrete manifestations of the historic process, but, rather, the structural determinant itself, that component that makes it possible to comprehend the sum total of manifestations, making reality intelligible—the element that finally explains and defines the others—but is not itself defined by them.

In the real world, colonization does not unfold strictly within the frame of the colonial system. Such systems never present themselves, historically speaking, in their pure form. Albeit coeval, the colonization of New England took place outside of the mercantilist colonial system's defining mechanisms. As we have indicated elsewhere, specific factors—the English politico-religious crises, occurring as they did during the formation of the modern English state—gave rise to a particular form of transoceanic expansion: settlement colonies (to use the terminology consecrated by Leroy-Beaulieu).[13] Based predominantly on small properties, their production mainly responded to the colonies' own internal consumption. In contraposition to these, the category of colonies Leroy-Beaulieu called exploitation colonies, whose production organized itself in terms of large slaveholding properties (as, for example, in Brazil), had economies completely turned back toward the external, metropolitan market. During the course of our exposition, these colonies have assumed new and easily discernible dimensions: the exploitation colonies were those best adjusted to the framework of the colonial system. The settlement colonies were those that remained relatively peripheral to that system. Yet in order for the explanatory scheme we're developing to be true, what with both types of colonies being generated from within the same colonizing process, the whole, and hence the settlement colonies as well, must be understandable in terms of that system, rather than the other way around. We will get to that in due time.

Similarly, if colonial Brazil was framed along the lines of the Old Colonial System as an exploitation colony, that does not mean that all colonial manifestations of Portuguese America directly expressed that mechanism. Rather, the mercantilist colonial system's mechanisms constitute elements fundamental to the whole, in terms of which it ought to be analyzed. At this early point in our analysis, however, we are trying to render explicit the basic category (the colonial system) in order then to comprehend its mechanisms and to study its crisis on a structural level. Naturally, we will further on have to take up some of the elements advanced here in order to redefine the positions of metropolitan Portugal and colonial Brazil within the entirety of the system. Thus, our analysis will become more concrete as we go along.

The Metropolitan "Exclusive"

Let us now examine the functional mechanisms of mercantilism's Old Colonial System. The essential element underlying this system lay within the regime of commerce occurring between metropolises and colonies. In reserving to themselves exclusive overseas commercial rights, the European metropolises organized an institutional framework of relations that stimulated the primitive accumulation of capital in the metropolitan economy at the expense of the peripheral colonial economies. The so-called colonial monopoly, or, more correctly and using a term of that era, the metropolitan "exclusive," made up the systemic mechanism par excellence through which colonial expansion was adjusted to the economic processes of European societies during their transition to capitalism.

Commerce was in fact the nervous system of the Old Regime's colonization. That is, the occupation, settling, and development of new areas were undertaken in order to foster mercantile activities. Along with the increasing mercantilization of various productive sectors in Europe and a widening circulation of merchandise there, colonial production on the peripheries of the European dynamic center was also mercantile production closely connected to the major international commercial routes. That alone would suffice to indicate the significance of colonization as a stimulating adjunct of mercantile capitalism. Colonial commerce was the metropolis's exclusive commerce—and it generated huge profits, an aspect that completes the characterization. Despite all the variations that colonial-metropolitan relations underwent during the course of the sixteenth through the eighteenth centuries, commerce was always the basic matrix of these relations, encompassing situations that diverge from this typical process only as variations arising from special factors or circumstances. The commerce that developed through the opening up of new maritime routes at the beginning of the early modern period was effectively exclusive. Throughout the course of Portuguese expansion during the 1400s, exploitation of commerce along the African Atlantic coast was the prerogative of the king alone, that is, of the absolute monarchist state, although he could delegate it to others.[14] Among these recipients figured the Order of Christ, personified by its Grand Master the Infante Prince Henry, as well as private and even foreign merchants. Still, the regime's basic exclusive principle never strayed, nor did the underlying mechanisms ever stop functioning.

The rounding of the Cape of Good Hope presented the Portuguese with the possibility of opening up commerce along the African and Asiatic shores of the Indian Ocean. These worthies then erected a military-political complex, the Portuguese vice-royalty of India, in order to exclude the Mussulmans and, through them, the Italians from participation in those mercantile activities. In other words, a coercive apparatus was organized in order to guarantee the monopolization, and hence the high profitability, of the route around the Cape. It amounted to an attempt to block off the entrances to the Red Sea and the Persian Gulf. Commerce was thus organized as a royal monopoly with the King of Portugal as the sole agent. Resources for the commercialization of oriental products were mobilized through the agency of the state. However, the scarcity of capital in Portugal alluded to earlier led the Portuguese crown to resort to foreign capital, especially that of Flanders, and so to transfer the European commercialization of oriental products into Antwerp's hands. This lent these Flemish entrepreneurial groups greater control over European prices. Their manipulation of prices, in turn, nudged them ever more into the capacity of financiers and creditors for royal undertakings; leaving the Portuguese crown to assume the not insignificant risks of transportation. In addition, the profits kept by the crown, on being integrated with the other sources of royal treasure, were not necessarily reinvested in oriental dealings, but were often diverted to attend to other expenses incurred by the Portuguese state. Thus, the "monarchic capitalist" scheme ended up frustrating the rationality of commercial enterprise in oriental products, greatly weakening the Portuguese position on the whole, and finally giving rise to bankruptcies and failures.[15]

One may nevertheless observe that such distortions took place on the level of distribution of profits generated through monopolized commerce. The essential aim was that there not be competition among buyers in the Orient, which would reduce the profits to their normal value in commercial transactions. The Portuguese royal monopoly thus guaranteed conditions favorable to the European economy in general, thereby promoting the acceleration of mercantile capital accumulation. Within the actual workings of the system, however, the bulk of its advantages were transferred outside the kingdom. With that, Portuguese domination in the Indies weakened in the end, resulting in a diminution of the volume of its commercial activity.

The Portuguese retreat facilitated the entry of the Dutch in the early seventeenth century. Despite the Dutch War of Independence (beginning in 1579 with the Union of Utrecht) and the annexation of Portugal by Spain in 1580, strong Dutch participation in oriental trade continued by way of Lisbon. In 1585, however, the year the Spaniards captured Antwerp, Dutch ships were apprehended in Lisbon. Even then, Dutch entrepôts were so bound up with and important to oriental commerce that Phillip n made a last-ditch effort to avert the breaking off of trade relations. Still, by 1598 all trade with Holland was prohibited with the passage of the impoundment decree—described by Grotius as a “barbaric edict.”[16] By this time the Dutch were already organizing the launching of direct commercial relations with the Orient. They mobilized their resources, and, in April of 1595, they made their first voyage. Although the compensation from this effort was rather paltry, the route to India, at least for the Dutch, was now open.

The Netherlands, within the context of the European economies, now found themselves in a peculiar position. Ever since the Middle Ages the region had figured prominently as one of the most active centers of development for the European merchant economy. Bruges, in the Lower Middle Ages, and Antwerp, beginning with the sixteenth century, had been economic and financial centers rivaling the Italian cities.[17] Flemish wealth arose as a consequence of its position as an entrepôt for transfer and distribution of products from various European economic regions; in sum, of its carrying trade. Its economic policy tended toward the lightest possible regulation in a spirit of grand liberalism in order to attract, and then redistribute, merchandise from all areas. In this manner and rooted in this tradition, in the latter part of the sixteenth century the Dutch organized many autonomous companies in efforts to trade directly with the Orient. Between 1595 and 1602 some ten companies were formed, deploying sixty-five ships. Few enjoyed success. For the majority, the results were disastrous. They ended up competing with one another in the purchase of oriental products. Their situation was further aggravated by the peculiar conditions attending such long-distance commerce in a region made hazardous by the monsoons of the Indian Ocean.

The need for a change in economic policy with respect to oriental trade became obvious. The Amsterdam Company, having done fairly well, petitioned the Estates General for a monopoly concession over this sector of Dutch trade. The petition was denied, and this action touched off heated debates and polemics until finally the monopoly was imposed with the charter of the East Indies Company (March 20, 1602), guaranteeing it exclusive mercantile activities in the Orient (between the Cape of Good Hope and the Straits of Magellan), with the right to sign agreements, name functionaries, and the like.

This Dutch experience is thus highly significant for the explanation of the mechanism we are analyzing, effectively offering a counterproof. The free practice of overseas trade, having been tried, was found ineffective for the requirements of European mercantile capitalism in need of external stimuli; the failure of the attempt led, in practice, to the adoption of a monopolist scheme.

It was within the context of monopolist overseas exploitation that colonial production was begun, and from it the commercialization of products generated within the New World. The earliest exercise in colonization proper took place, as is known, in the Atlantic islands—particularly on the island of Madeira. The cultivation of cane and production of sugar were introduced to these islands during a phase when the resources of the small entrepreneurial kingdom of Portugal were concentrated on circumnavigating Africa. From the outset, therefore, this colonizing effort depended on the participation of foreign resources and capital. The Genoese, it seems, were foremost among those connected with setting up this new economy, an economy by means of which the Venetian monopoly in certain products was being broken. Then, with the breakup of that monopoly, there came an attendant increase in consumption of sugar that was eventually serviced by the Dutch; by the last quarter of the fifteenth century a state of overproduction had clearly been reached, bringing on the restrictive measures instated by Manuel I, who in 1498 fixed maximum production at 120,000 *arrobas* annually, of which 40,000 went to the Netherlands.[18]

Even earlier, however, in 1482, amid the airing of numerous complaints in the Portuguese *cortes* of Évora about the economic activities of "foreign residents, such as the English, Flemish, Castillians, and Genoese" who caused "great damage to the people of thy kingdom" and "bring great impairment of thy taxes," the situation on the islands was being seriously criticized. Remembering that Prince Henry, the "inventor" of those islands, had not condoned the presence of foreigners there and had insisted that island products come first to the kingdom, paying the duties and yielding freight rates for national ships, only then being shipped abroad, the *cortes* decried the concessions that now permitted the residence of foreigners on the islands, concessions that resulted in the direct transport of goods outside of the kingdom (during 1480, twenty Spanish ships and forty or fifty from other nations had done so). The alleged loss of royal duties "both on entering and leaving" and large losses borne by the people prompted a petition to "determine, your Lordship, and uphold that foreigners not be countenanced as residents on said islands, nor allowed to load ships outside of the kingdom, and that all sugars and other merchandise come to Lisbon or to other ports in thy realm where they may be unloaded and from thence carried by whom you approve to whence they will, rendering payment upon departure." This "will be a great advantage to thy revenues and a great benefit for the common good," for otherwise there will be a "loss of shipping" in Lisbon and "other places in Portugal."[19] The interests of Portugal's mercantile bourgeoisie could not have been more clearly put than in these complaints.

The proposal amounted to an appeal for the restructuring of the Atlantic islands' colonization into the framework of monopolist overseas exploitation. Once again, the exclusivist logic of colonization is made clear. As a consequence of these demands, the residence of foreigners on the colonized islands was indeed forbidden, allowing those residing there a period of one year within which to leave. One observes, then, the policy astutely followed by the Portuguese crown: free trade in the initial stage to stimulate the entry of resources and capital for the installation of colonial production; restructuring into the exclusivist system once the peripheral economy had begun functioning fully.

The implantation of the sugar economy in Brazil featured, after a fashion, a repetition of the process. During the first purely predatory economic contact, nothing beyond the commercialization of natural products —the bartering for brasilwood with the aborigines —was tried. Such commerce was at the outset considered a "monopoly" of the crown, which delegated it to the recently converted New Christian entrepreneur Fernando de Noronha or Loronha. It amounted, then, to a simple unfolding in the Americas of the regime already applied to African and Indian commerce. During the transition to colonization, that is, in the introduction of cane cultivation and sugar refining, the king resorted to private entrepreneurs through the concessions of captaincies whose charters still perpetuated the principle of royal monopoly. We know that few of these licensees enjoyed success—as did Duarte Coelho in Pernambuco—in the difficult business of installing costly agro-industries in Portuguese America. None of this gainsays the hypothesis advanced by Celso Furtado that during this arduous phase recourse had to be made to foreign capitalists, especially Dutch, as they were already heavily involved in European sugar dealings—although monographic studies have not yet fully validated that affirmation.[20] It is nevertheless correct that during this early phase the commerce in goods was relatively free. There are even reports of licenses for direct commerce to foreign ports.

The sugar economy expanded in this manner so that in the decade of the 1560s Brazil already boasted 60 mills, producing some 180,000 *arrobas*. The greatest upswing, however, occurred during the final quarter of the sixteenth century and the first decade of the 1600s. Calculations indicate that in 1610 there were already some 650 mills in existence, the surge in production corresponding with an accentuated upward movement of prices. The sugar-price curve for Lisbon reveals remarkable increases, but, as noted by Frédéric Mauro, in Brazil prices remained nearly stable.[21] This was because at the opening of the prosperous phase, King Sebastian decreed (February 3, 1571) the exclusivity of Portuguese shipping in the then-flowering colony. One notes the coincidence between the decree and the boom of the Brazilian sugar economy; it was, in essence, the framing of the new peripheral economy within the structural lines of the colonial system. One also notes that the end of the sixteenth century was marked by intensified repression of foreign commerce and multiplying seizures of foreign ships.

It is quite true that external pressure was mounting at the time and that the Spanish monarchy [to which Portugal and thus Brazil were now subjugated] was struggling with enormous financial difficulties. This led the King of Spain and Portugal, despite new prohibitions (for example, of February 9, 1591), to concede some special licenses—to the point of permitting direct regular trade between Brazil and Hamburg, which sent nineteen ships between 1590 and 1602. But after that time, all indications are that direct voyages to non-Portuguese ports ceased. Let us immediately emphasize here, however, that these licenses in no way altered the fundamental mechanism we are exploring. Such concessions did not imply the establishment of competition among buyers. One may legitimately affirm, as substantiated by price records, that along with the rapid growth of the sugar economy we also witness its reshaping along the lines of the colonial system. Prices rose little in the colony, but increases were sharply noticeable in the metropolis, that is, excessive profits were generated—monopolistic profits—that accumulated among metropolitan merchants.

Repercussions of the intensifying clashes in the war between Spain and Holland were clearly felt by the commerce to Brazil. Repeated prohibitions attest to the increasing pressure of smugglers. Thus, in January of 1605 restrictions were imposed again on foreigners seeking to enter Brazil or, rather, on their ships, obliging the petitioners to submit their proposals to the Council of the Indies itself, whose president would sign a passport if the petition were conceded. New restrictions were enacted on March 18,1605: no foreign ship of whatever nationality could go to Brazil, India, Guinea, and the Atlantic islands, nor to any other lands either discovered or yet to be, excepting only Madeira and the Azores; all foreigners residing in overseas Portuguese territories were required to move to Portugal within a year or face the penalties of death and confiscation of property. That this legislation in itself was naturally impotent to maintain the Portuguese monopoly—which really depended on military conditions to oppose pressure from Holland—does not make the adoption of an exclusivist commercial regime any less patent. These principles were incorporated into the *Philippine Ordinances* of 1603.[22] Smuggling certainly did not cease, but the decision on the part of the low countries to set up a special company to deal with the West Indies and to organize the military occupation of the sugar producing northeast of Brazil shows that smuggling did not suffice to satisfy the expansive needs of the Dutch economy.

The restoration of Portuguese independence from Spain (1640) marked a temporary diminution of Portuguese overseas exclusivism. The internal political situation faced by the new government and the weak Portuguese position internationally explain the concessions made to Holland and England in exchange for alliances in the struggle against Spain. It was exactly because the Portuguese colonization of Brazil was by that time already structured within the functional lines of the colonial system that the concession to foreigners of the right to participate became a powerful coin with which metropolitan Portugal could bargain in its anti-Spanish schemes. The concessions contained in the treaties with England (1654) and Holland (1641) amounted at root to the participation by these countries in the fruits of exploitation by the Portuguese colonial system.

From another angle and along similar lines, the Portuguese government sought to organize its system of overseas control more efficiently, mainly through the creation of the Overseas Council, which came to oversee all colonial activity. It was an effort to exercise as much control as possible over concessions already granted. Similar considerations prompted the institution of the monopolistic General Commerce Company for Brazil in 1649.

From then on, amid increasing colonial competition among the powers, the Portuguese crown struggled diligently to minimize the breaches of its colonial monopoly. In a petition for redress of grievances in 1672, Portuguese merchants loudly sought reparations, for they were finding the Brazilian markets saturated when their ships arrived there. The Edict of November 27, 1684, forbade ships departing Brazilian shores from proceeding to any ports other than Portuguese ones. The Royal Order of February 8,1711, in the same vein, established that foreign ships (those admitted by treaty) could only go to Brazil in the official fleets or in cases of forced landings, and prescribed rigorous penalties for infractions. One measure followed another, gradually canceling out the concessions to foreigners, until their legal presence was reduced to cases of forced landings only. The process culminated with the Edicts of June 19, 1772, and December 12, 1772, which, revoking the concessions of 1765 and 1766, prohibited all intercolonial commerce while stating that it was "a generally accepted maxim constantly practiced among all nations, that Commerce and Navigation to the Colonies should be made from the Capital, or Dominant Metropolis, and not among the colonies themselves."

If we now examine, albeit more succinctly, the economic relations established during the process of Spanish colonization in America, we find ourselves faced with the same principles and the same mechanisms. The Castilian colonial enterprise surfaced initially as an exclusive business of the crown, associated with Christopher Columbus. The widening of the enterprise, while necessarily reducing the audacious discoverer to a position of insignificance, consolidated the royal monopoly, which naturally embraced its Castilian subjects. In reality, beginning with the institution in 1503 of the Sevillian Casa de Contratación, all legal commerce with Hispanic America came to be done through the Andalucian port. This was the single-port regime that was only altered at the end of the eighteenth century under the enlightened despotism of Charles III's ministers. That important Sevillian organ, despite having been subordinated since 1524 to the Royal and Supreme Council of the Indies, superintended all colonial traffic, vigilantly safeguarding the monopoly. External pressure, in the form of piracy and harrying unleashed by rivals who by the first half of the sixteenth century were already equipping themselves for overseas competition, brought on a stiffening of the regime. Already in 1543 and more so between 1564 and 1566, navigation was limited to convoys—"fleets of galleons"—sailing during specific seasons along predetermined routes to a few privileged ports in the Americas from which proceeded the distribution of metropolitan products. Veracruz in New Spain, Cartagena on Tierra Firme, Panama and Porto Bello on the Isthmus were the privileged centers. One result, for example, was that the provisioning of Buenos Aires and the Río de la Plata River basin had to be done exclusively by way of the Pacific. The result of the Sevillian merchants' monopoly or that of their associates was, in Professor Céspedes del Castillo's synthetic formulation, "a regime of large profits [for Spain] that determined a regime of high prices in the Indies."[23] There is no doubt that Spanish colonization, like the Portuguese and the Dutch, was organized along the lines of the mercantilist colonial system, which tended to set up mechanisms designed to accelerate primitive capital accumulation in Europe. The fact that Spain proved unable to reap its advantages—that they ended up being transferred to rival powers—stems from conditions peculiar to the metropolitan situation.

Clearly, a regime given to such single-minded inflexibility had to provoke immediately the defiance of rival powers, who hastened to provide incentives for smuggling into Hispanic America. Beginning in colonial Brazil itself, an enormous trade in illegal commerce soon developed into the Río de la Plata region, especially during the period of the Iberian Union. Englishmen, Frenchmen, and Dutchmen gave the exclusivist Castilians no respite until, in the seventeenth century, having ensconced themselves in the Antilles, they erected competing colonial economies while setting up entrepôts to stimulate traffic in contraband to the Indies of Castile. The Spanish system offered its enemies several enormous flanks, the most important of which was certainly the traffic in black slaves to the Hispano-American colonies. The difficulties in setting up African posts led the Spanish crown to subcontract the provisioning of their colonies to foreign merchants through the *asiento.* Competition for this highly lucrative overseas traffic was especially violent; the Portuguese, Dutch, and French successively controlled the *asiento,* which was finally awarded to the English through the Treaty of Utrecht (1713). It is well to keep in mind that contraband does not negate the reality of the colonial system. What the entrepreneurs from rival powers sought was precisely the reaping of advantages inherent in this system. This truth is underscored by the fact that the colonial policy of these same powers (Holland, France, England) never wavered in its adherence to that same policy that had crystallized during the first phase of transoceanic expansion.

Overseas competition, undertaken at the outset on a purely commercial level, soon unfolded, as we have seen, into a veritable colonial competition with the installation of the English, French, and Dutch colonies. We have already dealt, albeit summarily, with the Dutch experience: their commitment to the establishment of direct trade routes to the Orient, an effort that led to their organization of a monopolistic trading company. Dutch dominance in the Orient soon transcended the stage of a purely mercantile action. Occupation of large islands such as Java and Sumatra gave way to a colonizing effort, shifting to the production of spices. The undertakings were still executed, however, within the monopolistic framework of the powerful East Indies Company. Their scheme for western expansion—to the West Indies — was no different: being set in motion through the agency of the West Indies Company, a clone of the first. Under its guidance and control, in addition to the temporary domination of the Brazilian Northeast, it also promoted the occupation and exploration of Surinam and Curaçao.

English maritime expansion, for its part, also adhered closely to formulated mercantilist principles. We've already mentioned Thomas Mun, defender of the British East Indies Company. He was followed by an entire dynasty of theoreticians (Josiah Child, Joshua Gee, Malachy Postlethwayt, to name a few of the most representative) who carried mercantilist doctrine to the highest degree of refinement, and, within it, the theory of the colonial system. English colonization itself exhibited the most variegated hues and aspects, at times assuming inconsistent forms, but Great Britain nevertheless prevailed in colonial competition to become, in the nineteenth century, the imperial power par excellence. In the early phase (during the sixteenth century), it embarked, along with Holland and France, on a parasitic venture: the plunder of Spanish colonial trade. The beginning of the seventeenth century marked its actual colonial expansion in several directions, including channeling dissident groups formed during the political and religious crises—in the midst of which the formation of the modern English state took place—into North America. This action gave rise to a pattern of colonization—the settlement colonies—different from that of the general European framework. But, finally, in the middle of the seventeenth century, "plantations" were set up in the Antilles.

The English "Old Colonial System" was given legal expression by the famous Acts of Navigation. The Act of 1651, under Cromwell, established that American, Asian, and African products could be carried to England only by English ships or those of English colonies. European products were admitted only aboard English ships or those from the country in which the products originated—a clause that excluded Dutch intermediary carrying trade. Exceptions were made, as for Italian silk, which was admitted from Flemish ports, and for products from the Spanish and Portuguese colonies, which could be imported from Spain. Note that the exception indicates a harmony of interests with Portugal and Spain, for England effectively had an interest in these imports— imports that, in a complementary manner, made it possible for British manufactures to reach Latin American markets by way of the metropolises. Another aspect worth mentioning in the Cromwell Act was the integration of measures encompassing overseas colonization as a whole (products from America, Asia, and Africa) in a single act, along with regulations concerning English trade with other European powers— doubtless, indications of the coherence of mercantilist policy, of which the colonial system forms only a part, albeit a central one.

The Act of 1660, enacted during the Restoration, underscores the persistence of English mercantilist policy in the wake of Cromwell's fall from power. It defined as English those ships whose captain, along with three-fourths of the crew, were English. It also specified that products from English colonies could be carried only by those ships, reaffirming an earlier ruling. Indeed, it established the "enumerated articles" that could leave British colonies only if bound for either England or other English colonies. These were the staple products of transoceanic commerce: sugar, indigo, cotton, tobacco, and timber. Three years later the "Staple Act" (1663) forbade the colonies from importing on ships that had not docked at English ports, opening exceptions for Madeira wine, French salt, and Scottish and Irish horses. Another Act, in 1673, taxed the enumerated articles that circulated from one colony to another. The system was reaffirmed in 1696 in an Act purporting to "prevent fraud and regular abuses in colonial commerce" (i.e., plantation trade).[24]

For France, the early phase of maritime expansion was characterized, as for England and the United Provinces, by piracy and harrying. Some ill-fated attempts at overseas occupation and settlement did occur in the meantime, but only under Richelieu (1624-1642) was expansion given new momentum, yielding its first rewards. Monopolistic new companies were created to further overseas expansion. The results achieved by such companies in New France (1627), the islands of America (1635), Senegambia (1641), and in the Orient (1642), although not brilliant, nevertheless established the first bases. Under Jean Baptiste Colbert (1669-1683), French mercantilism—or Colbertism, as it came to be called—was structured as a wide-ranging plan, simultaneously affecting all sectors of the national economy and then providing the most complete example of the simultaneous application of mercantilist policy. Overseas and colonial expansion was thus organized within the framework of the monopolist scheme. Colbert reapplied Richelieu's policies, reorganizing the privileged companies and gave them new and decisive momentum. Accordingly, the East Indies Company, the West Indies Company, and the Senegal and Guinea Companies retained their exclusive rights over the various areas of French overseas commerce (trade in oriental products, colonial products, slave trade, etc.), and it was within this context that French colonization took root.

By the second half of the seventeenth century, as colonial competition among the European powers was defined and crystallized, we find overseas development organized within a commercial regime that, despite minor variations and fluctuations, everywhere displayed at root the same fundamental mechanism. All of the processes operated within the same basic exclusivist system. The tensions of competition, the struggle among the powers, the smuggling—none of this negated that system. If we visualize it in conjunction—on one side, European mercantile capitalism during its rapid expansion phase and, on the other, the peripheral colonial economies—we restate, in essence, the system of exploitation of the latter by the former. The conflicts among the various Old World nations arose precisely over the reaping of their advantages and the redistribution of commercial and colonial profits.

We focus, then, on the basic mechanism of the commercial regime; the axis of the mercantilist colonial system. The metropolitan "exclusive" over colonial commerce consists, in sum, of the reservation of the colonial market for the metropolis, that is, for the metropolitan commercial bourgeoisie. This was the fundamental mechanism, generating excess profits, colonial profits. Through it, the central metropolitan economy incorporated the surplus products of the ancillary colonial economies. By retaining exclusive purchase rights for colonial products, merchants from the homeland were able to depress colonial prices to a level below which the continuation of the productive process would have become impossible, that is, toward the level of production costs. On the other hand, resale in the metropolis, where they enjoyed exclusive selling rights, guaranteed them excess profits too; thus, they benefited on both sides—in purchase and in resale. This promoted, on the one hand, a transfer of real income from the colony to the metropolis, as well as the concentration of this capital among the merchant classes connected to overseas commerce. Conversely, the possessors of exclusive sales privileges over European products shipped to colonial markets were able to resell in the colonies at high prices, prices above which consumption would have become impracticable. Here, then, was a reiteration of the same mechanism stimulating the primitive accumulation of capital by merchandisers in the homeland. Further on, we will analyze other aspects that will enable us fully to comprehend this process of original accumulation in all its dimensions; in the meantime, let us simply state that we will argue that the socioeconomic structure being organized in the colonies—slave-based production and the ensuing concentration of income in the dominant strata—was what made possible the functioning of the entire system.

But here let us further particularize the mechanism whose exclusivist essence is described above. The metropolitan "exclusive," just as the subordination of the colony, could assume many gradations, complicating the scheme in many ways. It is true that the "exclusive" over maritime trade could, in the extreme case, belong to a single business man; as in the case, for example, of royal monopolies granted to special contractors or even retained by the Portuguese king himself, as was true during the earliest phase of oriental commerce. In this circumstance, the sole entrepreneur retained an exclusive right over the purchase of external products, that is, of their procurement in the colonial market (here we speak, in technical terms, of a "monopsony"). He also retained, naturally, an exclusive right over the sale of the product in the central economy (a "monopoly," technically speaking). The most common arrangement, however, was for exclusive access to colonial commerce to accrue to the metropolitan mercantile business class as a group. In the colony, this group retained exclusiveness in procuring colonial products (that is, "oligopsony"), as it did in the sale of European products in the colonial markets ("oligopoly"). The situation typifying the colonial system, were we to classify it technically, would then be that of an "oligopsony-oligopoly" or "bilateral oligopoly." Intermediate between the sole agent and the entire class of metropolitan merchants, the exclusiveness could remain restricted to a more specific group of metropolitan businessmen, as in the Spanish single-port system, which favored those merchants linked to Sevillian commerce. Colonial trading companies also figured in this intermediate position: for in reality they included only a fraction of the metropolitan merchants.

In the metropolitan markets the situation could, in its turn, also vary. If the group connected with overseas commerce sold colonial products under conditions of monopoly or oligopoly (naturally, at high prices), this promoted a transfer of income from the population of the homeland as a whole to the entrepreneurs involved in colonial commerce. If they resold these products in another country under the same conditions, the transfer of resources was made from outside the national borders to the inside, always concentrating in the same privileged caste; if, however, the same was done under conditions of competition with other nations, this avenue of accumulation declined or could go to other nations. Likewise, the purchase of European products for provisioning the colony could be accomplished under more or less favorable conditions. If the products for provisioning the colony were acquired outside the metropolis, as when the metropolis failed to provision the colonies itself, this avenue of accumulation naturally tended to become blocked.

Some objections to this line of interpretation can still be made. They involve those mechanisms that operated throughout the span of the entire Modern Era, and that, according to some authors,[25] would counteract the functioning of the system: treaties conceding overseas commercial advantages to other powers, licensing of foreign merchants, and, finally, contraband. In our view, nevertheless, such occurrences do not invalidate, but rather confirm our analysis. In fact, such licenses and concessions presuppose that the mechanism of colonial exploitation generates excess profits. Otherwise, what would one really be conceding? If a monarch in need of financial resources eventually sold licenses to foreign merchants, or if a metropolitan state, because of political necessity, permitted merchants from other nations to trade in their colonies (as did Portugal, in the wake of the Restoration)—what was really happening was a transfer of the advantages of the colonial system's economic stimuli. This did not establish real competition. It was, rather, the very possibility of more highly lucrative commerce that made such licenses and concessions so desirable, to the point of wars being fought to obtain them.

Contraband, to be sure, involved a more complex situation, but, as concerns our analysis, is confirmatory nonetheless. It is obvious that smuggling always involved serious risks: imprisonment, confiscation of merchandise and ships, and so on. What could move merchants to take such risks and apply themselves to illegal trade—if not the prospect of colonial superprofits? Contraband, then, also presupposes the basic mechanism rather than negates it. In order to find an area for his activities, the smuggler must certainly offer somewhat better prices for colonial products, as well as offer European products at lower prices than metropolitan merchants; but never at a level implying perfect commercial competition, for otherwise, what would compensate him for the high risks? Capital would then be channeled to other areas of equal profitability and smaller risk. So it seems certain that although smuggling may have been a palliative, it did not imply the end of the system. The basic exclusivist mechanism always persisted as the explanatory element of all this movement.

In sum, licenses, concessions, contraband, all seem to us phenomena best relegated to the area of disputes among the various European metropolises aimed at appropriating the advantages of colonial exploitation. And this exploitation operated throughout the system, that is, in all the relations between the European central economy and the peripheral colonial economies. None undermined the essence of the system of colonial exploitation. They were all variations of its fundamental element.

In the end, the regime of colonial commerce—that is, metropolitan exclusiveness over colonial commerce—constituted throughout the sixteenth, seventeenth, and eighteenth centuries the mechanism through which the metropolitan merchants appropriated the excess profits generated in the colonial economies. Accordingly, then, the functioning of the colonial system impelled the primitive accumulation of capital within the framework of European mercantile capitalism. With such a mechanism, the colonial system adjusted the process of colonization to its own purpose in the economic and social history of the modern era.

The Colonial Economy, Slavery, and the Slave Trade

The analysis we have been sketching out of the Old Colonial System cannot be complete without studying, however summarily, the type of economy organized in the colonies. We've already seen that the guidance provided by the broad outlines of the colonial structure is indispensable to an understanding of all the broader mechanisms encompassed in overseas exploitation. By the same token, the starting point for the characterization of the colonial economy is the larger meaning of colonization and the basic mechanisms underlying metropolitan-colonial relations. European expansion and the organization of the New World's productive activities effectively proceeded from, and as a function of, that underlying purpose. To repeat, the occupation, settlement, and economic development of the new areas developed within the framework of Old Regime commercial capitalism and as a function of the mechanisms and adjustments inherent in that formative phase of modern capitalism. Essentially, European colonial expansion developed according to a fundamental impulse generated by tensions emanating from the slow transition to industrial capitalism in Europe. The acceleration of primitive capital accumulation is, then, the direction of the motion—not present in all its manifestations, but immanent in the entire process.

In this sense, colonial production was necessarily oriented toward those products capable of fulfilling the Old Colonial System's function within the context of merchant capitalism: commodities saleable in the central economy for which potential or manifest demand could be found in European society. These were mainly tropical products: sugar, tobacco, cotton, cocoa, indigo; or raw materials such as furs for luxury clothes, dye-bearing woods, and so on. Beyond those, naturally, they produced coinable metals, lest the expansion of the market economy be constrained by scarcity of currency.

It bears repeating also that the earliest attempt at colonization, in the Atlantic islands, began very early under the direct leadership of Prince Henry, who sent over the first settlers. The initial idea seems to have been to populate these strategically located islands in order to maintain possession of them, while at the same time trying to keep Portuguese routes and discoveries secret. This resulted initially in the organization of an economy oriented primarily toward the pioneers' own consumption, albeit with a little exportation to the metropolis of much-needed cereal grains. Not long thereafter, however, the island economy turned toward the external market, aiming toward Portugal and, soon after that, toward the European market in general. The introduction of the sugar industry, especially on Madeira, and its rapid diffusion, led, little by little, to productive activities tying into an expanding European commerce. With the development of a sugar economy in Brazil, viticulture, which had begun in the latter part of the fifteenth century, came to dominate production on Madeira.

Likewise in Brazil, colonization proper (occupation, settlement, and development) was shaped from the outset by preoccupations mainly political in nature: aiming, through peopling, to retain possessions already being disputed by Dutch, English, and French corsairs. However, advice about this goal presented to King John III (by Diogo de Gouveia, among others) pointed already to the example of the Atlantic islands.[26] With the inception of colonization, the charters granting captaincies visibly aimed at agriculture: the earliest donatories received the specific privilege of building and possessing waterwheels and sugar mills. In this manner, the colonization of Portuguese America was functionally organized from the beginning around production for European markets, and so it developed throughout the sixteenth century.

When the Iberian nations lost their privileged position overseas and colonial competition became general, we witness the same adjustment of colonial expansion to the functional lines of the system. At first the Dutch, English, and French assault on the Castilian Antilles, as we've seen, was directed at establishing beachheads from which to pressure the Spanish colonial system. By the middle of the seventeenth century one notes, there too, a change in course: With the introduction of the sugar economy, the islands of the "American Mediterranean" organized themselves into producers for European markets.

In those areas of the New World reserved to them through priorities of discovery and papal adjustments, the Spaniards were faced with a more densely concentrated population of a higher cultural level than the Portuguese. The previous accumulation of wealth by the inhabitants, along with difficulties of undertaking with them a purely commercial exchange, led the Spanish to a third alternative: conquest, that is, the sacking of accumulated wealth and domination of the indigenous population, along with the direct dismantling of their traditional political structures. Spanish conquest exposed modern colonization's naked coerciveness. Once past that phase, their colonization organized around the mining of silver and gold, the central axis about which everything else revolved: so that even in this case, production for the European market dominated the colonizing process.

Finally, in North America we witness once again the same shift. Colonized since 1607 (Virginia settlement), emigration to these areas had a different connotation. Although the fundamental European expansionary impulses were present, other components interfered in the English version, blurring the results. Even there, emigration to the various American colonies was organized through the mediation of companies that engaged workers for North Atlantic regions, with an eye to colonial profits. But other cases arose through spontaneous emigration of groups persecuted as a result of English political and religious turmoil during the organizational phase of the modern state. The company system, as a rule, did poorly; almost all of them failed. The difficulties of producing products complementary to the metropolitan economy was one factor; others will be examined further on. At the end of the seventeenth century, however, expansion of European tobacco consumption finally opened up for the English colonies south of the Delaware the possibility of meshing with European commercial lines. Virginia, especially, underwent a rapid transformation from a settlement colony, organized on the basis of small and medium-sized properties of diversified production, to an exploitation colony organized into large slaveholding properties producing for the external market.

It was only in the most northerly areas—especially New England, geographically situated within a temperate climate where the possibility of setting up a complementary economy was either reduced or ruled out by the natural setting—that the old configurations of a settlement colony persisted. The establishment of plantations in the south (on the continent and in the islands of the Antilles) that specialized in export goods—and hence short of nutritional and manufactured products—opened up for those northern colonies the possibility of an external market for timber, cereals, manufactures, and so forth. The relative proximity of the two types of structurally divergent colonies thus created an entirely new situation, one particularly favorable to the northern settlement colonies. At the same time, the markets of the metropolis were less interesting to these colonies, for they could but furnish products similar to those available in Europe, and were therefore unable to fit themselves into the role of dependent economies. The diversified subsistence economy directed at internal consumption that characterized these colonies had little capacity for developing a high level of productivity and income until external markets were opened up to them. What is fundamentally important to emphasize, then, is that these markets, when they did open up, were by nature different from the external market common to the other colonies. Within the colonial system as a system the colonies' external market was the metropolitan market. The linkage was made through the regime of the "exclusive," which promoted the exploitation of the colony by the metropolis. In the case of New England, the external market consisted of other colonies: English, French, Dutch, and Spanish. This meant that the relationship that got established was not rooted in the mechanisms of the system; so, the income generated in this relation was not carted off (as was the rule in metropolis-colony relations) but was instead concentrated in the exporting economy itself. This is the fundamental point that permits the understanding of the later development of these settlement colonies, all in all surprising in the frame of the colonial system. They formed an exception, being "colonies" only in nominal political statutes—they were not colonies in a rigorous, structural sense. But bear in mind that it is in relation to the colonial system that they can be understood, even in their anomaly.

On the whole, then, one can now discern the general trend that characterized the setting up of modern colonization within the mechanisms of the colonial system: initial settling, with production for local consumption, followed by interlacing into European commercial lines, and hence into the mechanisms of the European economy. On shifting to production for the external market they would then fully mesh with the larger system since that commercial regime is, as we have seen, the system's nerve center. Thus, the process of colonization adjusts to the thrust of mercantile capitalism's colonial system: the primitive accumulation of capital in European economies was promoted through exploitation of overseas areas.

Not just production, but its rhythm also had to adjust to the system, and, in the end, to the European market, for fluctuations in European demand for overseas goods *(Kolonialwaren)* defined colonial production to a greater or lesser extent. Clearly, alongside the essential production for the European market, another entire sector dependent on it was organized within the colony, which sought to supply internal subsistence needs. But even here we find the colonial system's mechanisms defining the whole and impressing a production rhythm upon it. During periods in which external demand contracted, that is, when European prices for colonial products fell off, plantations tended to shift toward subsistence production because their capacity to import was diminished. When, on the contrary, external demand increased, colonial productive units tended to mobilize all their resources for export production; only then did the possibility of autonomous self-development open up for the colonial subsistence economy. On the whole, then, the exporting sector commanded the entire productive process.

Further, all the structuring of colonial economic activities as well as the societal form for which they serve as a base, was determined within the mercantilist colonial system, that is, within its connections with commercial capitalism. In fact, not just the concentration of productive factors in the fabrication of key products, nor the mere volume and rhythm of their production, but also the actual *mode* of their *production* was defined by the mechanisms of the colonial system. Here we touch on its weakest point. Colonization was organized with the intent of promoting the primitive accumulation of capital within the framework of the European economy, or, in other words, to stimulate bourgeois progress in Western society. This was the deeper meaning that brought together all parts of the system. In the first place, the commercial regime developed within the framework of the metropolitan monopoly; from there, colonial production oriented itself toward those products complementary or indispensable to the central economies; and, finally, production was organized and molded so as to permit the overall functioning of the system. In short, the production of wares for which there was a growing demand in European markets was not enough; it was indispensable that their production be organized in such a manner that their commercialization would serve to provide a stimulus to bourgeois accumulation within the European economies. It was not just a matter of producing for commerce, but rather for a special type of commerce— colonial commerce. It was, once again, that ultimate goal (acceleration of primitive capital accumulation) that commanded the entire process of colonization. This imperative forced the colonial economies to be organized in a mold that would allow the functioning of the colonial system of exploitation, and this, in turn, imposed the adoption of compulsory forms of work, or, taken to its limit, *slavery.*

*S*o Europe was able to contemplate the truly edifying spectacle of the rebirth of slavery precisely at a time when Western civilization was taking decisive steps toward the suppression of compulsory labor and the diffusion of "free," that is, wage labor. While in the sixteenth, seventeenth, and eighteenth centuries Europe made the transition from feudal serfdom to wage labor, which came completely to dominate productive relations with the advent of the Industrial Revolution, overseas, that is, where the world was being

Europeanized, the raw, monstrous hulk of slavery reappeared with unprecedented intensity and size. We know for certain that the perplexity created in Christian consciousness by such a situation gave rise, on the one hand, to a vigorous lineage of publicists who, without hesitation, denounced the horrors of modern slavery, and, on the other, to remarkable mental contortions rationalizing slavery and associating it with Christian morality. And Marx used to say that the colonies wind up revealing the secret of capitalist societies....

Let us take a closer look at this point, for it is fundamental to understanding the whole of the system we are analyzing. Slavery was the labor regime preponderating in New World colonization; the slave trade that fed it was one of colonial commerce's most lucrative sectors. If in addition to slavery we add up the various other compulsory, servile and semiservile forms of labor—"encomienda," "mita," "indentured servants"—we find that an extremely narrow strip was left, in the whole of the colonial world, for "free" labor. Old Regime colonization was, then, the ideal universe of unfree labor, the Eldorado that enriched Europe. Explanation of that fact has, at times, bordered on the picturesque. It has been argued, for example, that the Europeans had "resorted" to African labor because population in the homeland with which to people the New World had thinned out. The affirmation handily applies to situations such as obtained between Brazil and Portugal; but if we switch the situations, for example, the French metropolis in the face of the Antilles, the argument does not make sense; there a settlement colony was initiated that only later gave way to slavery. And in certain areas settlement continued to predominate. Anyway, the argument could merely be that Europeans or the European metropolises had at their disposal insufficient demographic contingents with which to people the Americas, and that they then "appealed" to Africa. Nowhere in this argument is there an explanation for why this "appeal" should end up in the enslavement of blacks. What really needs explaining is the regimen of slave labor.

Was it, in any case, really a matter of populating? Within the framework of the colonial system, it was, in essence, a matter of developing new areas so as to promote the primitive accumulation of capital in the metropolises. This naturally involved setting up a productive apparatus, and hence, yes, occupation and settling; but the exploitation of resources for Europe was the essential aim. That is why occupation, that is, geographic expansion, tended toward certain areas (tropical and semitropical), and settlement was organized through the recruitment of workers (whether European, indigenous, or African). The labor regime—the various forms of compulsory labor—still remain to be explained.

But as we have seen, colonial production basically amounted to production for the metropolitan market, that is, mercantile production. Within the market economy, wage labor is the most profitable. The compulsory forms of labor (ancient slavery, and, above all, feudal serfdom) had for their part hinged on premercantile economies (e.g., the closed manorial economy of the Middle Ages). The emergence of mercantile economies (the development of commerce) tended precisely to promote the untying of servile bonds, gradually creating conditions for the expansion of "free" labor—that was the process under way in the early modern period. Mercantilization of production can only become general—dominating all social relations—when the productive force of labor itself becomes a merchandise, that is, when the mercantile economy transforms itself into capitalism proper. To simplify: within this capitalist structure, the productive process begins with an investment of capital (a certain *quantum* of value) in its original form, money, which, on being invested, is transformed into factors of production (productive capital); interaction among these factors generates merchandise, an other form of capital (goods), which, when sold in the market, restores capital to its original monetary form supplemented by its surplus value; it is then used to remunerate the various factors (interest, profits, rents, wages) allowing reinvestment at a higher level. Capitalist production is thus steadily amplified, through self-stimulation.

Now it is evident that only wage labor makes possible this type of functioning: if the regime is slaveholding, the cycle binds up, since payment for the labor factor has to be partially made beforehand (in the purchase of slaves), while in the wage labor version remuneration takes place only after consumption of the labor commodity in the actual productive process. The feeding and care of the slave-merchandise stretches out the cycle throughout the slave's lifetime, further jamming the system. In addition, the capitalist system's extraordinary flexibility gets blocked because production cannot adjust itself to fluctuations in demand—for it is impossible to dispense with a labor factor that has been engaged once and for all. Slave labor is thus less lucrative for mercantile production. In that sense, the overseas labor regime prevalent at the very time of the Old Regime was, on the face of it, a breach of good sense. Adam Smith considered such an absurd institution the fruit of slaveholders' pride and love of domination.[27]

Notwithstanding, the slave system dominated the scene of mercantilism's colonial economy. This did not come about through stupidity on the part of colonial businessmen or as a result of flaws in their domineering character. Analysis of the problem simply cannot be limited to a formal logical level.

Examined by itself, the functional aspects of mercantile production preclude the use of slaves for market production. Karl Marx, who framed an analysis of bourgeois society not only from a logical but also from a historical perspective—that is, simultaneously explaining both the mechanics of its functioning and the conditions of its emergence—did not lose sight of the fact that capitalism emerged out of the disintegration of the preexisting feudal-servile and artisan-based (independent producers) structure. Hence, he understood that the development of mercantile relations during the dissolution of the old structure, while enhancing the division of labor and specialization in production, at the same time generated markets thereby permitting the powering of the process. In the most decisive step toward constituting capitalism proper, dissolution of traditional social bonds fostered expansion of the wage labor regime: a process that presupposes, on the one hand, liberation of the worker from all servile obligations, but on the other, at the same time, a dissociation between the producer and his instruments of production, depriving him of any productive factors other than his own labor. In its historical unfolding, the evolution of "free" wage labor involved, on one side, the overcoming of servile bonds (obligations, homage, etc.) and, on the other, a differentiation between the labor of the direct producers and all other factors of production, such as the peasant serfs' rights over the land, the instruments with which they produced their subsistence, or independent artisan producers' tools. We lack space here to study the lengthy history behind the gradual development of the wage labor regime in Europe. It was through it, however, that the work force emerged at its purest, compelled to trade its labor in the market. If workers had remained linked to the means of production instead of merely renting out their labor power to the owners of those means, they would have made use of those factors to sell their product themselves as autonomous producers, and the capitalist would have had no place in the sun. Whereas, isolated from the other components in the productive process, labor became a commodity like any other. Thus was consolidated the capitalist mode of production, although it was only during the Industrial Revolution that the process of constituting capitalism acquired an irreversible impetus.

To the bourgeois consciousness, of course, what was seen in this lengthy historic process forming the wage regime was the "liberation" of labor from servile injunctions, an ancient barbarism. For, in the capitalist economy, the commercialization of labor hides the new form of exploitation: the generation of surplus value in the hands of the capitalist.

The same Marx—always the implacable analyst of the bourgeois world—precisely because he had carried his study beyond all mystifications was able straightforwardly to affirm that the colonies did not favor conditions allowing the constitution of a "free" labor regime, because in the colonies there was always the possibility of a direct producer transforming himself into an independent producer by appropriating a vacant plot of land. So, while the development of capitalism in modern Europe "liberated" direct producers from medieval serfdom and integrated them into the new productive structure as wage workers thus camouflaging the exploitation of labor, the peripheral colonial economies, erected precisely as levers to foment the growth of capitalism and intimately integrated into its framework, stripped that same exploitation of all pretensions, exposing its darkest, rawest nature. The colonies displayed Europe's viscera.

Eric Williams, in reapplying Marxist analyses to study the genesis of modern slavery, noted quite correctly that the implantation of colonial slavery, far from having been an option (wage worker or slave), was in fact imposed by historico-economic conditions.[28] And here again we face the deeper meaning of colonization and the Old Colonial System's mechanisms, touching on the essential point needed for understanding it. Given the historical conditions attending the colonization of the Americas, the implantation of compulsory forms of labor derived directly from the need of the colonizing entity to have colonies fit in with the mechanisms of the Old Colonial System, that is, to promote the primitive accumulation of capital in the European economy. Otherwise, given the abundance of one productive factor (land), the result would have been the overseas constitution of European settlements developing a subsistence economy directed toward their own consumption, with no effective economic interconnections with the dynamic metropolitan centers. That, however, did not figure into European mercantile capitalism's expansionist impulses as it did not address its needs.

Nothing, in principle, negated the possibility of a colonization in that more restricted sense (of occupation, settlement, and development of new regions). At that point in Western history, however, it was a matter of colonizing for capitalism, that is, in accordance with the system's mechanisms, and those mechanisms imposed compulsory labor. Otherwise, no production for the European market would have taken place as the colonists would have developed an economy turned toward their own consumption. Or, if one were to imagine an export production organized by businessmen who paid their labor wages, those wages would have had to be at a level that would compensate the direct producers for abandoning the alternative of becoming autonomous producers of their own subsistence. In that case, the costs of production would have been such as to preclude colonial exploitation and hence prevent colonization from playing its role in the development of European capitalism. How, then, could the mechanisms of the commercial "exclusive" have been made to function? In short, production for the European market within the frame of colonial commerce, tending to promote the primitive accumulation of capital in European economies, required compulsory forms of labor. From another angle, colonial production for export—of a volume and at a rhythm defined by European markets and therefore attending to the needs of capitalist development—could only adjust itself to the needs of the colonial system through organization of large-scale production, a move that presupposed ample initial investments. With that requirement, the possibility of production organized on the basis of small autonomous proprietors—who might produce their subsistence, exporting a meager surplus—was also excluded. By analytically examining the impossibility of these alternatives for men living in that era who undertook capitalist colonization, slave (or slave-prone) production reveals itself, as Eric Williams observed, as the almost "natural" choice.

Accordingly, there developed a colonization in the New World centered on the production of staple goods bound for the European market, production firmly rooted in various forms of compulsory labor—at the limit, slavery. Colonial exploitation meant, in the final analysis, the exploitation of slave labor. Thus, the colonists metamorphosed into slaveholders, thereby assuming their destined role in the great world theater. Nor is it any wonder that they yielded to the pleasure of dominating other people—that was merely the misery of the human condition caught in the system's web.

The enslavement of blacks effectively takes us back to the very beginning of overseas expansion. Gomes Eanes de Zurara memorably described the arrival of the first slaves in Christian Europe.[29] But these earliest supplies of slave merchandise were destined for European "consumption" during a precolonial commercial expansion, and that introduction of slave labor into the midst of an expanding capitalist mercantile economy was not widespread. Only because of the conditions in the colonies that we have just examined did slavery find fertile soil for development in the overseas colonial world. In the Atlantic islands—site of the first modern colonization—the initial settlement, with its diversified, self-sufficient economy, gradually shifted toward specialized production for the metropolitan market, bringing with it a new labor regime. The next step was the introduction of African slavery: "[sugar] cultivation expanded into a new world; it prospered, while Africa was despoiled of her wilderness children so the civilized might dine cheaply."[30]

With agro-industry transplanted to Brazil during a phase in which large-scale consumption predominated and prices were rising anew, the natives were at first compelled to perform the arduous work of cane cultivation and sugar refining. Expansion of production utilizing an ever larger enslaved labor force soon gave rise to the Negro slave trade to the New World. "It is unquestionable," said the historian Lúcio de Azevedo, "that we owe to sugar the development of slavery at the core of modern civilization"[31]—which is probably an exaggeratedly synthetic way of putting it: All of the complex interweaving of the colonial system is connoted by the word "sugar." But it was on this slaveholding basis that the colonization of Portuguese America was developed, and colonial society continued to be molded on that same basis. The Jesuit Manoel da Nóbrega noted, in Brazilian colonization's early days, that "the men who come here find no way other than to live off of the work of slaves."[32]

The introduction of African slaves has been explained, from one side, curiously, by the "inadaptation" of the Indians to tillage, and from another by citing Jesuit opposition to Indian enslavement. There is no doubt that Jesuit sermonizing weighed in the aborigines' defense, though we may note in passing that this failed to safeguard them entirely: whenever there was a shortage of Africans (due to difficulties in navigating the Atlantic or due to colonial competition, for example) the Portuguese immediately turned to the compulsion of natives. It is also true that the blacks could not rely on that same Jesuit defense. The arguments justifying such a discrepancy were truly edifying, but it does not behoove us here to delve into theological questions. What appears indisputable to us is that not only were the natives made use of at certain times, especially during the initial phase, but that one certainly cannot allege any greater or lesser "aptitude" to slave labor (for that is what the argument amounts to). What may have mattered was the demographic thinning out of the indigenous population, along with difficulties in their supply, transport, and so on.

But in the preference for Africans,[33] there reappears, we believe, yet another time, the workings of the mercantilist system of colonization. This system unfolds, we repeat as often as necessary, within a system of relations tending to promote primitive accumulation in the metropolis; the trafficking in Africans, that is, the supplying of the colonies with slaves, opened a new and important sector of colonial commerce, whereas the capture of Indians was an internal colonial business. Thus, the commercial profits deriving from the supply of Indians were kept in the colony by the colonists. The accumulation generated through the trade in Africans, however, flowed into the metropolis and was realized by metropolitan merchants engaged in furnishing this "merchandise." This may well be the inner secret of the better "adaptation" of the Negro to tillage—to slavery. Paradoxically, it is by commencing with the slave trade that one is able to understand colonial slavery, and not the other way around.

In the English, French, Dutch, and Spanish colonies, instances of the phenomenon exhibit regional variations—we lack space here to analyze the manifestations of the phenomenon in all its minutiae—but the background remains the same. All relied on varying forms of compulsory labor, servile or semiservile, especially slavery, that dominated overseas production and defined colonial society.

The Crisis of Mercantilist Colonialism

Such were the parts of the system, and its functional mechanisms; we now have at our disposal the elements with which to analyze its crisis. For if we think in terms of *the system's* crisis, then it is from its own functioning that that crisis must emerge, and not from exogenous factors. In short, as it evolved, the Old Regime's colonial system simultaneously fostered elements that led to its own eclipse.[34]

And, in fact, while colonization in the mercantilist era developed by promoting primitive capital accumulation for the European central economies, toward that end (i.e., in order for colonial exploitation to continue to function) it went about engendering within the overseas world the universe of the seigneurial slaveholding society. Yet the interrelations and values of this society became increasingly opposed to those held by the rising European bourgeois society.

Let us linger, however, for just another moment, on the implications of slavery for colonial societies and economies. To begin with, within the sphere of production one immediately distinguishes two basic sectors. The first, an export sector, organized into large productive units functioning on the basis of slave labor and centered on the production of goods for European consumption, was the essential sector that addressed the very reason for capitalist production. The other, subordinate to and dependent on the first, was a subsistence economy to attend the needs of local consumers with goods not imported from the metropolis. It fell to small proprietors and independent laborers and was organized so as to allow the functioning of the first. The dynamic of the whole of the colonial economy was determined by the exporting sector. In some circumstances and within given areas, the subsistence sector could, as in the cattle industry, loom somewhat large, organizing into extensive properties, or, as in other cases, incorporating the slaveholding regime.

But the global dynamic always depended on the external flux, the ultimate primary center being European capitalism. It meant, in every sense of the term, a dependent economy—with the principal sector directly dependent, and the secondary sector indirectly so.

Second, at the level of socioeconomic relations, the slaveholding structure greatly increased the concentration of wealth in the hands of the slavemasters who owned the enterprises that produced goods for colonial trade. The direct producer, reduced to the status of a mere instrument of labor—*instrumentum vocale*—that is, a person transformed into a thing as a slave, did not, by definition, possess an income of his own; the earnings thus concentrate in the seigneurial stratum. At this point, we meet up with the element we lacked for our understanding of the system's mechanisms: This concentration of income was precisely what was necessary in colonial society, permitting it to function and finally hinging together the various parts of the mechanism. Note well: the overall income generated by the peripheral economies was only finally realized in the European central economies' markets; thus, the greater part of it was transferred, through the colonial commercial mechanisms analyzed above, to the metropolises, or better, to those bourgeois groups connected to overseas transactions. But it happens that the concentration of the remaining minor parcel retained within the colony among a small seigneurial stratum was what made the continuous functioning of colonial exploitation possible. It was this concentration of income that made it possible, despite the transfer of the larger share to the European bourgeoisie, that the seigneurial colonists were still able to maintain continuity in the productive process to the point of affording themselves luxurious standards of living. By the same token, still within the mechanisms of the system, the very colonists themselves had resources with which to import products of the European economy. The most significant part of their income was created through exports and consumed in imports, transactions made within the colonial commercial regime, and which transferred the profits to the metropolis, so that, viewed as a whole, colonial society was exploited by the metropolitan bourgeoisie. But within that selfsame colonial society, the colonial seigneurial class found itself in a privileged position, and this fact made possible the meshing of all the various parts of the system. And slavery, which is the other side of the same coin, reappears as its essential element. Now, viewed from another angle, colonial exploitation means the exploitation of slave labor.

The implications derived from the mode assumed by colonial production do not end there.[35] Slave-based production for the European market, that is, the *mercantile-slave* system, was characterized by a shortage of local capital (linked to the exploitation of the colony by the metropolis) and an abundance of land (we've already noted the structural connections between availability of land and introduction of slavery).

Furthermore, the very structure of slaveholding hindered investment in technology. The slave, as a slave, has to be kept at subhuman cultural levels so as not to awaken to the true nature of his human condition—that is an indispensable part of slaveholder's domination. It follows that the slave (as slave) is not apt to assimilate more advanced technological processes. In some situations the seigneurial colonists came even to oppose, to popular amazement, the teaching of the catechism to slaves (which, after all, had been the very argument used to justify their being drawn from Africa), for it posed dangers: learning a common language would enable communication among various African groups. We must remember that, contrary to the common supposition, it is an illusion that a slaveholding society enjoys stability. In fact, flight and rebellion were quite common, and the ubiquitous whipping posts could not, even from a distance, be mistaken for decorative objects. Let us not, however, stray too far from our reflections: capital was not available, and the slaveholding structure did not favor technical progress.

The result: the colonial economy suffered from low productivity. As a consequence, as noted by Celso Furtado, it grew extensively, that is, through aggregation of new units composed of the same factors.[36] But still, since it did not reinvest on an increasing scale, but simply replaced and aggregated—it depleted natural resources. The mercantile-slave economy was a predatory economy. Again we meet up with the primary purpose of colonization: the unfolding of European commercial expansion. Just as New World colonization began as a purely commercial activity involving natural products (dye-wood, furs), just so, although with the emergence of colonial production the system took on extraordinary complexity, it kept on depredating natural resources. In this sense, then, colonial expansion faced natural limits: the draining off of resources dilapidated by the colonial mode of production. Since, meanwhile, this process developed within a larger context and not just in a purely economic one in its strictest sense, long before any of those limits had been reached, tensions of every type began to appear. Thus, we begin to uncover the contradictions within the system.

The slave structure of the colonial economy and society effectively implied, albeit indirectly, an eventual limitation on the market economy's growth. The contradiction thus points up the very nature of colonial production: at once both mercantile and slaveholding, that is, producing goods for European capitalism through the labor of slaves. Those two defining components of the colonial economy coexisted with difficulty within the same context, generating rising tensions. On one hand, slavery brought about a low level of productivity and, hence, only a limited profitability in colonial production (as distinct from its commerce). But since it lacked the means for minimizing costs through technical progress, the seigneurial-enterprising class necessarily had to try to minimize the cost of maintaining the slave-labor force. To that end, it tried to get from the labor of slaves at least a portion of their own subsistence within the estate itself. Thus, there was inserted into the core of a basically mercantile economy, an entire segment of subsistence production whose activities took place along the edge of and almost outside the market economy. Added to this was that part of the payment for the labor factor went outside the producing area (the payment for slaves made to European merchants), while the other part (for the maintenance of the slaves) took place through subsistence production, leaving no place for mercantile operations within the colony, at least not on a large scale. Therefore, neither of the two sectors into which the remuneration of labor was divided within the colonial economy created an internal demand that could have stimulated economic development. To sum up: the mercantile colonial slave economy necessarily had a very small internal market.

Within the whole of the system, this meant that the colonial economy became ever more dependent on the metropolitan economy. Given the narrowness of the internal market, it had no means of stimulating itself, thereby being left subject to the impulses of the dominant dynamic center, that is, of European commercial capitalism. In that sense, the phenomenon adjusted itself to the system and there were no contradictions.

But let us examine it from another angle. On the one hand, European expansion had meant, basically, commercial expansion, the opening of advantageous new markets—and colonization, as we have seen, had meant an extension of the market economy. Looked at internally, however, colonial economies revealed themselves as a mercantile-slave mode of production that limited the constitution of their internal market. There was a substantial layer of the population (the direct producers) whose consumption, in large part, was effected outside of mercantile transactions. It was truly an expansion of the market economy, but it carried within it structural limitations to that expansion. What followed from this was extremely important. In the typical colonial (mercantile-slave) economy, or, more precisely, within colonial society, the universe of mercantile relations affected only the upper social strata of slaveholding colonists.[37] They only imported merchandise from the central economies for their own consumption: food or manufactured goods for personal consumption, implements for productive consumption.

To be sure, the reality was somewhat more complex. Colonization involved other activities (administrative, military, religious, etc.) that amplified to a certain extent the segment of colonial society connected to the mercantile economy. The actual functioning of colonial production demanded social categories other than the master-slave binomial. The sugar industry, for example, required an entire range of skilled workers, technicians, suppliers, and so on. Commerce itself relied on intermediary personnel, clerks and accountants, for instance. All of this resulted, within the colonies, in the formation of the earliest urban settlements that enlarged the sector involved in the market economy.

But note that all of the components of colonial society that we have been indicating (functionaries, administrators, clerics, military) were basically secondary categories of colonial society to the extent that their presence in the overseas world followed from the slaveholding economy and from production for European capitalism. Colonization was undertaken to produce for the metropolis, and colonization ended up involving other components. The other social categories, however, depended on the master-slave matrix the same way as the subsistence sector depended on the export sector. At root, therefore, within the colonial environment, everything depended on the seigneurial class, and the mercantile economy within the colonies expanded as a function of it. The fundamental mechanism remained. The universe of mercantile relations was a function of the masters and, shall we say, their entourages. The mass of direct producers (the slaves) lived outside mercantile relations, and this hindered the constitution of an internal market.

On the whole, such a configuration of the colonial world responded adequately to the functioning of the system as long as the central economies only developed at the level of the primitive accumulation of capital and production only expanded through handcrafts or even manufacture in the true sense of the word. However, once this stage was surpassed, and the mechanization of production in Europe reached toward the Industrial Revolution, invigorating productivity at a rapid pace and in an intense way, it led to a growth of capitalist production at a volume and rhythm that came to demand much more ample overseas consuming centers, consumption not only by upper societal strata, but by the colonial society as a whole. And this required the generalization of mercantile relations in the colonies themselves. Then the system was compromised and entered a crisis.

Now, in promoting the primitive accumulation of capital in the European central economies the colonial system had acted, as we have seen, as a fundamental instrument for promoting the transition into industrial capitalism. (Of course, it was not the only element: one must consider the internal factors related to the development of capitalism in Europe.) In organizing themselves within the framework of the colonial system, the peripheral economies developed their production along lines tending to complement the central economy, supplying those products that it needed and providing raw materials first for European manufactures and later for the factory system. They were thus configured into authentic complementary economies, tending to bestow on the metropolises autonomous economic conditions in competition with other mercantilist nations. Note the importance of this mechanism, in an era during which the practices of mercantilist policy became general among the various

European states. The colonial markets were those where, by definition, mercantilist rules could be exercised: hence, the truly furious disputes over the conquest of those exceptional markets.

Along these same lines, there had developed in the metropolises a colonial policy aimed at obstructing manufacturing production within the colonies. They sought in this way to reserve the colonial market for the manufactures of the homeland. Given the social and economic structure into which the typical colony was organized, or at least the ones that were perfectly conformed to the system, the possibility of developing manufactures was basically reduced anyway. The prohibitionist policy encountered weak resistance due to the poor conditions for the growth of manufactures in the colonial world. Accordingly, expansion of overseas colonization efforts effectively came to involve only a gradual enlargement of the manufactured goods consumer market.

Only in the settlement colonies such as New England were such conditions favorable, but New England was regarded in mercantilist circles as "the most prejudicial plantation of this kingdom" (Josiah Child).[38] Likewise, the results of the prohibitionist policies were successful or not according to whether they applied to colonies with a greater or lesser degree of adjustment to the system. The settlement colonies had been constituted, as we have seen, within the New World's temperate zone, a region not targeted for modern European colonization in its early phase precisely because of the impossibility of organizing in that location a type of production able to satisfy the European market's demands. So, during the seventeenth century, English emigrants fleeing the political and religious tensions of the homeland had migrated into the region in an effort to rebuild their way of life in the New World. The settlement colonies were thus formed bordering the system, and the struggle for independence and the establishment of the United States were impelled by metropolitan efforts to make these colonies conform to the larger system. Such events signaled the beginning crisis of the Old Regime.

Adding up the elements analyzed so far, that is, the colonial system's functional mechanisms, we can now explain its position within the rise of capitalism. The colonization of the New World in early modern times, that is, the exploitation of overseas colonies organized along the lines of the Old Colonial System, formed a powerful instrument for accelerating primitive accumulation within the context of European mercantile capitalism. It comprised a process for transferring income from the colonies to the metropolises, or more precisely, from the periphery to the dynamic centers of the European economy. Such income tended to concentrate in the entrepreneurial strata connected with colonial commerce. By being themselves complementary economies, that is to say, economic buttresses for the metropolises, these elements of the Old Colonial System heavily contributed to the development of European national economies; development that, at the time, consisted in expanding mercantile capitalism, thereby hastening capital accumulation.

If we now recall what we indicated earlier regarding commercial capitalism as an intermediate phase between the disintegration of feudalism and the Industrial Revolution, the mercantile colonial system reveals itself as operating on the two basic prerequisites for the transition to industrial capitalism. Overseas colonial exploitation promoted, on the one hand, primitive capital accumulation on the part of the enterprising stratum in Europe; and, on the other, it enlarged the consumer market for manufactured goods. It simultaneously augmented the factory system's productive capacity and increased the demand for manufactured goods. The prerequisites for the Industrial Revolution— the central historic process in the emergence of capitalism— were thus created.

Now we reach the heart of the system's dynamic: in functioning as a whole, it simultaneously brought on the conditions for the onset of its crisis and its denouement. Even before the system's alternatives had been exhausted, that is, prior to reaching the limits inherent in colonial exploitation, the tensions generated by these fundamental mechanisms began to impose new adjustments, alterations, and changes that then compromised the colonial system. In other words, it was not necessary for industrial capitalism to achieve the highest possible levels of development and expansion before the colonial system — slaveholding, colonialist — entered a crisis. As a matter of fact, the first impulse was enough. The first steps into the Industrial Revolution were sufficient to get it under way.

The furious overseas competition among the mercantilist powers was inherent in the very logic of the system of colonial exploitation. Such competition could perforce only result in the hegemony of one of these powers. Nor was it any coincidence that England was both the power that won the race of colonial competition and the nation that took the first steps toward modern industrialism. One should not overlook the internal factors affecting its economic growth on the way to industrialization, but it is clear that its colonial supremacy allowed England to transfer within its borders— to a greater extent than the other powers— the stimuli forthcoming from the colonial system. The consolidation of British preponderance and the opening of the Industrial Revolution converged about the 1760s.

During the critical period between 1763 (end of the Seven Years War) and 1776 (independence of the United States), those problems were acutely felt. Having overcome the rivalry with France, Great Britain sought, on the one hand, to reinforce its own metropolitan "exclusive" (in an effort to bring the New England colonies into conformity with mercantilist policies), and, on the other, to widen commercial inroads into the Hispanic colonies, whether legally through their metropolises or through smuggling. All of this sprang from Britain's political supremacy and industrial development. Yet, just as the system was fully worked out, it engendered tensions of all kinds. The more the process developed, the less England could withstand the "independent" trade of its colonies. At the same time, smuggling with Iberian colonies became itself an insufficient outlet for the flow of its industrial production. Further, the monopoly that the Antillian English plantations enjoyed in the English metropolitan market (the other side of the Colonial Pact) became increasingly onerous to the metropolis: it was as though the Colonial Pact were inverting itself, benefiting the colony rather than the metropolis.

Within this framework of acute tensions, this complex of multiple interests, the equilibrium became increasingly precarious. It broke down entirely with the independence of the United States. The emergence of the new republic in effect carried implications that greatly transcended the merely political event. It was the first time a colony had ever become independent. The tensions, the competition, the appropriation by one power of colonies belonging to others, all had been adjustments within the system. What obviously could not be contained within the system was the breakdown of the Colonial Pact itself. To the extent that structural tensions worsened, causing divergent interests to surface, the colonial world came to exist in a state of constant excitation. Criticisms of the Old Regime were heard also in the colonies and found a highly receptive audience. With the independence of the United States, however, what had once been a possibility came to be reality. The political innovations woven into the republican form adopted by the new state further highlighted the significance of the change, marking the beginning of the crisis not just of the colonial system, but of the entire Old Regime.

NOTES

[Richard Graham: This chapter was translated from Femando A. Novais, Estrutura e dinâmica do Antigo Sistema Colonial. That text first appeared in his "Portugal e Brasil na crise do Antigo Sistema Colonial," PhD diss., chap. 2, and was subsequently included (with some modifications) in his book by the same title. I have shortened the text in a few places where it did not alter the argument.]

1. Les migrations des peuples, 1 l-16ff. [Richard Graham: Aside from explanatory notes, those that follow are limited to those that give the source of quotations in the text or refer to authors actually mentioned in the text. The full bibliographical basis of this chapter can be found in the original as well as in Portugal e Brasil]

2. "Collecâo das leys e ordens que prohibem-os navios estrangeiros, assim os de guerra, como os mercantes, nos portos do Brazil," Ms., Arquivo Histórico Ultramarino (Lisbon), cód. 1.193; also copy at Biblioteca Nacional, Rio de Janeiro, Ms. 7, 1, 6.

3. Britain's Commercial Interest Explained (1747) as quoted by Sée, As origens do capitalismo moderno, 136. See also the expressive example of the mercantilist concept from the pen of the Marquis of Pombal when addressing the French ambassador in 1776: "the overseas colonies having been established precisely for their utility to the metropohses to which they belonged, from thence were derived the infallible laws, universally observed in the practice of all nations, " Pombal to Marquis de Blosset, January 31,1776, quoted in visconde de Santarem, Quadro elementar das relaçoes, VIII, 151-155 (our italics).

4. La época mercantilista, 17-29.

5. Studies in the Development of Capitalism, 37ff.

6. Stark, Historia de la economía, 20-26. Even Hecksher [La época mercantilista] may not have been aware of something that did not escape the attention of Lord Keynes, who noted that at a time when governments had practically no way to manipulate interest rates, the best way to keep them low and thus foster productive investments was the abundance of currency: Keynes, Teoría geral do emprego, 319-350.

7. [Richard Graham: In 1979 Novais added at this point the following note:] Without getting into an exhaustive analysis of the transition from feudalism to capitalism, which would be beyond the limits of this chapter, we have indicated in the text the most important connections among the various levels and sectors of historical reality in the modern era. That should be our principal aim at this point. In this regard Immanuel Wallerstein's The Modern World System (New York, 1974) is most suggestive.

8. La Mediterranée et le monde méditerranéen, 619.

9. For example, "The best indication of her [Brazil's] wealth is that when men return from India to Portugal they bring along all they own because none there have real estate (or if any do their holdings are slight), and all their fortune consists of physical things with which they embark and with the sale price these command in Portugal they assure themselves a life-income or buy houses. Whereas the residents of Brazil have all their wealth in real property, which cannot be taken to Portugal, and when any depart they must leave it in the land" [Brandão?], Dialogos das grandezas do Brasil, 79.

10. Prado Júnior, Formação do Brasil contemporâneo, 4th ed., 5-26,113-123.

11. Marx, El Capital, I, 801 and esp. 840-851. We lack space in this chapter for a more extensive discussion of primitive accumulation.

12. Weber, Wirtschaftsgeschichte, 3d ed., 256-259.

13. Leroy-Beaulieu, De la colonisation chez les peuples modernes, 533ff. ; or, in the 5th ed., II, 563ff. He based himself on the classification of Roscher and Jannasch, Kolonien, Kolonialpolitik und Auswanderung, 3d ed., 2-32.

14. Soon after the rounding of Cape Bojador — a decisive event in the history of European expansion — the Portuguese king forbade navigation to the discovered lands without the authorization of Prince Henry: Carta Regia of 22 October 1443 in Godinho, ed., Documentos sobre a expansão portuguesa, I, 142.

15. The phrase is from Dias, O capitalismo monárquico português, II, 355ff.

16. Quoted by Holanda and Pantaleão, "Francêses, Holândeses," tomo 1, vol. 1, 165-166.

17. "The notable progress made by this city [Antwerp], so rich and so famous, began around the years 1503 and 1504, when the Portuguese, having earlier occupied Callicut by dint of marvelous and stupendous navigation and having made an accord with that country's king, began bringing spices and drugs from the Indies to Portugal and thence to this city's markets": Ludovico Guicciardini, Discrittioni di tutte Paesi Bassi (1567) quoted in Hauser and Renaudet, Les débuts del'âge moderne, 61-62.

18. [Richard Graham: 1 arrôba = 15kg.]

19. In Santarém, Memórias e alguns documentos, 65-66, 222-224.

20. Furtado, Formacão económica do Brasil, 1st ed., 20.

21. As can be seen in the table he presents in Le Portugal etI'Atlantique, 256, the price of sugar in Brazil remained at 800 réis per arroba from 1570 to 1610, whereas in the same period in Lisbon it ran up from 1,400 to 2,020 réis. In 1614 prices in these two markets converged (1,000 réis) only to diverge again: by 1650 it was 700 réis in Brazil and 3,800 in Lisbon.

22. Book V, Titles CVII and CVm of the Código Phihppino, edited by Almeida, 1253-1259.

23. Guillermo Céspedes del Castillo, "La sociedad colonial americana en los siglos XVI y XVII," in Vicens-Vives, ed., Historia social y económica de España y América,III ,479.

24. Quoted in Clough and Cole, Economic History of Europe, 347.

25. For example, Mauro, Nova história e Novo Mundo, 61-64.

26. Gouveia quoted by Azevedo, Epocas de Portugal econômico, 233-235.

27. An Inquiry into the Nature and Causes of the Wealth of Nations, 364-366.

28. Capitahsm and Slavery.

29. Zurara, Crônica dos feitos da Guiñé, chap. 24, 122-123.

30. Azevedo, Epocas de Portugal econômico, 228.

31. Ibid.

32. Cartas jesuíticas, vol. 1, 110.

33. Goulart estimates their number to the end of the eighteenth century at 2,200,000: A escravidão africana, 217.

34. Contradictory development appears inherent in various stages of capitalism's colonial exploration; see, for the nineteenth century, Marx's analyses of British domination in India: Marx and Engels, "Sobre el colonialismo."

35. [Richard Graham: In 1979 Novais added at this point the following note:] To further the analysis of the colonial system's crisis it does not seem necessary to explore in depth the issue of "the colonial mode of production," although our position on this theme is implicit. The works of Ciro F. S. Cardoso are clearly those that have taken this conceptualization the furthest. See his "Severo Martínez Peláez y el carater del régimen colonial" and "Sobre los modos de producción coloniales de América." These two works are also published in América colonial: ensaios, ed. Santiago. As is natural, given the complexity of the problem, we do not entirely agree with some of Cardoso's views.

36. Formacäo econômica do Brasil, 66-69.

37. To the extraordinary complexity of the "colonial economy" engendered by the structures of the Old Colonial System is connected the peculiarity of the social formation that it supports. See the reflections of Florestan Fernandes characterizing Brazilian social formation: Sociedade de classes, 9-90.

38. A New Discourse of Trade (1669) quoted in Clark, History of Manufactures in the United States, I, 4.

CHAPTER 3

THE CAPITALIST EXPORT ECONOMY IN BRAZIL 1884-1930[*1]

João Manuel Cardoso de Mello
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Introduction

This essay will analyze the formation and dynamics of Brazil's capitalist export economy. To do this, we must have in mind the origins of that system, or more precisely, the passage from a colonial to a capitalist export economy by way of a national mercantile-slave economy.[1] This historical process is best understood in light of the transformations undergone by world capitalism since the Industrial Revolution — changes that brought crisis to the old colonial order.[2]

Metropolitan commercial capital developed the colonial economy for the purpose of stimulating primitive accumulation at home during the transition from feudalism to capitalism. Significantly, in Latin America commercial interests did not limit themselves to the exploitation of pre-conquest modes of production; rather, they extended their normal range of activities to engage not only in trade but also in production itself. In so doing, they founded the colonial economy, and very early gave it a mercantile character by assuring the realization of production in the world market. In colonizing for capitalist ends mercantile interests asserted control of the colonial economy by "reinventing" servile and slave labor. They effected the continual reproduction of slavery's intrinsic social relations through the slave traffic — a sector of colonial commerce and a principal source productive of accumulation. In sum, commercial capital mobilized Brazil's productive forces and implanted corresponding social relations of production to serve its own ends.

If at the outset the evolution of capitalism and the colonial economy constituted a single, unified process, and if this process stimulated capitalism in its early manufacturing stage, this same movement eventually led to the Industrial Revolution and the emergence of specifically capitalist modes of production. Thereafter accumulation relied on its own momentum for growth

*1 The authors would like to thank Rae Flory for her translation. Technical review in this edition by Pedro Paulo Zahluth Bastos.

and ceased to require external props. The transition to industrial capitalism both foreshadowed and hastened the ultimate dissolution of the colonial economy, as mutual advantage turned into antagonism and what had once furthered development now obstructed it. From this point on, the relations between capitalism and the colonial economy became increasingly contradictory.

With its hunger for markets, the Industrial Revolution provoked crisis in the relatively complex precapitalist economies with which it came into contact. This was generally true in Latin America where, nonetheless, European industrial capitalism did not destroy the economic bedrock of forced labor. Rather, its major impact at this juncture was to contribute decisively to the demise of the colonial pact and to the formation of independent national states. The existing labor arrangement remained intact both because it was in no way affected by the entry of British manufactured goods and because the choice of substituting free for forced labor had become a *national* decision. In other words, the passing of one feature of the colonial economy—the dual political domination and commercial monopoly exercised by the metropolis—opened Latin American markets to British industrial capital. At the same time, however, the emergence of national states meant that Latin American development would cease to be a purely "reflexive" process. At best, free trade industrialism could use all the resources it could muster to exert pressure on slave trade; it could not, by itself, impose its objectives.

If competitive capitalism initially brought crisis to precapitalist economies, it soon created the conditions for their reorganization. In Britain the passage of the Corn Laws in 1846 roundly defeated agrarian Protectionist interests, while the shift in the focus of accumulation from the textile industry to the capital goods industry (definitive with the Great Railway Mania of 1845—1847) encouraged the exportation of capital— defined as money capital and capital goods, but principally as the extension of capitalist social relations of production.[3]

It was at this point that British industrial capitalists promoted India's cotton export industry based on wage labor, thereby reorganizing the Indian economy to serve their own interests.[4] Circumstances were different in Latin America, however, where the British lacked both the power and the incentive to reorganize individual national economies. Here Britain was dealing not with its own colonies but with independent nations, albeit weak ones. Furthermore, in view of Britain's competition from her own colonies and from other industrialized nations such as the United States, investment opportunities in Latin America did not seem particularly attractive.[5] In other words, the weakness of capitalism's power of diffusion in this region ultimately derived not from the absence or instability of external demand but from the internal difficulties posed by mounting vigorous export economies. Where national mercantile capital proved capable of undertaking this task, as in Brazil, it became possible in a certain sense to create external demand. For their part, capital imports, although less visible, played a significant part in Brazil's transition from a colonial to a capitalist export economy.

It should be added, however, that during its competitive phase (from the Industrial Revolution to the beginning of the depression of 1873) capitalism's power of diffusion was itself limited; only England had advanced sufficiently to promote the extension of capitalism abroad. With the emergence of monopoly capitalism between 1880 and 1900, circumstances changed dramatically. Monopoly capitalism greatly accelerated the subversion of social relations and the global diffusion of capitalism by converting the exportation of capital — now directed chiefly at precapitalist areas — into a basic characteristic of the world market.[6]

We can identify three concrete historical situations in which capital from industrialized nations penetrated precapitalist economies. In the first, capital was invested in largely undifferentiated precapitalist systems that, for the most part, had not been incorporated into the world market. In such circumstances one can correctly refer to "imported capitalism" imposed entirely from without, inasmuch as internal factors had little to do with economic reorganization.

The second form of capitalist penetration consisted of the conversion of previously unoccupied colonial areas into large-scale producers of foodstuffs. Massive immigration made it possible to overcome the resistance of small private commercial producers and to implant capital as a social relation, while the importation of means of production permitted the installation of the vital infrastructure to the operation of the food export business. In is this case, which concerns a particular form of capitalist colonization, it is preferable to speak of the *transplantation* of capitalism.[7]

The experience of much of politically independent Latin America was substantially different. It is true that roughly between 1880 and 1900 both the extraordinary inflow of capital (whether channeled into the productive nuclei of the export sectors or into their supporting infrastructures) and mass immigration in some countries were crucial to the formation of capitalist export economies. Nevertheless, Latin American economic history cannot be categorized in terms of either the importation or the transplantation of capitalism, since development in this instance was not strictly a function of the actions of the industrial nations. To the contrary, any study of economic change in Latin America must necessarily begin with an analysis of the dynamics of the national economies themselves and then consider how immigration and the transfer of capital acted as catalysts to transform these economies from within.

In conclusion, the passage from a colonial to a capitalist export economy was a complex process that must be viewed from a broad perspective. Economic change was determined in the first instance by internal factors, and in the last instance by the evolution of world capitalism—that is, by the emergence of industrial capitalism, its development during a competitive stage, and the transition from competitive to monopoly capitalism.

This is precisely the perspective we adopt to outline the beginnings of the Brazilian capitalist export economy. Thereafter we examine the dynamics of that economic system in the period 1889 through 1932. Our analysis of this phase of Brazilian development begins with a study of the cyclical movement of coffee capital, the focal point of accumulation in these years. Next we offer an assessment of the relationship between official economic policy and capital accumulation in the coffee sector.

Once these fundamental issues have been addressed, we turn our attention to the establishment of large-scale industry in Brazil and, in so doing, attempt to clarify the relations between the Brazilian economy and the dominant monopoly capitalist economies. It is our contention that the subordinate position of Brazil in world capitalism was determined both on the side of realization of coffee capital and on the side of accumulation of industrial capital. This approach ultimately reveals how the development of monopoly capitalism determined the movement of the capitalist export economy, and how this movement translated internally into the hegemony of coffee capital — predominantly mercantile — over industrial capital.

We further propose to explain the industrial expansion that took place between 1895 and 1929 and to deal, finally, with the crisis of 1929. This critical period had a decisive impact on the coffee export complex and prepared the way for a change in the pattern of accumulation within the Brazilian economy that, from the 1930s on, initiated a new phase in the country's capitalist development.

Coffee capital: the dynamics of accumulation

There can be little doubt that the coffee export complex was the dynamic center of the Brazilian economy between 1886 and 1930. Accordingly, the expansion of coffee capital, an eminently cyclical process, is the logical point of departure for understanding the pattern of accumulation in this period.

Accumulation and the Cyclical Development of Coffee Capital

The coffee export complex consisted of a productive nucleus that included the processing industry, as well as an urban sector that provided transportation, export-import and financial services. In consequence, coffee capital, with its agro-industrial, commercial, and financial components, was multifaceted.

We can begin by explaining the reproduction of coffee capital as a whole. In the process of production, coffee agriculture incurred certain determined costs — the depreciation of fixed capital, wages, commercial and financial charges, transportation costs, and taxes — and also realized a profit. Those expenses relating to commerce, finance, and transportation also represented income for their respective sectors, which, in turn, was converted into the depreciation of fixed capital (railroads, port facilities, commercial buildings, etc.), input costs (fuel, etc.), payrolls, taxes, and profits.

Furthermore, we can assume that taxes would be used to acquire means of production and to meet payrolls, and that profits would be divided between the consumption of luxury goods (capitalists' consumption) and accumulation, and that wages would be devoted entirely to the purchase of food and manufactured consumer goods. It is clear, then, that coffee production simultaneously comprehended a demand for land, labor, and means of production on the side of accumulation, and a demand for foodstuffs, wage goods, and luxury goods on the side of current expenditures.

Both the accumulation of means of production and capitalists' consumption were financed with the importing capacity generated by the coffee export complex itself. However, once Brazil's commercial food production had expanded and an industrial sector was in place, domestic output could attend to the demand for food and manufactured wage goods, at which point the reproduction of labor became internalized.

The movement of coffee capital tended to follow a cyclical pattern, which was accentuated to some degree by the nature of official economic policy. The "natural" cycle of coffee production followed from the fixed character of cultivation, in particular the maturation period of four to five years. Thus the supply of coffee was inelastic in the short run and responded slowly to variations in external demand (which responded to fluctuations within the importing economies).

Expansion began with a rise in external prices prompted either by prosperity abroad (which boosted demand) or by a contraction in supply owing to climatic factors. The rise in external prices would be transferred to domestic prices according to the movement of the exchange rate. Profits would climb and the rate of accumulation would increase or not, depending on profit expectations. On the assumption that new investments would prove lucrative, additional productive capacity would be created. Once the young coffee trees began producing, world and internal prices would fall in relation to, respectively, conditions abroad and the evolution of the exchange rate.

The rate of return would diminish, gradually retarding accumulation, and a period of depression would begin.

When we look more closely at the impact of a decline in external and internal prices on the coffee export complex, we must necessarily distinguish among (1) productive capacity in use, (2) productive capacity under construction, and (3) the projected increase in productive capacity.

The first obviously consists of the coffee trees actually producing. Some planters in the productive nucleus barely managed to cover their monetary costs and became marginalized because their plantations were located on low-yield lands and their trees, on the average, had passed the optimum age for maximum productivity. When depreciation is taken into account, these enterprises showed negative rates of return. In contrast, the intramarginal producers enjoyed positive profit rates that, nonetheless varied according to soil fertility, the average age of their coffee trees, and freight charges, which reflected proximity to the ports of embarkation.

Productive capacity under construction includes the young coffee trees planted but not yet producing. At this stage, money costs consisted entirely of wages and the servicing of the bank loans inevitably contracted at some point to meet payrolls and/or to purchase land.

Finally, the desired rate of increase in productive capacity refers to the number of new seedlings the planters hoped to cultivate. This was largely determined by profit expectations.

The initial result of a decline in external and internal prices would be a reduction in the profit margins of working enterprises, part of which would immediately be absorbed by a fall in money wages. Marginal producers, together with the least productive intramarginal planters, would be ruined and a portion of the coffee sector's productive capacity would be wiped out. The proprietors of new trees that became productive during the depression would find themselves near insolvency, unable to meet their bank debts; the planting of new seedlings would cease altogether.

The crisis originating in the productive nucleus would soon spread to the urban branch of the export complex. It would not only engulf the commercial-financial and transportation sectors but would affect industry and commercial food and raw material production as well (once these were established). The fall in income would curtail the demand for imports and lower government revenues, which were based on tariffs; and this would provoke a new cut in demand, assuming policymakers sought to balance the budget.

In the worst of hypotheses, the crisis would have run its course when the coffee export complex reached its lowest point — when intramarginal producers could cover only their monetary costs and capitalists' consumption. Then, under the combined stimulation of a diminished productive capacity on the one hand, and the reactivation of external demand (reflecting conditions within the importing countries) on the other, recuperation would begin.

In sum, the development of the capitalist coffee export economy not only responded to cyclical movements within the importer nations but was also governed by factors operating on the side of supply, in particular the four- to five-year delay between planting and the first harvest.

Moreover, while the *duration* of expansion and depression was clearly tied to fluctuations within the importing economies, it further depended on the economic policies of the government. This is not to say that policy was formulated in a vacuum, but that, given the structural exigencies imposed by the pattern of accumulation, official policy could strengthen expansion or deepen depression.

The First Coffee Cycle (1886-1918)

During the years 1886 through 1897 the coffee economy enjoyed a period of remarkable growth. Average production climbed from 5.2 million bags[*2] between 1886-1887 and 1890-1891 to 6.5 million bags between 1891-1892 and 1895-1896. Then, in the years 1896-1897 to 1902-1903, when the coffee trees planted from 1891 to 1897 became fully productive, average output reached 11.4 million bags.[8] For the most part, expansion took place in the state of São Paulo. That region's installed productive capacity — that is, its stock of coffee trees — trebled from 220 to 665 million plants between 1890 and 1902, while its share of Brazil's total yield increased from 40 percent in 1885 to 60 percent at the turn of the century.[9]

At the time conditions were extremely favorable for accumulation. The extension of the railroad system opened new lands for coffee cultivation, while mass immigration generated a labor supply that was more than sufficient to satisfy the urban and rural requirements of the coffee export complex. Between 1888 and 1900 nearly 1 million immigrants arrived in Brazil, 890,000 of whom settled in São Paulo.[10] Economic changes in Europe in the last two decades of the nineteenth century had led to the formation of an international labor market composed of large contingents of unemployed workers disposed to emigrate. It is well known that during the 1880s central-north and western Europe were the principal points of origin, while during the 1890s the source shifted to southern Europe, to Italy in particular. Ninety percent of all newcomers to Brazil in this period came from southern Europe and the Italians alone represented 60 percent of the total.

*2 One bag equals 60 kilos.

Considering the North American and Argentine competition for labor, the existence of a large pool of free laborers in the international market does not by itself explain the strong current of migration to Brazil. As it happened, however, the diversionary effect of competition faltered during the 1890s as the North American economy entered a period of crisis (1893—1897) and the Argentine economy stagnated. Douglas Graham explains:

> In sum, the indicators strongly suggest that around 1885—1906 the cyclical prosperity of the Brazilian economy became less dependent on the cyclical movements of the American, Argentine, and Italian economies. This fact played an important part in permitting Brazil to import so large a number of immigrants (principally Italians) during the 1890s. It would in fact have been difficult, if not impossible, for Brazil to attract so many immigrants if the Argentine, and particularly the North American, economies had been expanding, and if the Italian economy had been prospering as well.[11]

Thus special conditions at work in the international labor market explain both the abundant supply of labor on hand for the coffee export complex and the prevailing levels of wages (see Table 1).

Wage scales such as those registered during the 1890s were possible only because the coffee complex was able to minimize the effects of the poor development of domestic commercial food production and manufacturing on the physical reproduction of the labor force and on its cost by importing necessary wage goods. The importation of wage goods was substantial, and allowed by an increase in the value of exports in the period.[12] (see Table 2). At the same time, export receipts facilitated the purchase abroad of means of production both for the urban and rural components of the coffee export complex and for the installation of a domestic wage goods industry.

The enlargement of Brazil's importing capacity reflected favorable marketing conditions abroad. Although currency appreciation absorbed a good share of the increment, international coffee prices climbed from 10.7 U.S. cents per pound in 1886 to 20.0 cents per pound in 1891. Together the growth of world markets—particularly that of the United States—and the poor harvests of 1887—1888 and 1889—1890 stimulated this upswing.[13] When coffee groves planted under the influence of this price trend began producing in 1891, North American prosperity (which, unlike that of Europe, lasted until 1893) helped prevent a dramatic fall in international prices. More important, when the demand for coffee began to falter, the currency depreciated sharply, which had the effect of elevating internal prices between 1891 and 1894 and cushioning their fall between 1895 and 1898 (see Table 3).

The result of all this was a sustained rise in profit margins between 1886 and 1894. In the first part of this period (1886—1890) profits expanded in response to the upward movement of all prices and the marked contraction in money wages; and from 1890 to 1894 profits continued to grow — despite the decline in international prices — because the increase in internal prices was proportionally greater than the rise in money wages. Even when the subsequent stability of money wages that was accompanied by a decline in internal prices cut profit margins between 1895 and 1898, the reduction was less than it would have been had the fall in world prices been transferred whole to domestic prices. Thus currency depreciation was intimately linked to the prolonging and acceleration of expansion between 1891 and 1894, and to the defense of profit margins between 1895 and 1897.

The coffee crisis broke in 1898 and continued until 1906, since the government had little alternative but to give free rein to market forces. External coffee prices fluctuated between 7 and 8 cents per pound from 1897 to 1906, but internal prices fell after 1900 because of currency appreciation (see Table 4).

The severity of depression depended, above all, on the flexibility of money wages and, as the figures in Table 5 indicate, wages did decline substantially. Thus, grave though it was, the crisis affecting the coffee export complex was more restricted than it would appear at first glance. Further proof of this assessment is the fact that the volume of coffee production and of exports grew appreciably in these years, while the value of exports recuperated to the level registered in 1894.[14]

With the boom in rubber exports, Brazil's import capacity was greatly enlarged and, given the decline in imports and the Funding Loan of 1898, ultimately generated a pronounced currency appreciation (see Table 6). Nevertheless the movement in the exchange rate had a dual effect on the coffee economy: it lowered domestic coffee prices, as we have noted, but it also reduced the cost of imported commodities purchased by wage earners, thereby contributing to a reduction in wages themselves.

Money wages declined not only because of the impact of the coffee crisis on the demand for and cost of labor but also because of the depressed state of the industrial sector. Industrial problems derived in the first instance from conditions within the coffee complex, but they were aggravated by a cut in government spending and by a contractionist monetary policy. Given this set of circumstances, the available evidence indicates that internal prices fell approximately 30 percent between 1899 and 1901, so that while money wages deteriorated, there was no appreciable reduction in real wages.[15]

In sum, because the profit margins of intramarginal producers most certainly had been very high in the previous period, and because money wages proved flexible, most of the installed productive capacity within the coffee sector was preserved at the cost of a pronounced urban crisis. Furthermore, the incomes of enterprises within the productive nucleus remained at elevated levels.[16]

Nevertheless, precisely because most productive capacity was left intact, the gathering of large harvests continued to exert pressure on the coffee market. At the same time, the currency appreciated further, stimulated by the level of receipts from coffee and rubber exports and by the inflow of foreign capital after 1903. This was the state of affairs in 1906, when predictions of an unprecedented harvest threatened to intensify the existing crisis.

As is well known, relief came in the form of the coffee valorization policy embodied in the Taubaté Agreement of 1906. In terms of its objectives, this price-support scheme was unquestionably successful: internal and external prices were held steady until 1909 and climbed between 1910 and 1912, while the exchange rate remained constant (see Table 7).

In addition, productive capacity was stabilized until 1910; only 38 million new trees were cultivated in the state of São Paulo between 1907 and 1910, in contrast to the 460 million planted between 1886 and 1897. Not surprisingly, a new expansive phase began to take shape in the years 1911-1913, when approximately 99 million seedlings were planted in São Paulo. However, this new phase, prompted by rising international and internal prices, was cut short by World War I.[17]

Between 1912 and 1913 world coffee prices declined from 13.8 to 10.1 U.S. cents per pound. However, with the wartime collapse of the balance of payments situation, a depreciation of about 30 percent bolstered internal prices. Devaluation, together with a slight decline in money wages, eased the coffee crisis, but in view of the volume of existing coffee stocks the outlook for 1917 was not particularly encouraging:

> In 1917, with the harvest complete and no way to export it (given the resumption of submarine warfare), coffee stocks accumulated in national ports reached alarming proportions. Reserves in the port of Santos passed from less than a million bags in July of 1916, to nearly six million in July of 1917. In such circumstances the price of coffee in national currency would surely plunge to an extremely low level, probably inferior to the average cost of production.[18]

Furthermore, a bumper crop was predicted for 1917-1918. In response to this forecast and to the growing reserves of coffee, the São Paulo government secured a loan from the União to implement a second valorization program, which withdrew 3.1 million bags of coffee from the market at a cost of 4.9 mil réis per 10 kilos. This second valorization scheme was crucial in sustaining prices and in preventing a worsening of the coffee crisis, especially when one considers that in 1917 the currency appreciated. Quite apart from the valorization program, as early as 1918 international prices advanced significantly when a frost damaged Brazil's coffee trees and reduced the size of the harvest. Favored by a nearly stable exchange rate, internal prices rose by nearly 15 percent.

The Expansive Phase of the Second Coffee Cycle, 1919-1929

The coffee export complex enjoyed a period of renewed and remarkable expansion during the 1920s. Production that had averaged about 14.1 million bags between 1914-1915 and 1918-1919, as well as between 1919-1920 and 1923-1924, increased to an average of 18.2 million bags in the years 1924-1925 to 1928-1929. Then, from 1929-1930 to 1933-1934, when the trees planted in the second half of the 1920s became fully productive, average output reached 24.2 million bags.[19]

Once again circumstances favored accumulation. Fertile lands suitable for coffee growing were readily available and the workforce supply was elastic. The coffee economy had at its disposal a good part of the natural increment in the economically active populations of the coffee states of São Paulo, Minas Gerais, and Espírito Santo. And coffee entrepreneurs also drew on a growing current of internal migration and on renewed foreign immigration—of which the Japanese constituted an ever-greater share.[20]

The other branches of the Brazilian economy exhibited scant growth in this period and thus offered little competition for the expanding supply of labor. To illustrate the relatively poor performance of the non-coffee export sectors in these years, suffice it to say that coffee's share of Brazil's total exports passed from 56 percent in 1919 to an average of more than 70 percent in the second half of the 1920s. The evidence further indicates that both industrial and commercial agricultural output registered comparatively low rates of growth in this period.[21]

Apart from the abundance of land and labor, both international and internal price movements (see Table 8) greatly encouraged coffee expansion during the 1920s. This came about not only because the prosperity of the industrialized nations spurred the growth of markets but also because it was possible to have constant recourse to coffee-support programs.

Taking the 1920s *as a whole*, the very auspicious conditions of accumulation and realization explain the fact that within the Brazilian economy almost the only dynamic sector was the coffee sector. However, this generalization must be qualified by pointing out that the decade actually bracketed two subperiods, 1919-1923 and 1924-1929, each of which exhibited its own characteristics of growth.

The increase in production registered between 1924-1925 and 1928-1929 attests to the marked acceleration in accumulation that occurred in the coffee sector between 1919 and 1923. Looking first at commercialization, we see that in 1919 and 1920 the international price of coffee attained the high level of 19.5 U.S. cents per pound—nearly the same price prevailing in 1890. This trend can be explained by two factors: frost damage in 1918 reduced the harvests of 1918-1919 and 1919-1920, while in 1918-1919 speculators undertook to rebuild their depleted inventories in the aftermath of war. Internal prices did not gain so much at this time because of currency depreciation.

A sudden downturn in the North American economy, together with predictions of yet another large harvest, diminished coffee prospects in 1921. However, the implementation of a third valorization program in 1921, followed by the unremarkable yields of 1921-1922 and 1922-1923 and the recovery of the U.S. economy in 1922, checked the sharp decline in external prices and even promoted their slight recuperation in 1922 and 1923. Meanwhile, internal prices increased substantially between 1921 and 1923 owing to a profound currency depreciation.

In the first period we are examining, then, internal prices advanced at an accelerating pace, moving from 47.4 to 146.9 mil réis per bag of coffee between 1918 and 1923. The rural wages paid by coffee producers also rose at this time, but not so much as prices, and, accordingly, profit margins in the coffee business expanded considerably.[22] It should be underscored that coffee accumulation in these years was not self-sustaining and could proceed only insofar as expanding domestic industrial and commercial food production contributed to the reproduction of the labor force. That is to say, in 1920 and 1921 the buying power of exports diminished substantially and recuperation in 1922 and 1923 was not sufficient to mitigate the balance of payments crisis. Since the coffee sector could not generate enough foreign exchange to import the required volume of wage goods, it necessarily relied on the growth of internal production to take up the slack.

In sum, the years 1919 to 1923 were characterized by the combined expansion of the coffee export complex, of primary commodity production, and of industry. The accelerated pace of global accumulation permitted an improvement in rural and urban money wages that culminated in the high level of 1923—a year of extensive coffee planting and notable industrial growth.[23]

The pattern of expansion in the period 1924-1929 offers a striking contrast. International prices climbed to 17.5 U.S. cents per pound in 1924 and thereafter stabilized at around 20-21 cents. Until 1926 internal price behavior followed a somewhat less spectacular course, owing to the currency appreciation resulting from increased exportation and a greater influx of foreign capital. To break this pattern the government created a Stabilization Fund (Caixa de Estabilização), which was designed to operate in much the same way as the earlier Conversion Fund. The currency was devalued by 20 percent and held at about 40 mil réis to the pound sterling until the crisis of 1929.

The very positive price trends in these years can be explained by the evolution of external demand and, above all, by the operation of the Permanent Defense Policy initiated in 1924. Unlike earlier programs, the objective of the Permanent Defense was not to prevent a fall in prices, but rather to maintain coffee prices at high levels.

Rural money wages deteriorated between 1924 and 1927, but recovered in 1928 and 1929 in response to the quickening rhythm of coffee accumulation and a certain degree of industrial growth. In consequence, profit margins widened in 1924 and must have held fairly constant thereafter.[24]

In contrast to the previous period, however, coffee was solely responsible for economic expansion between 1924 and 1929. The value of exports averaged 93.5 million pounds sterling per year in comparison to 74.6 million pounds sterling per year between 1919 and 1923. The terms of trade improved significantly and the inflow of foreign capital grew markedly.[25] Accumulation within the coffee sector no longer depended upon the enlargement of domestic industrial, food, and raw material production; in fact, these sectors were not subjected to intense external and internal competition. The autonomy of the coffee complex discouraged increases in the prices of wage goods, which would have pushed wages up and reduced profits.

For all this, the prosperous years 1924 to 1929 harbored the makings of a general crisis in the export complex that would break abruptly in the 1929-1930. The internal symptoms were discernible from 1926 on, and the serious implications of the ceaseless overproduction promoted by the Permanent Defense Policy were brought home by the record harvest of 27 million bags of coffee in 1927-1928. Thus, as we will see at the end of the next part of this essay, the calamitous economic situation abroad did not create the Brazilian crisis in 1929; it only exacerbated an already critical state of affairs.

Coffee accumulation and economic policy

The Economic Policy of the First Republic: An Overview

There are two prevailing views of the economic policies of the First Republic. One holds that the vagaries of fiscal, monetary, and exchange policy resulted from the constant shifting between austere and permissive, or between liberal and protectionist, governments.[26] The second characterizes policy history as a series of expedients designed to serve the short-term interests of "the coffee oligarchy and its foreign ally — international finance capital." From this second perspective, the narrow range of internal and external policy is attributed to the dependent position of the Brazilian economy in the world market.[27]

It is our contention that neither of these interpretations fully appreciates the contradictory nature of economic policy between 1889 and 1930. The belief that everything can be ascribed to the whims of those who govern, or worse, to their ignorance of the sacred principles of Economic Theory, merits little comment since it disregards what is elemental: that any economic program is elaborated by a given state and is implemented to serve the concrete demands of classes and interest groups. The second and quite different interpretation can also be dismissed because it fails to take into account either the relationship between decision making and the cyclical dynamics of the coffee economy, or the precarious economic and political foundations of the Brazilian state.

We can begin by approaching the question of economic policy in general terms. Public finances were largely determined by the fluctuations of external trade, and it fell to the central government to levy import duties, while the state governments were empowered to tax exports. The financial frailty of the Brazilian state was therefore twofold: because the coffee sector represented the government's principal source of receipts, federal revenues were dependent on the cyclical behavior of the coffee economy. On the other hand, state incomes, which were similarly tied to foreign commerce, were unequally distributed; in reality, only the coffee states possessed a stable tax base. Yet a government that functioned without benefit of an integrated national market, and was unified by the preeminent interests of only a minority of truly national classes, nevertheless was a national body; and as such, it was compelled to consider the needs and demands of other classes and interest groups in formulating spending policy. In those years when exports were expanding, the pressures on federal spending were intense, both for attending to export requirements, however indirect (for example, those related to the urbanization of Rio de Janeiro), and for meeting the more urgent regional needs that tended to accumulate and fester during times of depression.

Fiscal deficits inevitably developed despite the efforts of the government to augment taxes. The impossibility of permanently carrying and financing such deficits by expanding the means of payment led to a persistent increase in external indebtedness — precisely because the growth of exports facilitated the negotiation of foreign loans. It became ever more difficult to cover the public debt, and even before they reached a critical state, public finances showed signs of deterioration, evident in the evolution of the exchange rate or in budgetary overruns. When the crisis arrived, falling revenues threatened the state with internal and external bankruptcy. Whether because of this calamitous financial situation or because of the near collapse of the balance of payments, further enlargement of the external debt was out of the question and renegotiation became the order of the day.

Thus, to guarantee its own survival, the government found it necessary to cut short expansion and to anticipate and even deepen the crisis by curtailing spending, elevating tariffs, and attempting to broaden its fiscal base. To be sure, all these measures were undertaken with the understanding and encouragement of the international bankers, who always recommended sound fiscal measures in such circumstances in order to ensure that commitments would be honored.

The question naturally arises as to why, given increased urbanization and a rapidly expanding internal capitalist market, the federal government did not raise its revenues through internal taxation in the interest of greater financial autonomy. The contention that the coffee oligarchy and foreign bankers were responsible for the failure of the excise or income tax as an alternative source of revenue is far too simplistic. The agro-export oligarchy would have been affected far more by a tax on its patrimonial base or by the removal of the export tax — measures obviously never contemplated by the administrations of the First Republic. But from the beginning, both the sales and the income tax were considered. Why, then, did the state fail to implement these measures, which would have strengthened it financially?

As it happened, in Brazil, as in the rest of Latin America, internal taxes proved workable only when the economic base of the urban masses had expanded sufficiently to support the cost of taxation. The elite groups and the petty rural and urban bourgeoisie never bore the brunt of, or submitted gracefully to an increase in, the internal tax burden. Without a decisive advance in industrial accumulation to promote the formation of a large urban proletariat, a tertiary sector based on salaried labor, and a growing bureaucracy of petty functionaries, the objective conditions for creating an adequate urban fiscal base and for freeing the government from its financial dependency on external trade did not exist.

The increments in internal taxes actually registered were effected erratically and were essentially emergency expedients (such as raising rates or diversifying rate schedules) designed to counter the worsening of deficits. Only with the coming of the Vargas regime (and particularly the Estado Novo) and the emergence of a new phase of capitalist development did the state begin to augment internal tax revenues. It was only after 1937 that the contribution of import duties to total revenue diminished, and income and excise taxes (besides the stamp tax) gradually assumed a preponderant position in public finances.[28]

Having explained the inevitable shifts in fiscal policy, it is appropriate to add a few comments on monetary and exchange rate management. At the start of an expansive phase the enhanced buying power of exports — in all likelihood reinforced by new infusions of foreign loan and venture capital — brought pressures to revalue the currency. To avoid currency appreciation, which would imply a reduction in the profits of exporters, the government was prevailed upon to establish support mechanisms. Thereafter, the increase in the rate of accumulation — which was necessarily sanctioned by monetary policy — inasmuch as it found no support in the growth of importing capacity, inevitably led to deepening balance of payments difficulties. Currency devaluation emerged then as the only admissible course of action, becoming at times an instrument of anticyclical policy. In times of crisis — which devaluation could not prevent — the state had little recourse but to apply orthodox fiscal and monetary measures in order to restore fiscal and external equilibrium; such measures not only accepted, but actually accentuated, a fall in employment and income. When export receipts were growing, in response to a greater volume of exports and perhaps to a slight rise in world prices, the balance of payments situation eased and the currency tended to appreciate, especially if the foreign debt had been renegotiated.

Thus at times the state found itself in the position of utilizing currency devaluation even when the income from exports was still rising, and with it coffee profits, the *ad valorem* tariff, and protection to industry. On the other hand, under the accumulated pressure of external commitments and the need to refinance the public debt, the government was obliged at times to revalue the currency in spite of a decline in international coffee prices, and, in doing so, to cast aside both the precarious profitability of the coffee sector and industrial protectionism.

Similarly, we can see that the coffee bourgeoisie promoted an official economic policy that repeatedly ran counter to its own immediate interests in order to serve the larger interest of preserving the existing machinery of government and the balance of political power.

We can further note the relative ease with which the coffee bourgeoisie periodically secured and extended foreign loans, even without the backing of the federal government. This was possible in the first place because of the autonomy of state governments and the particular influence wielded by coffee interests. Their semimonopolistic position as exporters with diverse markets that were not controlled by a monopoly of buyers, greatly expedited negotiations with a variety of commercial and financial groups within international capital. In addition, the change in the relative importance of North American versus British finance capital (beginning with World War I) provided some leeway to those Latin American nations not strictly dependent on Britain.

Having offered these general comments, we can now reconstruct Brazilian's economic policy from the beginning of the First Republic to the crisis of 1929.

The Period 1886-1898

During the years 1886 to 1898 important political, economic, and institutional changes took place that were connected to two decisive historical events: the abolition of slavery in 1888 and the proclamation of the Republic in 1889. Policymaking in the first years of the Republic addressed several serious problems of internal and external financing built into the cyclical character of the coffee economy and aggravated by the particularly unfavorable financial conjuncture inherited from the Empire. Scarce liquidity (which had become more acute in the last decade of the Empire), an enormous public debt, and the financial turmoil that followed abolition in all agricultural regions except São Paulo all prompted the first administration to undertake fundamental banking and tax reforms that, nonetheless, succumbed to the financial crisis of 1891 known as the *Encilhamento*:

> The emphasis placed in our literature on the "monetary chaos" and the "avalanche of paper" that characterized the *Encilhamento*, with its enormous monetary expansion and currency depreciation, obscured for a long time the true significance of effective accumulation in the period. Arguments that seek to demonstrate that any potentially positive effects obtained from expanding banking operations and the means of payment would have been nullified or offset by currency depreciation and by the rise in internal prices — both of which would augment the costs of internal investment and production — or others that view the *Encilhamento* as a period of "internal paper speculation and ghost enterprises," contribute little to our understanding of the era.[29]

The significance of reforms implemented under the early Republic and the general lines of economic policy up to the crisis of 1899 appear to be the following: the banking reform that empowered private banks to issue paper money was largely an effort to expand the sources of liquidity and internal financing and to separate them from the fluctuations in the public debt and in external trade that severely hamstrung federal monetary and financial policymaking. The law further permitted banks to engage directly or indirectly in extra-banking activities through the creation of corporations, thereby transforming financiers of current activities into active agents of capital accumulation.

The race between monetary expansion, currency depreciation, and rising prices was translated, however, into an open and unrestrained inflationary process. If inflation favored the accumulation of urban capital in this period, it also created internal financial disorder, which, together with the requirements of renegotiating the external debt, led to the adoption of a series of exchange stabilization measures. The first of these, in 1896, provided for the suspension of decentralized emissions and the replacement of bank notes by treasury notes. Reform continued with the negotiation of foreign credit to establish an exchange stabilization fund, and culminated with the drastic stabilization and exchange revaluation plan (1899) designed by Joaquim Murtinho, Minister of Finance in the Campos Salles government.[30]

The central problem of tax reform at this time was the same: that of maintaining fiscal revenues in real terms and avoiding repeated and sizable losses due to currency fluctuations. For this purpose a gold quota was established in 1890; however, it was soon abolished (1891) with the argument that the currency depreciation and the resulting rise in wage costs made it extremely difficult for buyers to pay customs duties in gold. Thereafter tariffs were levied *ad valorem* according to the official schedule set in 1890. Since currency depreciation persisted until 1899, customs receipts did not hold their own in real terms as a proportion of imports. This obliged the central government to resort to successive elevations in customs duties, including a general tariff revision in 1896. Yet once again effective tariff reform was blocked because of the adverse impact it had on the cost of living. In spite of a declining importing capacity and the corrosive effect of currency depreciation on fiscal receipts, the government in 1897 decreed a new tariff schedule that was 25 percent lower than that of the previous year.[31]

Given the uncertain progress of tariff reform and its own inability to broaden its tax base, the federal government was forced drastically to curtail expenditures related to consumption and, particularly, to investment. Even so, it could not prevent the growing accumulation of budget deficits after 1892.[32]

The public debt was financed in part by paper issues but primarily by the expansion of the external debt, which grew by approximately 30 percent between 1890 and 1897. This, in turn, fed internal inflation. Because the external debt had to be amortized in hard currency, debt servicing absorbed an ever-greater proportion of fiscal receipts. Moreover, since both exports and imports began to decline after 1896, the rapidly failing ability of Brazil to meet and extend its foreign commitments produced the near-insolvency that necessitated the funding loan that was part of Murtinho's broad stabilization program.

Before we examine the crisis of 1899 and the serious stabilization policy pursued by the Campos Salles/Murtinho administration, we will digress for a moment to clarify the problem of currency depreciation and its contradictory character vis-à-vis the cyclical movement of coffee accumulation.

The Contradictory Character of Currency Depreciation

The essential point to be made here is that currency depreciation derived, above all, from the cyclical dynamics of the accumulation of coffee capital. To the degree that the rate of accumulation quickened in response to the internal and external prices that prevailed in the previous stage of the economic cycle, it placed additional pressure on Brazil's importing capacity — at precisely the time when the purchasing power of exports was declining in response to "new" and lower international prices. At this point any attempt to restore equilibrium through the rules of the gold standard would have a drastic effect on current profit rates within the coffee economy. It was in this context that devaluation emerged as the one course of action that would simultaneously curtail the excessive demand for imports and preserve, for better or for worse, profit margins and capital accumulation in the coffee sector.

Depending on whether public spending was expansionist or contractionist, official policymaking obviously furthered or arrested depreciation; furthermore, the steps taken to finance the public debt either stimulated or retarded accumulation in the coffee complex, particularly in its urban division. Nevertheless, we must not lose sight of the fact that persistent currency depreciation originated in the global process of accumulation in the coffee complex; it did not derive — as has been claimed by those who favor "structuralist" explanations — from the special interests of the export entrepreneurs. The view of Furtado in this respect has gained wide acceptance:

> In the ultimate analysis, the process of correcting external disequilibrium implied an income transfer from those who paid for imports to those who sold exports. Since imports were paid for by the community as a whole, the exporters were actually promoting the socialization of the losses which economic mechanisms tended to concentrate on their profits.[33]

Yet the problem is considerably more complex once we abandon the exporter-importer dichotomy, which Furtado uses as a point of departure, and incorporate the concept of coffee capital into our explanation. From this perspective, a substantial proportion of coffee accumulation consisted of urban accumulation, which necessitated the importation of means of production and absorbed a significant part of the immigrant labor force. Inasmuch as the reproduction of labor in the productive nucleus and in the urban sector also required the overseas purchase of food and manufactured wage goods, this process further strained Brazil's import capacity. We have noted elsewhere that the percentage of wages used to buy imported commodities was particularly high during the first short cycle of coffee expansion. Thereafter this share diminished, as coffee prosperity itself stimulated domestic food production and engendered the large-scale production of consumer wage goods, both of which began satisfying a growing part of internal demand.

While currency depreciation did have the effect of elevating the costs of both the means of production and the reproduction of the labor force, it does not necessarily follow that the favorable impact of devaluation on coffee accumulation was therefore neutralized, or that the increments in internal costs were "socialized" or paid by "the community as a whole."

In fact, the critical determinant of profit margins within the coffee complex was not the escalation in the cost of imported means of production provoked by currency depreciation, since this was proportional to the rise in internal coffee prices and did not, on the average, modify the price-cost relationship of constant capital. Rather, the decisive factor had to do with *variable* capital, that is, with the determination of the cost of wages.

Because wages increased less rapidly than prices, the profit margins of *all* entrepreneurs, not just exporters, rose throughout the period of devaluation; at the same time, internal prices climbed and real wages fell concurrently, approaching intolerable levels for the subsistence of the urban labor force. In other words, in the last stage of coffee's expansive cycle, the "socialization of losses" was accomplished above all at the expense of wage earners.

At a certain minimum level of subsistence, however, money wages tended to become rigid and so could no longer offset the fall in the domestic price of coffee. At this point, devaluation was demonstrably incapable of cushioning the fall in international prices. Certain latent tendencies in the economy became apparent with a corresponding narrowing of profit margins in the coffee sector that could not be counterbalanced by intensifying the rate of labor exploitation.

If the more moderate but persistent currency depreciation registered between 1895 and 1898 was not sufficient to maintain current profit margins in the coffee sector, it nevertheless prevented a sharp decline in returns, and continued to produce a growing disparity between domestic and external prices. This spurred further accumulation (in spite of the pronounced decrease in coffee prices), which later aggravated the general crisis of overproduction, a crisis from which producers would only extricate themselves with the first valorization plan of 1906.

On the other hand, devaluation continued to favor the industrial sector until the general crisis of 1899 and the implementation of Murtinho's stabilization and exchange revaluation policies. Infant industry had already benefited from tariff and exchange rate protection, as well as from the period of easy credit (1890-1894) promoted in the first years of the Republic to stimulate investment.[34] By utilizing the productive capacity installed earlier to strongly expand both current output and profit taking, the industrial sector managed to live with a restricted importing capacity — made worse by the fall in exports. In other words, infant industry was self-financing in the years 1895 to 1899 in spite of the monetary and credit restraints exercised by the federal government to combat inflation.

Thus a currency devaluation policy originally conceived as a means of supporting the coffee export complex, in practice, encouraged capital accumulation in the industrial sector and actually intensified the cyclical movement of the coffee economy, thereby precipitating a profound crisis that affected not only coffee but the financial foundations of the central government as well.

The serious contradictions of devaluation were particularly evident in its impact on public finance. Although they were genuinely alarmed by real losses in revenues from import duties, policymakers nevertheless faced a dilemma: not raising tariffs meant that public receipts would lose even more ground, which was tantamount to accepting the financial ruin of the state. On the other hand, an upward revision of the tariff schedule to offset real losses in income would escalate the cost of living and, therefore, of wages, and would reduce the already fragile profit margins of the export sector.

The reactions of the coffee bourgeoisie were equally contradictory. As long as profit margins were expanding, the coffee economy could tolerate some fiscal pressure to prevent too great an erosion of government revenues; however, when profit margins narrowed, coffee interests demanded a reduction in tariffs and in the level of protection afforded to industry.

The decision to limit the tax burden and maintain expenditures at a minimum signified still greater reliance on external indebtedness as a means of financing the federal deficit. However, declining fiscal receipts sharply diminished the government's ability to meet its foreign obligations. Eventually the impossibility of amortizing accumulated debts necessitated a comprehensive renegotiation with creditors abroad.

The Crisis of 1899 and Economic Recovery up to 1913

The crisis that had been averted between 1891 and 1894, and relatively contained between 1895 and 1896, began emerging in 1897-1898 and broke near the end of 1898, when the Campos Salles administration took office. The new administration simultaneously confronted two grave problems: falling internal and external coffee prices and the financial bankruptcy of the state.

There were clamors for official intervention to solve the coffee problem; the government was to withdraw surplus production from the market with the objective of "valorizing" the product by boosting, or at least preventing a fall in, international prices. This course of action was hardly feasible, however, because the government lacked the means to finance it except through money issue, a move that would generate inflation, depreciation, and a general worsening of the already critical state of public finances. Neither could the Brazilian government resort to further borrowing abroad at this time, since it was already incapable of meeting its commitments and was seeking a funding loan from its international creditors. The only solution that remained was to live with the coffee crisis. Minister of Finance Murtinho observed:

> In relation to present consumption, the cultivation of coffee can be considered to be composed of two elements: one established in fertile soils, favored by climate, and undertaken by intelligent agriculturists in good economic circumstances; the other established in inferior lands and climates by routine-bound growers in poor economic conditions.[35]

He concluded:

> Convinced that official intervention would only increase our difficulties, the government permitted coffee production to decline through natural selection. Those unequipped for survival were eliminated, leaving production in the hands of the most hardy and best prepared for the struggle.[36]

It was decided, then, to allow the coffee crisis to run its course through the free operation of market forces. As a result, the "coffee problem" drew out until 1906, when intense and mounting pressure for a price-support policy led to the signing of the Taubaté Agreement and intervention by Campos Salles' successors.

In order to deal with the desperate state of public finances, the Murtinho ministry adopted a series of austerity measures that deepened the rural and urban crisis. To begin with, the government responded to the balance of payments emergency by establishing a gold tariff requiring that 10 percent of the value of import duties be paid in specie, to which another 5 percent would be stabilized. The accomplishment of this objective beginning in 1902 was due in large part to the impact of the funding loan of 1898, which consolidated external debts — whose servicing had come to greatly exceed the capacity to pay afforded by the balance of trade — and suspended amortization payments for thirteen years.[37] Furthermore, by 1902 a new foreign loan secured in 1901 had steadied the exchange rate market and the currency appreciated until the end of 1906, when the valorization scheme went into effect.

A second set of expedients addressed the problem of budgetary equilibrium and provided for higher internal taxes and the withdrawing of excess paper money in circulation. These measures can be classified as "internal" even though they were the terms imposed by overseas creditors in exchange for refinancing the foreign debt. This illustrates, once again, the degree to which "internal" and "external" policy measures were intertwined even while the general economic policy of which they were part was essentially contradictory in nature.

As a result of the stabilization program, internal prices declined by 30 percent between 1900 and 1902. Deflation was severely felt in all economic activities and even provoked a bank panic.[38]

Having attained the desired budgetary equilibrium, a new government began to pursue a vigorous investment program in 1903, preserving, nonetheless, the essential lines of existing monetary and fiscal policy. Aimed primarily at the transportation infrastructure (railways and ports) and at urban improvements, investments were intended to remedy deficiencies accumulated during nearly a decade of paralysis of capital outlays in the federal public sector.

This investment effort was consciously undertaken as a "program of economic reconstruction" that would later be substantially expanded and would generate new and large budget deficits. This time, however, deficits emerged within the context of steadily growing federal receipts, provided by recuperation itself beginning in 1903. The program proved viable in part because the ever-higher level of exports and of foreign borrowing (particularly in the form of loans for public works) facilitated the importation of needed capital goods.[39]

Urban improvements and general economic recovery offered a striking contrast to conditions within the coffee sector, where the structural crisis continued unabated. The considerable inflow of foreign capital and the boom in rubber exports had improved the balance of payments, but the ensuring currency appreciation in no way benefited coffee producers who, given the relentless gathering of large harvests, remained engulfed in a crisis of overproduction.

When a record harvest was predicted for 1906, pressures for official intervention could no longer be ignored and the Agreement of Taubaté was formalized with the following objectives: (1) to maintain coffee prices at between 55 and 65 mil réis a bag; (2) to negotiate an external loan of 15 million pounds sterling to finance intervention in the market; (3) to tax the planting of the new coffee trees; (4) to create a conversion fund designed to stabilize the exchange and prevent appreciation; and (5) to prohibit the exportation of low-quality coffee.[40] In sum, the coffee bourgeoisie that controlled 75 percent of the world's production resolved to utilize its monopoly power as a class to manipulate international prices.

The chief obstacle at this point was the difficulty of securing the foreign funds necessary to finance the withdrawal of coffee "surpluses" from the market. When skeptical European and North American bankers declined to offer their backing, the government of São Paulo turned to private European commercial groups, who agreed to supply 80 percent of the amount required to purchase 2 million bags of coffee at 7 U.S. cents per pound. In 1907, following its initial success, the program won the support of international finance capital, which then undertook to furnish the São Paulo government with the massive funding necessary to continue the program.

For its part, the federal government also consented to back the price boosting scheme — to which only the states of São Paulo, Minas Gerais, and Espírito Santo had originally subscribed. The central government further agreed to create a Conversion Fund (Caixa de Conversão) that would attract foreign exchange by maintaining a currency more depreciated to that prevailing on the open exchange market, but not so as to encourage international arbitrage dealings.[41] By issuing stabilization notes for the purchase of foreign exchange, the Conversion Fund expanded the money supply. In this way, monetary policy simultaneously sanctioned an increase in public spending and budget deficits, and a rise in total economic activity and in the rate of accumulation in the coffee sector.[42] In the meantime, the exchange rate stabilized, owing to a favorable level of exports and the substantial infusion of foreign capital.[43]

The War Years

The threat of war provoked both a run on imports and a fall in the world price of coffee that created an unprecedented commercial deficit. Additionally, capital flight also occasioned by the impending conflict, made the gravity of Brazil's exchange and monetary situation apparent. The Intensified demand for foreign exchange one hand, and the contraction in the money supply due to Conversion Fund operations on the other, created an extraordinary scarcity of liquidity:

> To convey some idea of this movement it is enough to remember that the issues of the conversion fund fell from 410,000 contos de réis in 1912 to something under 300,000 contos in 1913, to less than 160,000 contos in 1914. This reduction in monetary circulation had a shock effect on internal commercial relations that was further exacerbated by the outbreak of war.[44]

Moreover, given its lack of reserves, the Brazilian government could not meet its foreign commitments, which were now higher than ever. The debt progressed from 40 million pounds sterling to 162 million pounds sterling between 1897 and 1914. The negotiation of a new funding loan substantially alleviated this difficulty.[45] In the meantime, given the fall in international coffee prices and the persistent overflow of capital, the currency depreciated around 30 percent between 1913 and 1916; hence internal coffee prices could be defended in a relative sense.

As we observed in Part I, business prospects in 1917 were not encouraging, and the extensive wartime amassing of coffee stocks,[46] together with the promise of yet another large harvest in 1917—1918, prompted the government of São Paulo to withdraw another 3.1 million bags of coffee from the market at a cost of 4.9 mil réis per 10 kilos. This second valorization program sustained internal prices and (given the currency depreciation of 1917) averted a severe depression in the coffee sector.[47] Then, as early as 1918, world coffee prices increased significantly, mostly because frost damage had reduced the harvest. The exchange rate held steady and internal prices rose by nearly 15 percent.[48]

Federal receipts plummeted in response to a fall in imports and, in spite of a cutback in total spending, the deficit expanded dramatically in 1913. The government was once again obliged to adopt the emergency expedient of taxing consumption—by raising rates in 1914 and 1917 and by widening the tax base to cover new products. By the end of World War I these measures had somewhat mitigated the budgetary imbalance.[49]

The Period 1919-1929

The fundamental lines of economic policy during the years 1919 to 1929 were determined, once again, by the difficulties confronting the coffee export complex. During the initial expansion of coffee production in the 1920s the purchasing power of exports fluctuated sharply in response to changing international coffee prices, which rose in 1919 and 1920 and then plunged until

1923. Moreover, the strong demand for foreign exchange both for private remittances and for the payment of the accumulated external debt put pressure on the balance of payments situation:

> The decline of export receipts led to the disappearance of the balance of trade surplus in 1920/22 and generated a deficit in 1920/21 which brought in consequence (given the requirements of capital remittances) a serious disequilibrium in the balance of payments… Thus the surplus in the balance of trade in 1923 was, in reality, much smaller, falling from £ 22.571.000 to £ 10.571.000. The external debt alone absorbed £ 14 million in 1923 and private remittances totalled £ 12 million. This conveys some notion of the size of the balance of payments deficit in that year, which exceeded £ 15 million and which occasioned a dramatic currency depreciation.[50]

Thus the currency, which had stayed level at 16.5 mil réis to the pound sterling in 1919 and 1920, increased significantly, reaching 28.7 mil réis in 1921, 33.2 in 1922, and 44.3 in 1923. In response to this movement internal coffee prices remained relatively stable until 1921 and registered a marked upturn in 1922 and 1923.[51]

Nevertheless, devaluation was not the only factor favoring accumulation in the coffee export complex. In view of harvest predictions and a crisis in the North American economy, a third valorization program was implemented in 1921 to withdraw 4.5 million bags of coffee from the market.[52] The newly created rediscounting department of the Bank of Brazil furnished necessary funding, which, together with other smaller loans, was later consolidated through the Coffee Guarantee Loan granted by the Rothschild, Schroeder, and Baring Brothers in 1922. This aid, together with resources obtained to finance both railway expansion and public works projects in the Northeast in 1921, represented an aggregate of 38 million pounds sterling, and increased by 25 percent the accumulated external debt registered in 1920.[53]

The fluctuations in foreign trade naturally had an adverse effect on the level of federal revenues. Nevertheless, the central government continued to pursue a vigorous program of public investment, which produced large deficits between 1919 and 1922.[54] This program, combined with the coffee support scheme of 1921 and the expansion of credit through the creation of the rediscount department of the Bank of Brazil, laid the basis for increased liquidity and clearly delineated an expansionist monetary policy.[55]

It is therefore evident that there was a very close relationship between the vicissitudes of the coffee complex and the economic policies of the state. Put more forcefully, economic policy sanctioned and stimulated coffee expansion even while spending decisions were of necessity at least minimally responsive to the demands of the non-coffee bourgeoisie and the concerns of other regional oligarchies.

It must be emphasized, further, that the positive impact of monetary, exchange rate, and spending policies on industry and commercial production of primary commodities supported—rather than undermined— the process of accumulation in the coffee sector; it did this by helping to assure the reproduction of variable coffee capital without adversely affecting profit margins in the process.

Circumstances were substantially different beginning in 1924, when the Permanent Defense Policy began operating.[56] The undeniable success of the valorization programs nurtured the idea of a Permanent Defense Policy. According to this approach, official intervention was designed to maintain coffee prices at high levels rather than to prevent prices from falling below a certain point in times of crisis. The one effective measure adopted while the Permanent Defense was executed by the federal government provided for the construction of regulatory warehouses whose storage facilities were intended to avoid a glut on the market that would depress prices. The elevation of world coffee prices in 1924 attests to the success of this undertaking. Nevertheless:

> The growers soon realized that the entire weight of defense rested on their shoulders because the receipts issued by the regulatory warehouses were not easily negotiable, since the dispatch orders for the port had a delay of more than 90 or 120 days, the minimum term the banks allowed for commercial transactions.[57]

Demands that the Permanent Defense be administered by the state of São Paulo became effective in November 1924 with the creation of the São Paulo Coffee Institute. This agency established the following policy guidelines: (1) coffee entering the port of Santos would be controlled through warehouse stockpiling and transportation restrictions; (2) low-interest loans would be granted on the coffee deposited in the regulatory warehouses; (3) coffee would be purchased when deemed necessary to limit supply; and (4) the program would be financed by a permanent defense fund based on foreign loans guaranteed by a duty levied on coffee transported in the state of São Paulo.

With respect to the harvests of 1925-1926 and 1926-1927, the intervention of the Coffee Institute was limited to the division of production into monthly quotas through warehouse stockpiling; the Banco do Estado de São Paulo provided the necessary funding in this instance. However, when a record yield was forecast for 1927-1928—a development bound to disturb the relative equilibrium of the coffee market—the institute resolved to effect what became known as the "valorization by Rolim Telles." A 1926 loan obtained from the Lazard Brothers enabled the institute to advance 60 mil réis per bag of coffee to growers, a sum that covered nearly half the costs of production in the newer coffee zone and nearly a third in the traditional coffee-growing region. The Rolim Telles program, with the aid of a comparative reduction in output in 1928-1929, sustained external prices in 1928 and 1929.

Because the Permanent Defense Policy was adopted at a time when the industrial nations were enjoying a period of prosperity, world coffee prices were held at extremely elevated levels and the annual value of exports averaged 93.5 million pounds sterling.

From the point of view of policymaking, coffee expansion after 1924 presented two types of problems. In the first place, it became necessary to block, at all costs, a currency appreciation that would compress profits in the coffee sector. Accordingly, in 1926 the government created a Stabilization Fund, much like the earlier Conversion Fund. In effect, the currency was devalued by 20 percent and held at about 40 mil réis to the pound sterling until the crisis of 1929.[58]

It was equally essential to prevent a rise in money wages, which, like currency appreciation, would have the effect of narrowing profit margins in the coffee complex. The required action in this case involved subjecting the industrial sector to intense competition — a course of action made possible by Brazil's enlarged importing capacity.[59] The government did not revise the tariff schedule in these years, and consequently the degree of protective duties afforded industry diminished significantly.

In executing the federal budget, officials followed "orthodox" monetary and fiscal guidelines. A sizable cut was made in capital expenditures and public spending grew slowly; deficits contracted and there were even surpluses in 1928 and 1929. Monetary expansion was relatively modest and the means of payment expanded only in 1927 and 1928.[60]

The Crisis of 1929 and the Mechanisms of Recuperation

The critical state of affairs confronting the coffee export complex beginning in October 1929 has not always been clearly understood. The Brazilian crisis was not merely an economic transfer or reflex of the Great Depression that engulfed the world's leading economies. Rather, the vicissitudes of the coffee complex can be explained, above all, by the contradictions that inevitably accompanied the accumulation of coffee capital — contradictions that were at once tempered and deepened by official economic policy, particularly from 1924 on.

In maintaining the profit rate in coffee agriculture at extraordinarily high levels for several years, the Permanent Defense Policy encouraged a great increase in productive capacity. To convey the magnitude of this change, suffice it to say that between 1928-1929 and 1933-1934 no fewer than three harvests yielded in excess of 28 million bags of coffee each.

At the same time, the elevation of international prices promoted a considerable broadening of *external* productive capacity that intensified foreign competition and gradually eroded the near-monopoly position enjoyed by Brazilian coffee interests in the world market. In his classic work Delfim Netto clarifies the issue:

> The central rationale of the defense consisted in artificially adjusting the relationship between supply and the world demand for coffee in order to support prices. As we see in a report of the President of the Republic, probable world consumption was calculated and the exportable output of our competitors was subtracted. The difference was to be supplied by Brazil. Thus, in order to keep prices high Brazil voluntarily assumed the position of residual supplier. The apologists for the defense never understood that price supports presented our competitors with an enormous incentive and a completely open market.[61]

Thus the fundamental explanation of the coffee crisis is to be found in the great excess productive capacity *concentrated* in Brazil. It is true that in terms of its impact on external demand and its contribution to the dislocation of Brazilian produce from the market, the Great Depression probably anticipated and certainly deepened the crisis that was, in any case, inevitable. The Crash of '29 imposed the coup de grâce to the international monetary system based on the gold standard, a structure that had already been shaken in the years following World War I. Subsequently, the foreign trade policies of most nations came to be based on a bilateral system of payments or on equilibrium within a block. Furthermore, the metropolitan countries promoted the substitute cultivation of primary products previously imported from other areas within their own colonies. Accordingly, throughout the 1930s African production expanded in the shelter of high preferential tariffs.[62]

Having clarified this central point, we can turn to the crisis itself and to the mechanisms of recuperation. Beginning in October 1929 the defense system elaborated by the Coffee Institute began to fall apart, not only because demand faltered but also because the federal government decided to leave the coffee sector to its own devices. Preoccupied with salvaging the Stabilization Fund, President Washington Luiz, once an ardent defender of institute policies, became a confirmed advocate of nonintervention in the market.

It is instructive to speculate on how severe and protracted the Brazilian depression would have been *if* the government had abstained from *any* form of intervention in the coffee economy and if it had implemented an orthodox fiscal policy in order to balance the budget.

In this hypothetical set of circumstances the balance between supply and external demand would be restored by adjusting capital stocks, that is, by destroying excess productive capacity. The fall in world prices would eventually be transferred to internal prices, and devaluation would lose its effectiveness as a defense mechanism. In this respect Furtado rightly observes:

> The currency depreciation, although cushioning the impact of the fall in international prices on the Brazilian entrepreneur, induced him to continue harvesting and maintaining pressure on the market. This situation led to a new price decline and renewed currency depreciation , contributing to further intensification of the crisis. As the degree of currency depreciation was much smaller than the fall in prices — inasmuch as the former was influenced by other factors — a point would clearly be reached where the loss to the growers would be large enough to induce them to abandon their plantations. Only then would a balance be reached between supply and demand.[63]

Both those planters who increasingly produced at variable monetary costs superior to prices and those who had secured bank loans during expansion and were now insolvent would necessarily be eliminated. Moreover, as profit expectations vanished, at a certain point the installation of new productive capacity would cease altogether. The low point of the crisis would be reached when external and domestic prices only barely covered the variable monetary costs and capitalists' consumption of all working enterprises. And there can be no doubt concerning the severity of the crisis, since we know for a fact that international prices plunged nearly 60 percent between 1929 and 1933 in spite of the withdrawal of millions of bags of coffee from the market. Thus the adjustment of coffee agriculture could only have been achieved at the cost of destroying a large part of the installed productive capacity, of imposing a very high level of unemployment, and of tolerating a substantial fall in money wages.

The crisis would spread from coffee agriculture to the rest of the economy. Without detailing the mechanisms of transfer, we may note that in view of the reduced demand for commercial, financial, and transportation services, as well as the insolvency of coffee businesses, the depression would almost at once extend to the urban sector of the coffee complex. The cut in consumption would have an immediate impact on the wage goods industry and on commercial agriculture that would produce new adverse repercussions throughout the economy. The fall in imports and in the general level of domestic economic activity would undermine public finances, and the government (according to our hypothesis) would assume a passive role, maintaining expenditures at the level of receipts.

The low point of depression does merit close attention. We have observed that for coffee producers this stage obtained when prices scarcely covered the variable monetary costs and capitalists' consumption of working units. Given the profound nature of its problems, coffee agriculture would transmit its low point to the other sectors of the economy. The collapse of demand would compress profits in the urban coffee sector and in industry to the level of capitalists' consumption alone. The same would hold for internal market agriculture organized along capitalist lines. Agricultural food and raw material production undertaken on small private holdings and within the great domains would regress to a subsistence level.

Finally, we may comment on the possible operation of automatic recovery mechanisms. In view of the state of the world market for agricultural commodities, the outlook for a rapid recovery based on export agriculture would not be bright. Nor would the prospects for recuperation through industrial growth be encouraging—in the first place because the replacement of industrial investments would have only a limited dynamic impact since their effects would largely be channeled to the exterior, and in the second, because it is extremely difficult to imagine a block of innovations capable of reviving the prostrate economy.

It seems logical to conclude, therefore, that had the government abstained from any form of intervention in the coffee market, and had it pursued an orthodox fiscal policy, not only would the depression have reached extraordinary depths but it would also have been difficult for Brazil to achieve complete recovery by the end of World War II.

As it happened, the Great Depression did not assume catastrophic proportions in Brazil, although it was indeed serious, considering that the gross domestic product (GDP) fell around 4 percent between 1928 and 1931 (its lowest point). Furthermore, in comparison to other countries, recovery in Brazil was relatively swift, and as early as 1932 the GDP surpassed the level registered in 1928.[64] The simultaneous operation of several mechanisms both prevented catastrophe and promoted recovery. Unquestionably the principal of these was the coffee defense policy, insofar as it maintained internal prices sufficiently high to at least cover the variable monetary and capitalists' consumption costs of most intramarginal producers, and in doing so, permitted relatively sustained operations and stabilized income levels within the urban division of the export complex.

Since the defense policy has generated considerable controversy, it is best to analyze its operation with care. Once the financing capacity of Banco do Estado de São Paulo had been exhausted and President Washington Luiz assumed his noninterventionist stance, the impotence of the Coffee Institute became apparent. Accordingly, the state government sought and obtained a loan of 20 million pounds sterling (720,000 contos) from four international bankers.

A portion of this sum funded the purchase of 3.1 million bags of coffee at a rate of 100 mil réis each, while the balance refinanced another 13.5 million bags.

Following the cautious approach of Whitaker's policy, the provisional government resolved to create the National Coffee Council, which, through the buying and destroying of coffee stocks took charge of the price support policy. The council purchased coffee valued at nearly 30 percent of exported receipts in 1931 and 1932 and destroyed 14.4 million bags between May 1931 and February 1933. Sixty-five percent of the cost of this project was financed by taxes and the rest through the Bank of Brazil and the national treasury.

It was precisely these massive purchases that formed the basis of all subsidization of the coffee export complex. In significantly diminishing the pressure exerted by supply, they helped to establish higher international prices. Furthermore, it became possible for currency devaluation to function once again as a defense mechanism, cushioning the fall in internal prices. Had the market been allowed to operate freely, this mechanism (through which external prices declined considerably more than internal prices) would have lost all effectiveness. Even if purchases had been financed entirely through taxation, the withdrawal of surplus output would have been a decisive policy. Moreover, as Fishlow reminds us, given the inelasticity of the demand for coffee, the burden of the export tax necessarily fell in part on the consumer.[65]

The expansionist impact of purchases financed by treasury and Bank of Brazil notes—no small matter—should not be viewed solely as a corollary effect. Rather, it must be borne in mind that the defense policy was a broadly conceived program based on the combined operation of external price supports, currency depreciation, and the anti-depressive repercussions of funding purchases by issuing notes.[66]

Granting the critical weight of the coffee defense policy, we should nonetheless acknowledge the positive intervention of yet another factor — the budget deficit. First, however, we should explain why it is not the balance-of-trade surplus — functioning as a defense mechanism for domestic income — that we consider to be important. The favorable balance of trade reflected the failure of internal demand, which was translated into a decrease in the importation of consumer goods, particularly capital goods, and did not derive from a specific economic policy designed to remedy the crisis. That is, the positive balance of trade was primarily a *result* of the Depression rather than a measure adopted *ex ante* to combat it. To the contrary, what concerns us are the budget deficits accumulated between 1930 and 1932, which originated in expenditures related to the Revolution of 1930, the Paulista Rebellion of 1932, and aid extended to the northeastern states devastated by the great drought of 1930-1933. In 1930 the deficit put the brakes on the fall in income, and in 1932 it was the driving force for recuperation. By itself, the finding that the state did not attempt to balance the budget means very little. The important point is that although their objectives were quite different, the policies implemented by the government in 1930 and 1932 "in practice" followed Keynesian lines.[67]

The relationship between coffee capital and industrial capital: the emergence and consolidation of industry

There can be little doubt that the intense development of coffee capital between 1886 and 1929 stimulated the formation and consolidation of industrial capital in Brazil. To examine this relationship, we can begin by tracing the emergence of large-scale industry during the expansive phase of the first long coffee cycle, that is, between 1886 and 1894.

The Formation of Industrial Capital

Before 1887 Brazil's industrial capital was only marginally significant. A few industrial establishments existed, but even at the regional level they never constituted an industrial sector of any magnitude. For example, the state of São Paulo contained only seven textile plants and twenty-one other industries specializing in foodstuffs, hats, beverages, and footwear. The declared value of these installations represented only 17.6 percent of the total industrial capital registered in the 1907 state census.[68]

Nevertheless, between 1886 and 1894 investments in industry grew considerably, according to the findings of Fishlow and of Wilson Cano. Cano's figures show that about 40 percent of São Paulo's industrial capital in 1907 had been installed between 1887 and 1894. Fishlow's research indicates, moreover, that the importation of capital goods in this period was not surpassed until much later.[69] Thus the timing of industrial birth coincided with the "momentum" of expansion of the coffee export complex, while industrial development took place increasingly in the coffee zone itself. By 1907 approximately 60 percent of the nation's industrial output originated in the states of Rio de Janeiro, São Paulo, and Minas Gerais.

Industrialization and the evolution of the coffee sector were, in fact, profoundly related. It was the coffee economy, in which production was based on a series of capitalist relationships, that created the social and economic prerequisites for the formation of industrial capital. Fernando Henrique Cardoso has placed the issue in its proper perspective:

> The process of industrialization in any region assumes the existence of a certain degree of capitalist development and, specifically, the presence

> of a mercantile economy; it further implies a relatively developed social division of labor. The latter, insofar as division proceeds within a capitalist framework, results in the formation of a labor market… Nevertheless, these prerequisites are created by the capitalist organization that predates industrial production properly speaking. Before the emergence of the industrial entrepreneur the Brazilian capitalist already existed, as merchant, planter, or financier, and as such he laid the groundwork for the elaboration of a capitalist regime of industrial production.[70]

The capitalist coffee sector, then, provided patterns and conditions basic to the emergence of industrial capital and large-scale industry. To explore the specific problem of industrial capital formation in Brazil, we can focus on three issues: how a given social class operating within a given context accumulated resources capable of being transformed into industrial capital; why this class chose to invest in industry, thereby breaking with traditional investment patterns; and finally, how these resources were used to acquire the labor force and the means of production necessary for large-scale industry.

First, it is evident that the coffee capitalists — that is, the coffee bourgeoisie — formed the social matrix of the industrial bourgeoisie. In other words, industrial capital was generated by investments made in the coffee export complex, both in its productive nucleus and in its related urban activities, in particular the import trade.

The involvement of coffee planters (i.e., the agrarian element within the coffee bourgeoisie) in industrial undertakings was impressive. According to the figures compiled by Bandeira Jr., in 1901, about 50 percent of all workers in São Paulo were employed in businesses owned by coffee *fazendeiros*.[71] Moreover, the import sector contributed decisively to the formation of industrial capital. The large import houses not only purchased foreign merchandise but took charge of its distribution and ultimately assumed control of much of the nation's internal commerce as well. As a rule, the import merchants were immigrants — precisely the persons best able to establish contacts in their countries of origin and obtain credit from banks abroad. Accordingly, a sizable share of the Paulista industrial bourgeoisie had immigrated to Brazil and begun their careers as importers. Matarazzo, for example, was initially an importer of edible oil, flour, and rice; the Jafet brothers, Crespi, Diedrichsen, and many others first established import houses.[72]

We may ask what prompted agrarian and commercial coffee interests to invest in industry. As we know, industrial capitalism did not emerge when the coffee export complex was in the midst of crisis, but rather during an export boom, when returns most certainly attained very high levels. It happened, however, that the profits realized between 1889 and 1894 could not be fully absorbed by the coffee economy itself. Earnings could not be reinvested in the productive nucleus in part because the rhythm of incorporating new lands was subject to a series of natural factors, such as the timing of clearing, planting, and so forth; moreover once the coffee trees were in place, productive accumulation became essentially a "natural" process; and finally, between planting time and the first harvest labor costs were almost completely reduced to remuneration for weeding. Nor could importers readily channel their profits into increased buying abroad because Brazil's import capacity expanded less rapidly than profit margins. Consequently, domestic industry became the only profitable application for surplus commercial profits.

Stated another way, there was a siphoning of capital funds from the coffee export complex because the amassing of money capital outstripped the possibilities for productive accumulation. Industrial projects had only to promise the overall reproduction of profits in order to attract investors. It is also true that the transfer of capital from coffee to industry was greatly aided by the easy credit facilities afforded by early Republican reforms and the expansionist monetary policy pursued until 1894.

The conversion of surplus money capital into industrial capital was accomplished in the following manner: in the first place, industrial capital benefited from the ample supply of free labor. Not only did coffee capital stimulate the formation of a labor market; more important, the volume of immigration exceeded the demands of the coffee export complex. Immigration permitted the reproduction of rural and urban capital and still "deposited" a "surplus" of labor in the cities.

Nevertheless, as we have pointed out in another connection, a ready supply of workers did not by itself assure the reproduction of the labor force, since this process also demanded adequate provisions of foodstuffs and manufactured wage goods. Insofar as internal production was initially restricted, the cost of reproduction depended on the ability of the export complex itself to generate the necessary importing capacity. Similarly, given the absence of a domestic capital goods industry, the transformation of money capital into productive capital hinged on the ability of the coffee economy to supply foreign exchange for the importation of essential machinery and equipment.

Of course the coffee complex absorbed a portion of the economy's import capacity to supply its own demand for means of production, foodstuffs, and manufactured consumer goods, while the state required foreign exchange for its own consumption and investment costs. On the other hand, rubber, sugar, and cacao exports augmented the importing capacity generated by coffee sales, while the inflow of liquid capital from the exterior further enhanced Brazil's ability to buy abroad.[73]

It is difficult to draw conclusions about the period 1890-1894, apart from the fact that imports grew appreciably in response to the expansion of coffee receipts and, to a lesser extent, to receipts of rubber and cacao. Moreover, on balance, these years experienced a net inflow of foreign capital. Even so, the pressures placed on the economy's capacity to import were considerable. And in contributing to the strain, the construction of new industrial plants helped provoke an internal adjustment of prices that in advancing the cost of wage goods and reducing real wages, fostered a realignment (inevitably altered later on) between the demand for imports and importing capacity. Similarly — although to a lesser degree — the erosive effect of currency depreciations on government revenues necessarily held down public spending and constricted the demand for imports generated by this source.

In sum, the coffee export complex itself both furnished the means and created the conditions for the conversion of money capital into industrial capital; it provided labor power and generated the foreign exchange used to purchase capital goods as well as the foodstuffs and manufactured commodities that were indispensable to the reproduction of an industrial labor force.

Investments in industry brought at least minimally positive returns for several reasons. Apart from the "natural" advantage of relatively lower transportation charges, infant industries could count on a high degree of tariff protection. At this level of discussion it hardly matters whether tariff policy embodied explicitly protectionist objectives; rather, the important point is that import duties represented the only revenue instrument at the disposal of the federal government that would prevent the burden of taxation from falling directly on the export bourgeoisie. Protection was relatively high until the introduction of the gold tariff in 1891, and thereafter fell off — although only slightly — until 1894. New manufacturers were further sheltered to a substantial extent by currency devaluation, which altered the exchange rate approximately 300 percent between 1889 and 1894.

The profitability of industrial capital in this period was therefore amply favored by a fall in wages and a high degree of protection. It also benefited from tax exemptions extended to the importation of machinery and equipment.

The question arises as to why industrial growth in this era was specialized and, for the most part, consisted of the production of consumer wage goods, textiles in particular. Certainly the reason is not the absence of a market, since, as we have emphasized, the coffee export complex created a market not only for consumer commodities but also for means of production. At first glance, yet another type of explanation is appealing: because heavy industry required a relatively higher ratio of capital to labor and relied to a greater extent on imports in the formation of constant capital, the profound currency depreciation and the evolution of wages in this period would have a greater adverse effect on its profitability in comparison to that of the consumer goods industry. Nevertheless, there are indications that in spite of these and other obstacles (e.g., the steel industry's difficulties in gaining access to raw materials), decisions were made to invest in heavy industry.

Obviously we must look elsewhere for an explanation of investment preferences. It should be noted that in the last two decades of the last century, during the "second industrial revolution," the capital goods industry underwent a profound technological transformation that led to the creation of immense economies of scale that required both higher initial investments and a larger minimum scale of operation for profitable production. For Brazil, this change introduced almost insoluble problems related to the concentration and centralization of capital, while investment risks assumed formidable proportions. Finally, and equally important, the technology of heavy industry was simply not available on the international market.

In contrast, light industry, and the textile industry in particular, relied on a comparatively simple technology that was more or less stable, easily mastered, and entirely contained in equipment accessible on the world market. In addition, both initial investments and the scale of production could be managed by the Brazilian economy of the time. These factors, rather than the problem of preexisting demand or relative factor costs, appear to be at the root of the preference shown by investors for the consumer goods industry.

Judging from the statistics on capital formation in São Paulo, the years 1895 to 1898 saw a pronounced advance in industrial production.[74] Although the investment rate of earlier years was apparently not sustained, general economic conditions were such as to permit the firm establishment of infant industry. Although public spending stagnated in real terms (even falling somewhat), the movement of the exchange rate preserved profit margins, relatively, within the coffee export complex. As accumulation proceeded, albeit at a slower pace, not only was a cut in demand for manufactured goods prevented, but demand actually grew. Furthermore, currency depreciation improved competitive conditions, while the degree of protection afforded by the tariff schedule increased in 1896 and diminished in 1897 and 1898.

The industrial sector was in a position to take advantage of the stimulating conditions operating on the side of demand because it possessed a reserve of underutilized productive capacity accumulated during the favorable investment climate of the years 1890-1894. Without this excess capacity it would have been difficult to expand output so much at a time when new accumulation was hampered by the curtailment of importing capacity occasioned by the fall in exports from 1896 on.[75] Industry also benefited from an elastic workforce supply created by continued mass immigration; this situation, coupled with inflation, most likely reduced real wages substantially. Finally, the imported components of constant capital were relatively less costly between 1895 and 1898, since the elevation in internal prices of final goods was more than proportional to the currency depreciation.[76] Therefore profit margins in the industrial sector must have widened considerably.

At the same time, in view of the excess capacity inherited from earlier years, the rate of accumulation of productive capital obviously declined.[77] Accordingly, much of the increment in earnings would have been applied to current operations, at a time when monetary policy was being tightened in order to hold down internal prices and support coffee profits.

It is not necessary to dwell on the difficulties industry faced from 1899 to 1902, which stemmed as much from the coffee crisis as from the cut in public spending and the sizable increase in excise taxes that had to be absorbed in a clearly deflationary context. What does merit close attention is the fact that despite all those difficulties nascent industry did in fact survive. It did so, first, because the fall in earnings was offset by the flexibility of money wages permitted by unemployment (linked to the depression) and by the cheapening of variable and constant capital imports owing to currency appreciation.[78]

Second, given the recuperation of exports after 1900, the reduction in protectionism afforded by the exchange rate (because of the currency appreciation) would have been fatal had it not been counterbalanced by the added customs protection provided by the gold tariff that same year. In sum, several defense mechanisms—the fall in money wages, the declining costs of imported primary materials, and tariff reform—enabled industry to weather the storm.

The available figures on capital goods imports attest to the recovery of the industrial sector after 1905, a process undoubtedly promoted by increased public spending beginning in 1903.[79] (see Table 9). The same data suggest that growth accelerated continually through 1912.

The circumstances favoring industrial development between 1905 and 1912 included, first, the enlargement of Brazil's import capacity after 1905 (and especially after 1909), which reflected both the growth in coffee and rubber exports and an improvement in the terms of trade.[80] Besides this, the significant infusion of foreign capital — for public and private investments and for the coffee valorization program — greatly augmented Brazil's foreign currency reserves. If we further consider that the export complex generated no demand for foreign exchange in this period, we can see why industry was able to rely on either currency appreciation or the economy's capacity to import capital goods to support its rate of accumulation.

The supply of labor power also contributed to industrial expansion: manufacturers could tap both the natural increment in the urban population and a renewed current of immigration. As one might expect, immigration had fallen off between 1898 and 1905, not only because the depressed economy offered little attraction to newcomers, but also because the recuperation and expansion of the Italian, Argentine, and North American economies had weakened the push factors and strengthened the diversionary forces that conditioned migration to Brazil. After 1905, however, immigration revived and an aggregate of 995,000 newcomers arrived between 1905 and 1913—680,000 (69 percent) of whom came between 1909 and 1913. This dramatic change reflected the extraordinary increase in supply on the international labor market, although it is no less true that in various years (1908, 1909, 1911, and 1912) Brazil benefited from the decline in migration to the United States.[81]

It should not be assumed, however, that additions to the labor supply through immigration were entirely at the disposal of industrial capital. The growth in public investments, as well as the notable expansion of commercial food production, generated a demand for labor.[82] Elsewhere we have emphasized that coffee prosperity during the 1890s depended on the massive importation of foodstuffs. However, once in crisis, the coffee complex maintained a level of accumulation that, although not insignificant, was much lower than in the previous period. Accordingly, it became possible to diversify production and seriously engage in the production of food items, particularly in São Paulo; so significant was this trend that by the end of World War I a small volume of commodities was actually marketed abroad.[83]

In summary, owing to the natural growth of the economically active population and to mass immigration, labor power was sufficiently abundant to support the combined expansion of industry, public investments, and commercial food agriculture.

For its part, the balanced growth of agriculture, together with that of industry, permitted the reproduction of the labor force without exerting pressure on real wages. Money wages even tended to rise, as prices stayed level between 1903 and 1905, moved upward only in 1906, and stabilized thereafter.[84]

This said, the conditions of industrial realization can be duly noted. Industry and agriculture were mutually supportive, since they provided markets for each other and both benefited from increased public spending, which they in turn supported by making available edible and manufactured consumer goods. Finally, industry was equipped to meet foreign competition, not only because it enjoyed a measure of tariff protection, but also because it modernized, acquiring from abroad equipment whose efficiency equaled or nearly matched that of foreign rivals.[85]

Expansion was cut short in 1913, and the ensuing crisis deepened in 1914. Industry's problems originated, in the first instance, in the financial turmoil created by the contraction in the money supply that was brought about by a run on foreign exchange held by the Conversion Fund. On the other hand, as the figures on capital goods imports indicate, the growth of productive capacity had greatly accelerated after 1910, creating an excess that would be utilized during the war years.

The War of 1914-1918

The debate over whether World War I had a beneficial or harmful impact on Brazilian industrial development — to which the work of Warren Dean on the industrialization of São Paulo furnished additional arguments in support of an "obstructed growth" thesis — has been clarified by a series of recent works beginning with that of Fishlow in 1972. Cano's doctoral thesis on the roots of industrial concentration in SãoPaulo provides what we feel to be a definitive treatment of the problem, based as it is on an investigation of the available empirical data and a careful interpretation of the relevant facts. To summarize, Fishlow and Cano demonstrate that Paulista industry grew not only by exporting to other regions and to the exterior (Dean's thesis) but also because the internal market itself expanded under the stimulus of recovery from the crisis of 1913-1914.[86]

In order to counter the adverse effect of the crisis of 1913 and the progressive contraction in spending and in the national debt, the government embarked upon a program of "assistance to national production" that consisted of a contractual authorization of credit expansion through the Bank of Brazil; this institution began operating as a commercial bank at the same time it financed the treasury deficit. Thus, the monetary restraint exercised from 1899 to the crisis of 1913-1914 was finally relaxed.[87]

This policy particularly benefited manufacturers, who could now finance new production, utilizing the excess capacity accumulated primarily in 1912 and 1913. For this reason, the decline in capital goods imports during the war can scarcely be viewed as an obstacle to industrial growth.[88] In reality, despite their reduced volume, such imports were adequate to create favorable conditions for the expansion of industrial demand and to enlarge industry's productive capacity. The aggregate data compiled by Cano on the capacity of the Paulista textile industry and on the number of new plants established during World War I clearly demonstrate that once industry recuperated from the slump of 1913-1914, further growth was not simply a function of an increase in the number of shifts worked by laborers, nor was further development obstructed by a lack of machinery — a thesis favored by Dean. Instead, Cano finds that "the total capital employed by industries established in years 1915 to 1919 amounted to 24 percent of all industrial capital registered in 1919, representing 5936 new plants created in that four-year period."[89] Moreover, the movement of the exchange rate clearly enhanced the advantageous condition of demand at this time. After the balance of payments crisis of 1914, the mechanism of currency devaluation — despite a slight appreciation in 1916-1917 — produced an alignment of internal and external prices that increasingly favored industry.

It was not only the industrial sector that profited from the inflationary boom of World War I. High inflation rates in the context of stable nominal wages (and even declining wages in some categories) boosted earnings in nearly all rural and urban activities.[90]

The marked advance after 1905 in the agricultural production of food and raw materials that accompanied coffee expansion does not appear to have been additionally stimulated by wartime restrictions on Brazil's importing capacity. In other words, it was not import substitution that encouraged agricultural growth, but rather the combined influence of easy credit, the opening of new areas for cultivation in the years before the crisis, and finally, the emerging possibility of exporting internal surpluses of industrial raw materials such as cotton—a relatively scarce commodity on the international market.

The current emphasis on the wartime import substitution of foodstuffs, evident, for example, in the works of Dean, and Villela and Suzigan, finds little support in the empirical data Villela himself presents. The decline in food imports paralleled the expansion of Paulista agriculture after 1905, and thus began well before World War I. In the years 1915 to 1918, in the midst of conflict, exports were already growing at an accelerating pace (see Table 10).

The 65,000-ton reduction in food imports between 1909-1913 and 1914-1916 noted by Dean in fact reflected restrictions imposed on the purchase of nonessential items. Significantly, European wine alone accounted for nearly 85 percent of the decline registered.[91]

In summary, World War I, which has provoked much debate concerning its positive or adverse impact on industrialization, appears to have brought no dramatic change to either the conditions of production or the pattern of accumulation within the Brazilian economy. The internal market expanded primarily in São Paulo, through industrial and agricultural (food and raw materials) growth, and this process only confirmed the dominance of the Paulista economy, a phenomenon clearly visible from the end of the nineteenth century. In addition, the elevation of the world food and raw material prices (other than coffee prices) gave some relief to the other regional export economies, some of which (like the old sugar complex of the Northeast) were clearly decadent, and provided the Amazon rubber economy with its last burst of activity.

Everything indicates, then, that the war merely represented a test of affirmation of the internal conditions of accumulation of an embryonic capitalism whose urban-industrial and agricultural diversification had become increasingly pronounced since the end of the last century.

The 1920s

Brazilian industry had already undergone considerable development by the early 1920s owing to the expanded production of wage goods. The census of 1919 reveals the near-domination of the sector by the food- and beverage-processing industries, which represented nearly 40 percent of the value of production, and by the textile and apparel industries, which accounted for 32 percent of the value of output. The figures in Fishlow's paper indicate that industrial growth afforded Brazil a high degree of self-sufficiency in terms of consumer goods.[92]

The 1919 census further demonstrates that the industrial preeminence of São Paulo was well established by that date.[93] Although space limitations prohibit a detailed examination of the issue of regional concentration, we may note that São Paulo's industrial superiority was established early (between 1905 and 1907), gained impetus from 1907 to 1913, and became consolidated during World War I. The origins of this position are to be found in the unparalleled, dynamism of the coffee economy, the growth of a vigorous branch of commercial food agriculture, and the existence of a sizable labor market. In sum, São Paulo's success can be attributed to the greater development of capitalist social relations of production.

It has been emphasized that the 1920s were characterized by low rates of industrial growth. Moreover, the available figures indicate that production advanced between 1919 and 1922, stagnated from 1923 to 1926, and expanded again only in 1927 and 1928.[94]

Nevertheless, we believe that it is necessary to go a step further and acknowledge two other fundamental traits of industrial evolution between 1919 and 1929: the modernization of the wage goods industry, and differentiation within the industrial structure. The data on machine and accessory imports for the textile industry clearly indicate that the wage goods sector underwent an intense modernization process.[95]

Unquestionably this transformation proved possible only because of the enlargement of Brazil's importing of capacity, which resulted as much from the enhanced purchasing power of exports as from the infusion foreign capital, particularly for the coffee valorization policy. On the other hand, as Brazil's balance of payments situation eased, the currency appreciated in 1919-20, 1925, and 1926, and relatively cheapened the cost of imported machinery and equipment.

If the widening of Brazil's importing capacity was a *sine qua non* for modernization, given the erosion of tariff protection, it nevertheless implied an intensification of external competition, at least between 1924 and 1926. It is this line of reasoning that underlies the current belief that industrial development during the 1920s was weak.[96]

However, the intensification of intercapitalist rivalry during the 1920s should not be interpreted solely as an extension of heightened external competition: it should also be viewed in terms of the tendency toward overaccumulation at work in a relatively concentrated market structure. The means employed was continued modernization, and the result was a greater concentration and centralization of capital, with a marked regional bias. Specifically, it was the São Paulo industrial sector that emerged as the driving force and chief beneficiary of the expansion of the period 1919-1923.

Brazil passed through an extremely volatile stage of development between 1924 and 1926. Whether because of the corrosive effect of prolonged inflation on tariffs, or because of currency appreciation, the degree of industrial protection diminished considerably.[97] The expansion of demand tapered off (even allowing for that generated by the coffee sector) at a time when the potential for accumulation was very great. In consequence, intercapitalist competition intensified and assumed the form of an interregional contest in which São Paulo industry held a considerable advantage — a situation that provoked a severe industrial crisis in 1926.[98] In 1927 and 1928, in all likelihood because of the reactivation of the demand for coffee and the rise in the degree of protection, production increased and intercapitalist competition subsided.

Cotton textiles, of course, were only one part of industry. Several other branches exhibited somewhat more favorable patterns of development. Moreover, the consumer wage goods industry underwent a degree of diversification: industries specializing in the production of woolen, natural silk, rayon, and knitted goods were installed; the manufacture of such items as stoves, electrical lamps, and enameled goods was introduced; and food processing branched out to include the extraction and refining of vegetable oils, the production of canned animal and vegetable goods, and so forth.[99]

Similarly, the mediocre level of national growth was not representative of all sectors. Either because it penetrated and gained control of other markets or because it diversified to a greater extent, the Paulista consumer wage goods industry augmented production at the significant rate of approximately 6 percent per annum.

In sum, the consumer wage goods industry modernized to an important extent during the 1920s, and the industrial sector of São Paulo assumed a highly advantageous position at the expense of its counterparts in other states.

A second distinguishing feature of industrial evolution during the 1920s was the greater diversification achieved with the embryonic development of a capital goods sector. Not surprisingly, a few such industries already existed, particularly those installed during World War I. However, these consisted of small factories devoted to repairs and assembling or to the manufacture of simple machines and parts, or else they were

installations of minor import, such as brickyards. Even a handful of ironworks had been present since the turn of the century, but they used the most primitive of processing techniques.[100]

Accordingly, there was little continuity between Brazil's early capital goods industries and those that came into being during the 1920s, i.e., small-scale steel production, the cement industry, and the manufacture of electric motors, machines for the sugar and textile industries, etc. Furthermore, limited as it was, the development of the capital goods sector was vital for the future because it laid the groundwork for the eventual reproduction of industrial capital relatively independent of mercantile-export capital.

Table 1 – Money Wages, 1884-1898 (Mil Reis)

Year	Weeding*	Harvesting[1]
1884	50	500
1886	80	400
1888	50	300
1890	60	300
1895	90	600
1898	90	680

Source: Michael Hall, "The Origins of Mass Immigration in Brazil 1871–1914" (Ph. D. diss. Columbia University, 1969), p. 186.

*Wages for weeding are annual, mil reis per 1,000 trees.

[1]Wages for harvesting are annual, mil reis per 50 litres.

Table 2 – Export Receipts, 1889–1898

Year	Value (£ thousands)
1889	28,552
1890	26,382
1891	27,136
1892	30,854
1893	32,007
1894	30,491
1895	32,586
1896	28,333
1897	25,883
1898	25,019

Source: Annibal Villela and Wilson Suzigan, *Política do governo e crescimento economia brasileira 1889-1945* (Rio de Janeiro: IPEA/INPES, 1973), p. 439.

Table 3 – External And Internal Coffee Prices, 1889-1898

Year	External Prices (1889 = 100)	Internal Prices (1889 = 100)
1889	100	100
1890	113	120
1891	90	171
1892	87	201
1893	103	276
1894	92	290
1895	91	262
1896	69	252
1897	47	180
1898	41	163

Source: A. Delfim Netto, *O problema do café no Brasil*, (2nd. ed. (São Paulo: Faculdade de Ciências Econômicas e Administrativas, Universidade de São Paulo, 1966), p. 29.

Table 4 – External and internal Coffee Prices, 1897–1906

Year	External Prices (U.S. cents per pound)	Internal Prices (mil réis per 60-kilo bag)
1897	7.5	55.6
1898	6.5	50.3
1899	6.7	48.2
1900	7.4	52.9
1901	6.4	34.5
1902	6.6	31.2
1903	7.0	29.7
1904	8.1	39.1
1905	8.6	30.0
1906	7.9	29.9

Source: C. M. Pelaez, "Analise econômica do programa de sustentação do café," *Revista brasileira de economia*, 25, no. 4 (December 1971), p. 205.

Table 5 – Money Wages, 1898–1904 (Mil Reis)

Year	Weeding*	Harvesting[1]
1898	90	680
1899	85	650
1901	65	500
1904	60	450

Source: Hall, "The Origins of Mass Immigration in Brazil, 1871-1914," p. 186.

*Wages for weeding are annual, mil reis per 1,000 trees.

[1]Wages for harvesting are annual, mil reis per 50 litres.

Table 6 – Importing capacity and Exchange Rates, 1901-1906

Year	Quantum Index of Importing Capacity* (1928 = 100)	Exchange Rate (mil réis per pound sterling)
1901	53.1	21.1
1902	44.9	20.1
1903	44.9	20.0
1904	45.3	19.0
1905	53.1	15.1
1906	58.9	14.8

Source: Pelaez, "Análise econômica do programa de sustentação do café," p. 205. Villäh and Suzigan, *Política do governo e crescimento da economia brasileira 1889–1945*. P. 441.

*The index of importing capacity is given by a value index of total exports divided by a price index of imports.

Table 7 – International and Internal Coffee Prices and Exchange Rates, 1906-1913

Year	Internal Prices (mil réis per 60-kg bag)	External Prices (U.S. cents per pound)	Exchange Rate (mil réis per pound sterling)
1906	29.9	7.9	14.8
1907	28.9	7.6	15.8
1908	29.1	7.5	15.8
1909	31.6	7.9	15.8
1910	39.6	10.3	14.8
1911	53.9	13.3	14.9
1912	57.8	13.8	14.9
1913	46.1	11.1	14.9

Source: Pelaez, "Análise econômica do programa de sustentação do café," pp. 205–206.

Table 8 – International and Internal Coffee Prices and Exchange Rates, 1919–1929

Year	External Prices (U.S. cents per pound)	Internal Prices (mil réis per 60-kg bag)	Exchange Rates (mil réis per pound sterling)
1919	19.5	94.6	16.5
1920	19.5	74.7	16.5
1921	10.7	82.4	28.7
1922	12.9	118.7	33.2
1923	13.5	146.9	44.3
1924	17.5	205.9	40.0
1925	22.3	215.1	38.9
1926	21.6	170.7	33.3
1927	18.5	170.4	40.6
1928	21.3	204.6	40.3
1929	20.4	191.9	40.6

Source: Pelaez, "Análise econômica do programa de sustentação do café," pp. 205-206.

Table 9 – Importation of Capital Goods, 1900-1913 (1900 = 100)

Year	Quantum Index 1900 = 100
1900	100.0
1901	56.8
1902	31.7
1903	38.0
1904	41.3
1905	62.3
1906	66.1
1907	93.0
1908	96.4
1909	102.9
1910	118.7
1911	153.6
1912	205.3
1913	152.6

Source: Villela and Suzigan, *Política do governo e crescimento da economia brasileira 1889-1945*, p. 347.

Table 10 – Foreign Trade in Foodstuffs, 1911-1918 (Exports Minus Imports, in Tons)

Year	Rice	Beans	Potatoes	Corn
1911	- 16,480	-8,058	- 17,846	-3,798
1912	- 10,189	- 9,388	- 28,971	-6,262
1913	-7,728	- 8,540	-29,800	-8,892
1914	-6,532	-5,310	-18,970	-1,119
1915	-6,945	1,042	-8,757	-2,066
1916	410	44,599	4,526	3,551
1917	44,603	93,402	4,401	23,867
1918	27,914	70,883	4,766	12,976

Source: Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1889-1945*, p. 145.

Table 11 – Growth of São Paulo Consumer Goods Industry, 1918–1928

Year	Quantum Index A (1920 = 100)	Quantum Index B (1920 = 100)
1918	78.7	78.6
1919	93.0	92.3
1920	100.0	100.0
1921	102.5	99.9
1922	114.7	113.5
1923	188.1*	136.4
1924	131.6	137.1
1925	118.1	123.5
1926	130.2	131.8
1927	144.1	168.6
1928	169.1	215.7

Source: Cano, *Raízes da concentração industrial em São Paulo*, p. 185.

Note: Index A is a composite of ten products, including four types of cloth, footwear, hats, beer, alcohol and cane brandy, sugar, and chilled meat. Index B includes all the products of Index A except cotton cloth.

*The large volume of cotton cloth accounts for this high figure.

NOTES

1 - Cardoso de Mello, J. M. *O Capitalismo tardio.* Brasiliense. 1982.

2 - On this point see E. Williams, *Capitalism and Slavery*, 2nd ed. (New York: Russell and Russell, 1961); F. Novais, *A crise do antigo sistema colonial* (São Paulo: Cadernos do CEBRAP, No. 17, 1974).

3 - On the change in the pattern of accumulation in Britain, see, for example, David S. Landes, *The Unbound Prometheus: Technological Change and Industrial Development in Western Europe from 1750 to the Present* (Cambridge, Eng.: Cambridge University Press, 1969), pp. 41ff.; J. A. Schumpeter, *Business Cycles: A Theoretical, Historical and Statistical Analysis of Capitalist Process*, abridged ed. (New York: McGraw Hill, 1964), pp. 201ff.; E. Hobsbawm, *Industry and Empire* (Harmondsworth, Penguin Books, 1969), pp. 109f.

4 - Marx, K. "Futuros resultados de la dominación británica en la India," in K. Marx and F. Engels, *Sobre el colonialismo* (Córdoba: Siglo XXI, 1973).

5 - On the exportation of British capital to Latin America, see J. F. Rippy, *British Investments in Latin America* (1822—1849) (Minneapolis: University of Minnesota Press, 1959), pp. 17—35; I. Stone, "La distribuzione geografica degli investimenti inglesi nell'America Latina (1825—1931)," *Storia Contemporanea*, 2 (1971): 495-518.

6 - On the transformations that occurred between 1873 and 1896, the period of the "Great Depression," see especially Landes, *The Unbound Prometheus*, Ch. V.

7 - The expression is Paulo Santi's. See his "El debate sobre el imperialismo en los clásicos del marxismo" in *Teoría marxista del imperialismo* (Córdoba: Ediciones Pasado y Presente, 1975).

8 - Peláez, C. M. "Análise econômica do programa de sustentação do café," *Revista brasileira de economia*, (December 1971), p. 209.

9 - Cano, W. *Raízes da concentração industrial em São Paulo.* DIFEL: 1977. pp. 41 ff.

10 - Graham, D. Migração estrangeira e a questão da oferta de mão-de-obra no crescimento econômico brasileiro," *Estudos econômicos 3* (São Paulo: IPEUSP, 1971): Il and 13. See also Cano, *Raízes da concentração industrial em São Paulo,* pp. 47 ff.

11 - Graham, D. "Migração estrangeira e a questão da oferta," p. 30.

12 - On this point see the conclusive evidence in Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1889-1945*, (Rio de Janeiro: IPEA, 1973), pp. 112—119. See also Cano, *Raízes da concentração industrial em São Paulo*, p. 58. Note that import values were generally quoted in pounds sterling but import prices were quoted in U.S. cents per pound.

13 - For Brazilian and world coffee production, 1850—1944, see Peláez, "Análise econômica do programa de sustentação do café," pp. 208—211. For U.S. import and Brazilian export prices for coffee over the same period, see ibid., pp. 204—7.

14 - Peláez, "Análise econômica do programa de sustentação do café," p. 205.

15 - On public spending, monetary policy, and price trends, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira 1889-1945*, pp. 105 f.

16 - Michael Hall, "The Origins of Mass Immigration in Brazil, 1871—1914" (Ph.D. diss., Columbia University, 1969), p. 157.

17 - Cano, *Raízes da concentração industrial em São Paulo*, p. 41.

18 - A. Delfim Netto, *O Problema do café no brasil*, 2nd Ed. (São Paulo: Faculdade de Ciências Econômicas e Administrativas, Universidade de São Paulo, 1966), pp. 95, 96.

19 - Peláez, "Análise econômica do programa de sustentação do café," p. 210.

20 - Cano, *Raízes da concentração industrial em São Paulo*, p. 308.

21 - Fishlow, A. "Origens e consequências da substituição de importações no Brasil," *Estudos econômicos* 2 no. 6 (1972), p. 64. On production, see also Villela and Suzigan, *Política do governo e crescimento da economia brasileira 1889-1945*, Appendix A and *passim.*

22 - The evidence on prices and salaries is presented in Cano. *Raízes da concentração industrial em São Paulo*, p. 282.

23 - For trends in wages and industrial production during this period, see ibid., pp. 279, 282, 291-293.

24 - Ibid., p. 282. See also Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1889-1945*, p. 431.

25 - For series on the terms of trade and foreign capital flows, see Villela and Suzigan, P*olítica do governo e crescimento da economia brasileira*, 1889-1945, pp. 441, 451, 452.

26 - Peláez writes, for example: "Industrial development was retarded in large part by the inadequacy of their monetary, banking, foreign exchange, and fiscal policies. This inadequacy, in turn, derived from the slavish adherence to one school of thought, here defined as the school of 'monetary orthodoxy. ' " C. M. Peláez, "Las consequências econômicas da ortodoxia monetária, cambial e fiscal no Brasil entre 1889 e 1945," *Revista brasileira de economia* 25 no. 3 (July—Sept. 1971), p. 8. Villela and Suzigan share the same view: "The evolution of Brazilian economic policy, expressed in monetary, foreign exchange, and fiscal measures, was characterized by sudden and frequent changes in orientation… The lack of administrative continuity was itself a powerful element of confusion in the directing of economic policy. In the first eight years alone, the new Republic had twelve finance ministers. And each one formulated his own policies, in most cases according to a strictly personal point of view." And later: "It is evident that any critique Of the orientation of government policy (monetary, foreign exchange, fiscal, and tariff) should take into account the economic doctrines in vogue in that particular era ." Villela and Suzigan, *Política do governo e crescimento da economia brasileira 1889-1945*, pp. 31 and 233.

27 - For example, see Caio Prado Júnior, *História econômica do Brasil*, 12th ed. (São Paulo: Brasiliense, 1970), Ch. XXII.

28 - See Villela and Suzigan, *Política do governo e crescimento da economia brasileira 1889-1945*, pp. 420-423.

29 - Cano, *Raízes da concentração industrial em São Paulo*, p. 1-45.

30 - J. Murtinho, Relatório do ministro da fazenda (Rio de Janeiro: Imprensa Nacional, 1899).

31 - For more details concerning Murtinho's fiscal reforms, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira 1889-1945*, pp. 105 ff.

32 - On the evolution of public spending and the fiscal deficit, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1889-1945*, pp. 140, Celso 156, 185, Furtado, 414-415.

33 - Celso Furtado, *Formação econômica do Brasil*, 4th ed., (Rio de Janeiro: Ed. Fundo and de Cultura, 1961), p. 168. Translated as T*he Economic Growth of Brazil* (Berkeley and Los Angeles: University of California Press, 1965), p. 182. The translation is that of Ricardo W. de Aguiar and Eric Charles Drysdale.

34 - On industrial investment in the period, see Fishlow, "Origens e consequências da substituição de importações no Brasil," p. 13.

35 - Murtinho, *Relatório do ministro da fazenda*, p. xv.

36 - Ibid., pp. 3-4.

37 - On the balance of payments crisis and the consolidation of the external public debt in this period, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira 1889-1945*, pp. 334 ff.

38 - For price data, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1889-1945*, p. 425.

39 - The details of the "Programa de Regulamento Econômico" are described in Villela and Suzigan, *Política do governo e crescimento da economia brasileira*, 1889-1945, p. 100.

40 - For an appraisal of the Agreement of Taubaté, see Delfim Netto, *O Problema do café no Brasil*, pp. 63ff.

41 - On the Conversion Fund, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, p. 314.

42 - On the money supply during this period, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 412—413.

43 - For data on exchange rates, capital flows, and exports, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 424-425, 439-454; Cano, *Raízes da concentração industrial em São Paulo*, pp. 263-278.

44 - Delfim Netto, *O Problema do café no Brasil*, p. 93. One conto de réis equals 1,000 mil réis.

45 - On the Funding Loan, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 138ff., 337, 338.

46 - Delfim Netto, *O Problema do café no Brasil*, pp. 95-96.

47 - Ibid., pp. 92ff. (on the second valorization scheme).

48 - For coffee prices in 1918, see Peláez, "Análise econômica de sustentação do café," *Revista brasileira de economia* (December do 1971), p. 206.

49 - On federal finances between 1913 and 1918, brasileira, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 140, 414-423.

50 - Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 318-319.

51 - On coffee prices and exchange rates between 1919 and 1923, see Peláez, "Análise econômica do programa de sustentação do café," *Revista brasileira de economia* (December 1971), p. 206, Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, p. 424.

52 - For a description of the third valorization program, see Delfim Netto, *O Problema do café no Brasil*, p. 92ff.

53 - Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, p. 338.

54 - On fiscal trends, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, p. 140, 156, 185, 414-423.

55 - On monetary evolution, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, p. 412-413.

56 - On the Permanent Defense Policy, see Delfim Netto, *O Problema do café no Brasil*, pp. 115ff.

57 - Ibid., p. 121.

58 - Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 157-159.

59 - On the development of Brazil's importing capacity, 1901-1945, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, p. 441.

60 - Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, p. 156, 413.

61 - Delfim Netto, *O Problema do café no Brasil*, p. 170.

62 - Ibid., pp. 139ff.

63 - Furtado, *Formação econômica do Brasil*, p. 188. (T*he Economic Growth of Brazil*, pp. 205-206.)

64 - See the appraisal of Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, and Fishlow, "Origens e consequências da substituição de importações no Brasil".

65 - Fishlow, "Origens e consequências da substituição de importações no Brasil," p. 28.

66 - In contrast to this view, see the works of C. M. Peláez on the question.

67 - The role of the public deficit has been appropriately underlined in the works of C. M. Peláez. However, Peláez unaccountably insists that it was not "intentionally" generated and concludes, curiously enough, that "effective" policy was not Keynesian. Peláez also misinterprets the balance-of-trade "deficit." For a good indication of the debate see Fishlow, "Origens e consequências da substituição de importações no Brasil," p. 29.

68 - Cano, *Raízes da concentração industrial em São Paul*o, p. 142.

69 - Fishlow, "Origens e consequências da substituição de importações no Brasil"; Cano, *Raízes da concentração industrial em São Paul*o, p. 142.

70 - F. H. Cardoso, "Condições sociais da industrialização: o caso de São Paulo," in M*udanças sociais na América Latina* (São Paulo: DIFEL, 1969), pp. 188-189.

71 - A. F. Bandeira, Jr., *A indústria no estado de São Paulo*, 2nd ed, (São Paulo, 1908).

72 - José de Souza Martins, *Empresário e empresa na biografia do Conde Matarazzo*, (Rio de Janeiro: Instituto de Ciências Sociais, 1967). Warren Dean, *A industrializacão de São Paulo*, (São Paulo: DIFEL, 1971).

73 - For foreign loans of the government, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 451-452.

74 - Cano, *Raízes da concentração industrial em São Paulo*, p. 142.

75 - Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 439-440.

76 - Ibid, pp. 424-425.

77 - Compare the figures for capital formation in the Paulista industrial sector between 1895 and 1897 with those for the period 1890—1894. See Cano, *Raízes da concentração industrial em São Paulo,* p. 142.

78 - Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 424-425.

79 - See Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*,, pp. 414-415.

80 - For the evolution of coffee and rubber exports, see Cano, Raízes da concentração industrial em São Paulo, p. 270. For the terms of trade, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, p. 441.

81 - On immigration, see D. Graham, "Migração estrangeira e a questão da oferta," p. 18.

82 - On the development of commercial food agriculture, see Cano, *Raízes da concentração industrial em São Paulo*, pp. 57ff.

83 - See Table 10.

84 - For the evolution of prices, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 424-425.

85 - Fishlow, "Origens e consequências da substituição de importações no Brasil," p. 17.

86 - The three works referred to in this paragraph are: Dean, A industrialização de São Paulo; Fishlow, "Origens e consequências da substituição de importações no Brasil"; and Cano, *Raízes da concentração industrial em São Paulo*.

87 - On the policy of "assistance to national production," see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, p. 142.

88 - On the wartime importation of capital goods, see Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, p. 437.

89 - Cano, *Raízes da concentração industrial em São Paulo*, p. 168.

90 - On wage trends during World War I, see Cano, Raízes da concentração industrial em São Paulo, p. 282.

91 - Cano, *Raízes da concentração industrial em São Paulo*, p. 169.

92 - See Fishlow, "Origens e consequências da substituição de importações no Brasil," pp. 21-22.

93 - See Cano, *Raízes da concentração industrial em São Paulo*, p. 241.

94 - See Fishlow, "Origens e consequências da substituição de importações no Brasil," p. 64.

95 - See Cano, Raízes da concentração industrial em São Paulo, p. 278.

96 - See Fishlow, "Origens e consequências da substituição de importações no Brasil," pp. 26-27.

97 - On tariffs, see, for example, Nicia Villela Luz, *A Luta pela industrialização no Brasil* [São Paulo: DIFEL, 1961], pp. 193 ff; Villela and Suzigan, *Política do governo e crescimento da economia brasileira, 1899-1945*, pp. 346ff.

98 - The intensification of interregional competition was first noted by S. Stein, The Brazilian Cotton Manufacturers: Textile Enterprise in an Underdeveloped Area, 1850-1950 (Cambridge, Mass.: Harvard University Press, 1957), pp. 114, 144-145.

99 - On diversification within the consumer goods industry, see W. Dean, "A industrialização durante a República Velha," in *O Brasil republicano* (São Paulo: DIFEL, 1975), p. 264.

100 - W. Baer, *Siderurgia e desenvolvimento brasileiro* (Rio de Janeiro: Zahar Editores, 1970), pp. 80-81.

CHAPTER 4

NATURE AND CONTRADICTIONS OF THE RECENT FINANCIAL DEVELOPMENT

Maria da Conceição Tavares

Warning Note

This essay represents an attempt to complement the presentation of some themes related to the character and functionality of financial development, already outlined in a paper on Financial Intermediation in Latin America, carried out by ECLAC's Division of Research and Economic Development (DIDE) and presented at the 16th Session of the Secretariat, in May 1971.

It was prepared in collaboration with the Seminar on "Capital Markets and Economic Development" to be held in Rio de Janeiro, in September 1971, under the sponsorship of IBMEC (Brazilian Institute of Capital Markets). The author is aware of the participation of national and foreign specialists who will make their contributions in the theoretical field and is aware of a vast, informative bibliography on the Brazilian financial sector in its recent development since 1964. In this sense, she tried to avoid a general discussion on the role of capital markets in economic development, as well as a long descriptive chapter. Instead, she preferred to focus on aspects of the financial sector functioning that, in her opinion, can be considered more related to the problems of expansion and re-concentration of the Brazilian economy in its current stage.

An interpretive approach to the more general role of the financial sector in the recent recovery process and accelerated growth helps clarify several issues related to the nature of the new style or "model" of development that has been taking shape in recent years.

The paper is made up of four parts. The introductory chapter presents the general problem to be dealt with. A summary presentation of the most general features of recent financial developments follows. The following chapter discusses the main characteristics of the current accumulation process, concentration, and centralization of capital carried out in recent years through an accelerated expansion of financial capital. Finally, the last chapter discusses some of the characteristics of the Brazilian economy's structure and growth style, comparing them with the Japanese post-war experience.

This essay is exploratory in nature. Consequently, the hypotheses raised in it and the possible value judgments implicit in the analysis are the author's sole responsibility and do not necessarily represent the views of ECLAC. Nevertheless, as a document of the organization, already mature and fruit of the work of the team of the Economic Development Division, the paper on Financial Intermediation in Latin America is presented for discussion or information.

Introduction

1.

In recent years Brazil has experienced marked changes in its structure and financial system mode of operation. These did not spontaneously occur as an endogenous reaction to the accelerated process of economic transformation, underway since the 1950s; on the contrary, they were preceded and accompanied by profound changes in the institutional and legal framework that governs the operation of the global economic system and, in particular, of the rules and form of operation of its financial agents, both public and private.

In general terms and to anticipate the main ideas contained in this essay, one can say that the financial sector development since 1964 has achieved the following results:

From the point of view of its functioning, operational modernization, diversification of financial instruments, and a certain degree of function specialization occurred, which allowed for a more fluid functioning of the money and credit markets, as well as the emergence of an institutionalized capital market. These took place within an institutional context of administrative centralization but with a markedly pragmatic economic and financial policy management.

From the point of view of global financing schemes, an open inflationary scheme with external indebtedness linked to severe balance of payments problems was replaced by controlled inflation and a new stage of external indebtedness linked, above all, to autonomous capital movements.

Concerning current financing of the private and public sector, a considerable expansion of liquidity was achieved, reasonably separated from its original source of primary growth of means of payment.

This expansion was achieved, above all, thanks to the development of nonbank indebtedness schemes and through the capture and intersectoral circulation of surpluses, through the issuance of public and private debt securities, with monetary correction.

Regarding the financing of consumption, the urban middle classes' expansion and diversification of durable goods was promoted, which served as a basis for the recovery and development of a series of new or modernized productive sectors in the manufacturing industry, commerce, and services.

In contrast, long-term financing for investments in priority sectors and areas continued to depend basically on special funds, foreign or public, linked to development agencies, national or regional, although with the creation of new financing instruments and proliferation of public funds assigned for specific purposes.

Finally, from 1968 until now, a capital market began to develop more effectively through the formation of investment banks, reorganization of traditional financial sectors, mergers of financial groups, initial public offerings (IPOs), and progressive activation of direct stock markets, mainly on the stock exchange.

In the development of the financial sector after 1964, therefore, two stages can be clearly identified.

The first began in 1965 and corresponds to an expansion and diversification of debt and credit relations among the most dynamic economic sectors, superior to the growth of payment methods. In this process, the following intersectoral indebtedness relations should be highlighted:

- within the private sector (companies and consumers), through the indirect intermediation of "financial companies;"
- between the private and the public sector, through compulsory placement (in the banking system) or free placement (to the public) of public debt securities with monetary correction;
- between the private sector and abroad, through large inflows of short-term capital, with public and private financial intermediation.

Finally, it is worth highlighting the creation of a specialized financial subsystem, housing, which articulates compulsory (salary fund) and voluntary (real estate bills) savings mechanisms for civil construction financing. Above all, intermediation takes place through the National Housing Bank (BNH), which also serves as the Central Bank for discounts on private real estate securities issued by finance companies or real estate companies. The particularity of this subsystem is that credit mechanisms are explicitly articulated in it with savings-investment mechanisms, due to the specialized nature of the type of intermediation it carries out; the general credit functions predominate in all other financial institutions, as the raising of resources from the surplus units has no specific destination.

The second stage begins in 1968 with the effective structuring of a capital market. This stage corresponds to an expansion of financial capital, that is, the creation of securities that allow the modification of the companies' patrimonial state and the general property relations of the "capitalistic" economic pole. The overall functionality of this process would not be so much to solve the problems of financing production or expenditure (whether in consumption or investment) but, above all, to allow the "unfreezing" of the capital invested in productive activities through its conversion into financial capital. In this way, intersectoral mobility and its subsequent centralization in the sectors of activities with greater dynamic perspectives can be increased.

2.

It would be appropriate to draw attention to some characteristics of financial capital related to its purpose in the general accumulation process to anticipate the argument about the nature of financial accumulation developed in the third chapter.

In this sense, the potential of capital in the financial form, as historically realized in developed countries in the stage of oligopolistic accumulation, and when capitalist accumulation was generalized on an international scale, could be summarized as follows[1]:

- Enabling financial accumulation by creating "fictitious" capital, that is, issuance of title deeds with the right to income, whose valorization depends on speculative operations in the launching or circulation of the titles in secondary stock markets.
- Separating functions of the entrepreneur from those of the capitalist. The first would be in charge of the company's internal organization to produce profits, that is, surpluses that can be transformed into capital. The second showed as a holder of property rights over the resulting income and would be responsible for its accumulation in the form of financial capital, as well as its conversion into productive capital through application in the sectors that seem more profitable (one of which can be the very financial sector for a while).
- Allowing the association of industrial, commercial, and banking capital under the hegemony of financial capital, thus giving the latter the possibility of promoting greater centralization of capital in its most general form, of property rights and, therefore, ultimate control of the global process of accumulation. This last potential of financial capital is the one that is mainly being discussed in the current stage of Brazilian financial development, when the formation

1 We refer, basically, to the theorization on Finance Capital made by Hilferding, in his famous book with the same title (Ed. Tecnos, Madri).

of holdings, corporations, or conglomerates as forms of business reorganization is proposed.

3.

In fact, the trajectory of recent financial development in Brazil, despite having resolved the fundamental problems of liquidity or current financing of companies in a relatively heterodox way, the government deficit and consumer financing seem to have not reached a substantial increase in the real rate of domestic savings. In this way, the hope, often expressed in "apologetic" documents about the development of the capital market, that the latter would be aimed at increasing the economy's savings-investment rate has been frustrated[2].

On the other hand, what is indeed being achieved in the current stage of restructuring of the financial market is the fulfillment of its primary functionality, which is to allow greater mobility of financial resources and their subsequent centralization in favor of activities that present higher rates of return or better prospects of competitive power in the national or international market.

This "financial capital" centralization process would confirm the high degree of concentration of urban economic activity in the country's leading industrial and financial centers and lead to a marked change in the oligopolistic economy structure through association and merger of domestic and foreign business and financial groups. The new forms of capital association tend to lead to a type of oligopolistic structure that assumes a much greater degree of international opening of companies and a progressive internationalization of the main economic sectors. However, several problems need further clarification; the most important is the objective basis for sustaining this business re-articulation.

Among the doubts about the fate of the possible advances of "financial capitalism" are the following:

- Is this really a process that moves towards the organic articulation of forms of financial accumulation and expansion of the real investment rate? In other words, will the current mergers of groups and IPOs continue to be carried out under strictly financial objectives, or will they attempt a more general re-articulation due to technical reasons of expanding productive capacity and increasing the scale of production, aiming at an increase in competitiveness and at the conquest of new markets?

2 The basic misunderstanding of this hypothesis about the functionality of the capital market, both in theoretical and historical terms, has already been pointed out in the work on Financial Intermediation in Latin America presented at the aforementioned Seminar promoted by IBMEC, which serves as a supporting document for this essay. (See mainly chapters 1 and 2.)

Will this re-articulation occur through the establishment of two separate business orbits, the productive and the financial, although with crossed solidary and director interests, or will it tend to form true conglomerates under the hegemonic control of which groups?

- Will the State, in addition to being a mediator between the interests of national and international groups of different origins, be the true articulator that will promote and control greater integration between the real and financial spheres?

In this essay, we will try to follow several exploratory clues to discuss these hypotheses without reaching definitive explanations. As understood, confirmation of the current optimism regarding the duration of the accelerated expansion and the clarification of the true character of the new "development model" underway will ultimately depend on the adequate answer to these questions.

I. General characteristics of recent financial evolution

To understand the economic significance of recent financial expansion and diversification, let us briefly return to the issue that involved the Brazilian economy in the first half of the last decade. Once the expansive effects of a set of public and private investments (mainly foreign) that characterized the intensive import-substitution stage had been exhausted, the economy needed to find new sources of dynamism, at the same time that its public and private financing schemes had used it, until the possible limit, the internal inflationary and external indebtedness mechanisms.

In fact, the possibilities of realizing the productive potential implicit in the new or modernized sectors (of durable consumer goods, intermediate products, and capital), and vastly underutilized, were hampered by two essential circumstances:

- the relatively reduced purchasing power of the "middle" social strata, potential consumers of new goods and services[3];
- the growing impossibility of the Government and companies to finance themselves or to use new external sources to cover their sales or autonomous investment programs, in some cases of long maturity.

Among the problems that arose in overcoming this impasse were those related to the financial system organization and functioning, an essential

3 See "Distribución del ingreso en América Latina", ECLAC, 1970, chapter on Brazil.

element to allow for changes in demand schemes and facilitate the transfer of resources to cover investments, especially in the public sector.

Until then, the traditional financial apparatus, distorted by years of chronic inflation under conditions of a maximum legal interest rate of 12%, counted on multiplying credit, basically, with the primary expansion of means of payment and the increase in deposits in the commercial banks. But, on the other hand, the unbridled growth of the number of bank branches to capture cash deposits from the public while allowing for an increase in the profits of the banking system (given the differences between the cost of money and legal interest rates), increased operational costs, without new sources of medium- or long-term fundraising.

Foreign capital had ceased to be interested in new applications in Brazil, given the situations of the economic and political crisis that had existed since 1962-63. The net inflow of autonomous risk capital remained to decline until the new institutional accommodation effects were verified.

Among the first measures adopted by the Government that took over in 1964 are the drastic changes in the wage and foreign capital policies - whose effects on the capture of surpluses would take place in the medium term - as well as a set of emergency measures to solve the short-term financing problems, both from the public sector and the dynamic sectors linked to foreign capital. Among the latter, the emergency tax reform, the periodic correction of the nominal value of public debt securities, and Instruction No. 289 of former SUMOC[4] could be highlighted to allow the inflow of short-term capital, mainly intended to finance the dominant companies' working capital.

After 1966, a new financial scheme came into full operation, supported by the new legal framework, which had been in development since the end of 1964 and markedly changed the ways fiscal and financial resources were raised.

We will focus, basically, on the financial apparatus modifications.

I. 1. The New Legal Framework and Its Effects on the Financial Sector Organization

The banking reform at the end of 1964, in addition to the law creating the Central Bank and the housing finance system centered on the National Housing Bank, promoted a broad ordering of the national financial system, which was complemented in 1965 by the capital market regulatory diploma.

The basic innovations of the capital market law reside in the introduction of the monetary correction clause in almost all operations of the financial

4 SUMOC is the acronym for Superitendência da Moeda e do Crédito, the agency that had central banking functions before 1965 (revisor´s note).

system and in the regulation of the general forms of operation of publicly traded companies, investment companies and banks, brokers and securities distributors, as well as the character of the main capital market instruments (endorsable shares and bonds, convertible debentures, etc.).

The National Monetary Council (established by the banking reform in place of the former SUMOC council) continued to periodically review the concepts and basic forms of regulation contained in that legal diploma through Central Bank's resolutions and circulars.

Among the dozens of resolutions and decrees adopted between 1965 and 1970, the most important concern the following aspects of the financial system reorganization:

- creation of real estate credit companies and real estate portfolios in financial institutions, thus facilitating through real estate bills (adjustable value) the fundraising from the public and the structuring of a financial subsystem for housing;
- regulation of the functioning of Investment Banks regarding the operation of medium and long-term credits and forms of fundraising; subscription of shares and debentures, licenses to obtain loans abroad and make transfers, placement of bills of exchange of their acceptance in the stock market, sale of investment fund quotas, fixed-term deposits with or without issuance of certificates. Subsequently, a series of Central Bank resolutions followed, regulating the issuance of equities and underwriting operations, minimum capital limits to create investment banks, ways of raising external resources to finance fixed or working capital, the registration of legal entities issuing securities negotiable in the Stock Exchange, the functioning and operations of the Mutual Funds, etc.
- the operating system of financing societies was completely overhauled, attributing consumer credit as their predominant field of activity and conditioning their performance in activities that don't compete with investment banks. The "bearer" modality in bills of exchange with an anticipated discount was eliminated, and an attempt was made to replace it with securities with a posteriori monetary correction. Norms were established regarding the volume of active operations of financial institutions to avoid their excessive expansion;
- regulation of consortia and other forms of popular savings associations to protect public interests and prevent the proliferation of these agencies and other autonomous ones (see Chart 1);

Chart 1 – Number of Capital Market Institutions 1969-70

Publicly traded corporations	400
Stock Exchanges	14
Investment Bank	30
Mixed-type Credit, Financing and Investment Society	213
Investment company	3
Real Estate Credit Society	41
Brokerage Company	40
Distribution companies	573
Securities Intermediaries	21
Autonomous Agents	8133
Consumer Consortium	457
Mutual Investment Funds	58
Tax Funds (institutions authorized to manage them):	
Investment banks	25
Credit, Investment and Financing Society	125
Brokerage Company	45
	195

Source: DELTEC and Central Bank.

- regulation and modernization of stock exchange operations. Since 1966 until recently efforts have been made to regulate and modernize operations on stock exchanges to ensure conditions for trading securities, stimulate the market, regulate brokers' activities and allow for a greater pace of operations;
- resolution on raising foreign funds, allowing the entry of short-term capital to be transferred to companies by commercial banks (which operate in foreign exchange), private investment banks and the National Bank for Economic Development (BNDE);
- finally, tax incentive laws and decrees since 1966 until now have allowed successive deductions of income tax, for individuals and companies, for application in priority areas or sectors and in new shares, debentures and other securities, public and private, of publicly traded companies. This last aspect favored the opening of capital of some companies and stimulated investment banks' underwriting operations.

Tax incentives, which began with priority investments in the Northeast, are now so broad that a large part of the income tax on individuals and corporations may be exempted through financial institutions with a good "portfolio" of shares in companies that meet the basic requirements. After the Decree No. 157, which established incentives only for investments in effective capital increases, the Central Bank allowed one third of the resources raised by investment funds to be used to acquire shares on the stock exchange previously issued by companies registered for tax exemption purposes. In mid-1970, the Central Bank authorized a new expansion, from one to two-thirds, of the investments of the "funds 157".

These facts, together with the increase in the number of taxpayers of income tax and the thougher inspection on tax collection, is partly due to the sudden rise in the movement of shares on the stock exchange that took place after 1969. Later, at the beginning of 1971, the rise was stimulated by a growing movement of initial public offerings, under new incentive laws for the revaluation of assets and capital expansion.

Chart 2 – Number of Operating Financial Institutions Year end

Item discrimination	1964	1965	1966	1967	1968	1969	1970
Commercial banking establishments	336	331	313	261	231	213	195
Development banks							
a) Federal	1	1	1	1	1	1	1
b) State							
State Banks	1	1	2	2	3	7	9
National Housing Bank	1	1	1	1	1	1	1
Investment Banks			7	21	21	29	30
Savings Banks							
a) Federal	22	22	22	22	22	22	1 [(a)]
b) State	4	4	4	4	4	4	5
Financing societies							
a) without real estate portfolio	134	202	272	247	235	203	212
b) with real estate portfolio			3	10	10	9	
Insurance company	144	151	157	156	157	158	157
Real Estate Loan societies			2	22	25	34	44
Savings and loans societies					21	32	32
Brokerage companies				254	377	394	404
Distribution Companies					556	576	573
Investment companies [(b)]				9	6	3	

Source: Central Bank Report, 1970.

(a) Unification of Federal Savings Banks in accordance with Decree-Law No. 759, of 8-12-69.

(b) Until 1966 these entities were included in the total of financial institutions.

I. 2. Major Changes to the Financial Structure

The main changes that occurred in the financial structure can be examined in Chart 3, which shows the composition, by origin, of credit to the private sector in the period 1964-70.

Chart 3 – Financial System: Loans and Financing By Institutions Lending to the Private Sector

Item	End of 1964 Millions of Novos Cruzeiros			End of 1970 Millions of Novos Cruzeiros		Average real annual expansion rate (at 1970 price)
	Absolute values	At 1970 prices	%		%	
Banking system	3,267	16,299.60	79.9	36,931	56.6	14.7
Commercial Banks	2,226	11,105.80	54.4	24,213	37.1	13.9
Banco do Brasil	1,041	5,193.70	25.5	12,718	19.5	16.0
Development agencies	571	2,848.80	14	6,219	9.6	13.9
Credit and Investment Company and Investment Banks	245	1,222.30	6	11,642	17.9	45,6
Credit and investment Companies			6,379	9.8		
Investment banks			5,263	8.1		
Housing Financial System			9,322	14.3		
Others (savings banks)			1.038	1.6		
Total	4,083	20,370.70	100	65,152	100	21.4

Source: Central Bank of Brazil report.

The new circumstances of expansion required, at first, greater diversification and specialization for financial intermediation functions, both public and private. This movement of expansion and modernization, having taken place very quickly and in parallel with important institutional changes, giving rise to new forms of financial fundraising, has appreciably changed the relative importance of different groups of institutions in private financing and its form of organization and internal and external relations.

In this process, there is a marked loss of relative importance of the banking system (it fell from 80% of total credit to the private sector in 1964 to 56.5% in 1970) and a corresponding increase in the weight of diversified financial intermediation, especially of the financing companies and investment banks and the emergence of an important financial subsystem for housing which alone represents more than 14% of total credit to the private sector. On the other hand, the relative weight of Banco do Brasil (State Bank) and Development Agencies in the total credit granted decreased, despite the greater specialization of their portfolios and the creation of countless public development funds.

New forms of fundraising have also markedly changed the composition of financial assets held by the public. This is how, between 1964 and 1970, the share of monetary assets (currency and demand deposits) dropped substantially, and the characteristic bonds of extrabank institutions, trade acceptances and real estate bills increased significantly (from 4% in 1964 to more than 16% in 1970). The same happened with the inflation-indexed public debt bonds, which in 1970 came to represent almost 11% of the main financial assets outside the monetary system (see Chart 3).

The increase and diversification of new institutions was followed by an acute process of competition for resources and clients, which raised the financial costs of operation, liquidated a certain number of traditional agencies (banks and small finance companies) and gave way to an intense reorganization process of private financial groups.

This process of merger and concentration of the banking system, which had been going on since 1958 as a result of the greater profits caused by the acceleration of inflation, was accentuated, this time, by competition from new extrabank branches. Thus, the number of commercial banks, which had decreased from 399 in 1958 to 335 in 1962 and remained practically stationary until 1964, from then on began to decline in an accelerated manner by successive mergers and re-concentrations, reaching only 195 establishments in 1970 (see Chart 2).

Credit and financing societies that had been operating without control for several years, and escaping the usury law through various means, multiplied rapidly after 1963, more than doubling their number in three years and operating in an entirely inorganic form, including in illegal parallel markets. In 1966, with the beginning of mandatory registration and a more intense legal framework for its operation form, they reached their peak (291 companies) and from then on they constantly declined through the same process of disappearance, merger and re-concentration.

Finally, the new financial institutions that emerged from 1966 onwards were investment banks, real estate credit societies and savings and loan associations, with a multiplicity of securities dealers and brokers (see Chart 2). The number of these new agencies has multiplied rapidly since 1968, concomitant with an unprecedented revival of the stock exchange; however, there are indications that its limits of competition and specialization have been reached since late 1969, starting a new process of re-concentration, now under the clear control of the most powerful financial and international groups.

Of the 30 investment banks existing in 1969, 10 had explicit links with foreign groups, and of the rest, all but 4 originated from mergers or reorganization of financial groups supported by old commercial banks. In fact, the tendencies towards financial re-concentration and the formation of new financial groups, with or without articulation with the traditional ones and abroad, have been clearly manifested since 1966, having been accentuated even before the most recent changes in the legislation on incentives to mergers of private groups?[5]

In the race to control and expand the financial market, the old national private banking system has been forced to adapt to new circumstances through an intense technological modernization of banking procedures, but above all to seek support in the creation or association with national or international extrabank financial corporations.

Currently, almost all large Brazilian commercial banks operate in the direct consumer credit market through controlled or associated financial societies. Of the deposits placed in the 50 largest private banks, more than 57% were in banks linked to credit, financing and investment companies[6].

Thus, the loss of bank participation in the assets of credit financial institutions to the private sector does not mean loss of financial power of large banks, but rather a financial system reorganization in which banks took advantage of the facilities granted to nonbank intermediation to expand in that form.

The advantages of diversification from the point of view of large financial groups lie less in economies arising from market specialization than in taking advantage of the differential advantages granted by financial policy to various types of new institutions, with the aim of stimulating and developing the financial market.

From the point of view of the general expansion of the system's liquidity, the fundamental advantage of non-banking intermediation resides in the fact that its fundraising is not subject to any type of reserve requirement and its multiplication of credit does not depend on, to a certain extent, the primary expansion of the means of payment and the Government's monetary policy.

5 See the networks of the various financial groups in Informe Banco Halles - Investment Banks.

6 See INDEX — The participation of Commercial Banks in the Brazilian Credit Market - April, 1970,

The formation of new foreign financial groups and the re-articulation of some old national groups, centered on investment banks and through the prior merger of commercial banks and financial groups, with their constellation of brokerage agencies and securities distributors, is the most important recent trend in the process of financial re-concentration. These new groups acquire hegemonic position in the process of increasing control of financial capital and some of them try to reach the conglomerate stage, that is, the type of capitalist centralization in which financial expansion is intertwined with control or participation in companies in the most distinct productive branches of goods and services.

Further on, when examining the problem of concentration and centralization of capital, we will try to better illustrate the complexity of these relations and advance some preliminary hypotheses about the implications of this "conglomeration" movement regarding the nature of the articulation between national and foreign groups present in Brazil.

I. 3. Relation between Financial Expansion and Growth Acceleration

The financial expansion that took place in the 1964/70 period markedly changed the general financing schemes of the public and private sectors, allowing them to detach themselves from the primary issuance of means of payment, through the placement of non-monetary assets with the public.

Even after 1967, when a regime of greater monetary liquidity was introduced, the financial assets corresponding to the expansion of nonbank intermediation continued to grow at a much higher rate than monetary assets (see Chart 4).

Together, and in real terms, while the means of payment grew at an annual average rate of 5.7% in the period 1964/70, which roughly equaled the GDP growth rate, non-monetary assets grew 37 .5% per year, based mainly on public debt instruments (ORTN) and private debt (trade acceptance).

The National Treasury's inflation-indexed bonds functioned in several years of the period as a liquidity-absorbing instrument, as they were issued in proportions much higher than the Treasury's cash deficit financing; on the other hand, since 1967, they became a financing mechanism for a growing share of public spending[7].

7 In 1970, the amount of public debt financed with ORTN already reached 5.6% of GDP.

Chart 4 – Financial Assets in Public Holding (In Percentage)

	Year-to-year rates of change - at 1970 prices					Annual increment rates in the period			Structure of assets	
	1964/1965	1965/1966	1996/1967	1967/1968	1969/1970		1964/1970	1965/1970	1964	1970
Monetary assets	11.3	-15.4	11.5	15.0	9.8	4.9	5.7	4.5	88.4	61.1
Paper money	-4.4	-1.2	-2.7	11.5	9.1	4.6	2.5	4.0	18.8	10.9
Deposits in Cash	15.6	-18.5	15.3	15.8	10.0	5.0	6.4	4.7	69.6	50.2
Non-cash assets	37.5	20.2	58.1	45.3	26.2	41.0	37.5	37.4	11.6	38.9
Savings deposits				317.1	114.8	86.4				3.2
Time Deposits	14.5	-3.6	60.2	51.9	13.8	81.1	33.0	37.0	2.7	7.3
Import and exports letters from Banco do Brasil	-73.8	-99.0							4.2	
Trade acceptances	80.9	-5.5	81.0	74.3	12.1	12.1	36.4	30.3	4.0	13.6
Real estate bills			1462.7	165.1	65.6	56.1				2.8
ORTN	568.9	106.1	28.3	-4.9	40.5	37.4	78.6	37.1	0.7	10.9
National Treasury bills										1.1
Overall Total	14.4	-10.5	20.2	22.5	14.6	16.5	12.4	12.0	100	100

Source: Central Bank of Brazil Report — 1970.

The expansion of credit to the private sector reached the highest growth rates in real terms since the post-war period, once the period of restrictive credit policy (1956/66) had passed; on average, it reached an overall rate of 21.4% per year.

Even during the period of monetary restriction, which translated into a sharp decrease in the volume of means of payment in real terms (down 15% in 1965), and practically led to the freezing of bank credit levels in current terms, nonbank institutions managed to expand their applications at a pace considerably higher than that of inflation.

The extrabank credit of financial institutions grew at an average rate of 45.6% per year in the period 1964/70. This, together with the creation of the housing subsystem (which between 1967 and 1970 reached 14% of total credit), allowed a reactivation of urban economic activity led by investment in construction and production of durable consumer goods, increasing production levels in the 1968/70 period at rates never seen in previous periods.

The financing of consumers and companies' working capital has been carried out simultaneously through the issuance of bills of exchange. One can get an idea of the meaning of these debt securities as a factor in sustaining demand, taking into account both their average rate of expansion in the period and the global amount of acceptances in 1970: 8.3 billion cruzeiros. This figure, which reflects the extra-bank private debt, is higher than the public debt and represents practically double of the celebrated movement of equities on the stock exchange in 1970 (see Chart 5).

Chart 5 – Main Negotiable Financial Securities on the Capital Market

	1967	1698	1969	1970	Annual rates of change in 1970 prices (percentage)		
	in millions of cruzeiros novos				1968/1967	1969/1968	1970/1969
Bill of exchange	2,105	4,558	6,172	8,285	74.3	12.1	12.1
Real estate bills	104	461	922	1,724	165.1	65.6	56.1
Treasure bonds	2,013	2,379	4,035	6,640	—4.9	40.5	37.4
Shares issued under Decree No. 157	57.3	818.3	286.8	108	66.1	100.8	-68.6
Shares issued for initial public offering			141.80	341.9			101.2
Movement of shares on the São Paulo and Rio de Janeiro stock exchanges	501	612.1	2464.1	4578.3	-1.6	233.4	55.1

Source: Central Bank of Brazil report.

Another indicator of the importance of the type of credit granted by credit, financing and investment companies is the increase in their relative participation in the total credit to the private sectors, from 6% in 1964 to 17% in 1970, representing, this year, an amount of loans similar to that granted by Banco do Brasil, through all its general, agricultural and industrial credit portfolios, and equivalent to almost double the loans granted by all development agencies in the country.

This increase in the extrabank private debt took place under conditions that the current financing of commercial banks also grew at a very high average rate in the period (14.7% per year, in real terms), allowing for a considerable expansion of liquidity and generalization of the real movement of transactions, originated in a few sectors linked to the urban consumption of the middle social stratum. These strata, through their growing indebtedness, have been the basic support for the expansion of the urban market for goods and services.

From the end of 1968 onwards, the accelerated financial development linked to the multiplication of debt relations within the urban sector of the economy was added to the speculative euphoria in the stock exchange, bringing the issue of the capital market to the center of attention.

Based on the aforementioned stimuli, and once a strong speculative climate was established, the movement of shares on the stock exchange grew rapidly in 1969 (more than 200% in real terms) and more moderately in 1970 (see Chart 5). The volume of transactions jumped from 100 million dollars in 1968 to almost 900 million in 1970, but almost half is due to equity appreciation.

The fiscal incentives of Decree No. 157, despite all introduced changes, did not reveal the expected dynamism, as share issues under that decree, after a 100% increase in 1969, fell by 68% in 1970. On the other hand, incentives for companies to go public have been obtaining results that seem to last longer, given the fact that the funds raised by companies in this way are unregulated.

Issuance of new shares through public offerings, with successive issuances, increased by 100% between 1969 and 1970 and the number of new companies registered by IPOs rose from 27 in 1968 to 88 in 1970, totaling, in that period, an issue of Cr$750 million, and reaching the number of publicly traded companies to 400 companies of all branches (including 117 financial societies)[8].

The extraordinary atmosphere of euphoria that prevailed during the first half of 1971 is the result of the extremely high profits obtained in IPOs and in the unbridled speculation that was established in the intermediation between the primary market and the secondary market ("over the counter"), even before the shares reached the stock exchange. This climate has forced an excessive valuation of equities, which could lead to serious disturbances in the development of the so-called capital market, and there seems to be a certain consensus that greater regulation of this type of operations should be sought.

The overall meaning of the financial accumulation carried out initially with securities and, later, with equities will be discussed in some detail in the next item. However, it can already be pointed out that, due to the dynamics of the ongoing expansion process, the financial orbit is gaining relative autonomy, which puts at risk the maintenance of an accumulation rate, without having contributed so far in a decisive manner, for an increase in the overall rate of domestic savings in the economy. Thus, part of the apologetic arguments about the capital market development and its influence on the

8 See "Economic Conjuncture", vol. V, no. 4, 1971 — special issue on Capital Markets and 1970 Central Bank Report.

increase in the real macroeconomic savings-investment rate has no support in concrete experience[9].

The relations between financial expansion and economic growth acceleration seem to be reduced, until this stage, to a mere re-invigoration of the economy through the expansion of a restricted consumerism and an unprecedented speculative euphoria since the agitated times of the financial boom of the 1920s.

II. Financial accumulation, concentration and centralization of capital

A process of financial accumulation basically means the capitalization of income obtained from financial securities that constitute "capital" only in the generic sense of a property right over an income. The realization of this income does not rest directly on the production process, but on a right to a share in the surplus generated by a company or by the economy as a whole. This right can be legally regulated as in the case of fixed-income securities, or it can be random, based both on the issuing company's expectations of profitability and on the rules of the institutional game and the company's own behavior (in the case of shares and other financial assets of variable income). In this case, the value of capital can fluctuate intensely according to the characteristics of the stock market, the public "trust," the economic situation of the companies and their own profit distribution policy.

Financial and Productive Capital

In the first instance, the accumulation of financial assets does not have a direct relationship with the macroeconomic savings-investment process because it does not necessarily imply the accumulation of real assets. In fact, the process of financial accumulation means only a modification of the patrimonial states of the different economic units and their relations of participation in the effective economic surplus generated by the economy. Financial capital

9 This is, in fact, not surprising if we take into account that, for a rate of investment that grows slowly, domestic savings are continually "complemented" by foreign savings, through growing deficits in the current account balance, re-established from 1967 onwards, despite strong increases in exports.
Although the amount of the deficit already exceeds 500 million dollars a year, it has been insufficient to absorb the inflow of capital in real terms thanks to a liberal policy of imports and remittances of services from foreign capital. This, by placing a heavy burden on the foreign exchange needs of the Brazilian economy, has simultaneously translated into an increase in the external debt and in the accumulation of international reserves. In fact, everything happens as if there was a potential for accumulation in the economy (which resides in the possibilities of increasingly mobilizing internal and external "savings"), far superior to its possibilities of realization, that is, of translating into productive investments.

does not represent, therefore, the result of the production and accumulation of economic surplus, but of the generation and "accumulation" of property rights.

In this way, it is possible that the volume of the surplus produced is not changed, but only the way in which this surplus is appropriated, that is, the way in which property rents are distributed among the assets' owners. It is in this sense that financial accumulation can be understood as a process of creating "fictitious" capital, which rests on the development of legal property relations that allow the separation of functions between entrepreneurs and capitalists[10]. This separation of functions poses the problem of converting financial capital into productive capital, that is, the way in which the two levels of accumulation are articulated, in the real and financial spheres. Thus, for example, given the demand conditions existing in a given period, it may be more interesting for both entrepreneurs and capitalists to invest resources in financing a growing consumer debt, private or public, rather than expanding the capacity production of companies; in these circumstances, the process of accumulating financial assets would be accelerated without a counterpart in an equivalent expansion of real assets. The possibilities of the aforementioned reconversion of financial capital into productive capital will depend, precisely, on the way in which the functions of capitalists and entrepreneurs are articulated inside or outside the company, as well as on the objective interests of both in the global process of accumulation.

Savings and Investment

This same phenomenon can now be observed from a microeconomic point of view. The "final savers," that is, the surplus economic units, invest financially, acquiring fixed or variable income securities that allow them a personal capitalization. In this sense, from their angle, they are accumulating at a certain rate of return, which depends on financial market conditions. From the point of view of the institutional financial investors (that is, the main agencies of the capital market), there can be both a simple intermediation operation, through the collection of commissions, or the application of resources (their own or from third parties) in the purchase of securities, which represents a financial investment whose risks will vary inversely with

10 We are not referring here to the usual separation of functions (of Schumpeterian inspiration) between the entrepreneur as the organizer of production factors and the capitalist as the financer of the production process. In this context, the business function is concerned with the production and accumulation of real surpluses, that is, the generation of profits and their accumulation within the company, resulting in the expansion of productive capacity. As for the capitalist, their fundamental role is not well characterized as a financial agent in the process (this is the function of credit institutions), but, above all, as holders of property rights that allow them to "accumulate" capital in an orbit different from the real one, that is, finance capital.

portfolio diversification and whose profitability will depend on the real or fictitious securities appreciation. With regard to the primary issuers that get into debt, there is a change in their equity status in the value and composition of their liabilities and assets. This indebtedness depends on several factors and has multiple uses. Thus, the greater demand for external funds by companies may be due to liquidity problems or be linked to investments aimed at increasing profitability or reducing risks. In all cases, it may be convenient to absorb resources in order to change the composition and terms of the existing debt and modify the structure of investments, without this giving rise to the expansion of production capacity.

In this way, there is no direct articulation between savers and those who use the resources and, as a result, savings from surplus units do not necessarily convert into real investment. It is one thing to carry out investments based on the profitability of securities, another, quite different, is that the resources that flow from surplus units (families and companies) are invested by companies in expanding their productive capacity.

The realization of new real investments will depend not only on the possibilities of self-financing or on obtaining credit by companies, but, above all, on the relationships existing in the market between the structure of the profit and interest rates and the expected rate of return of the new investments (profitability and risk expectations).

Financial Accumulation and Real Capital Formation

The fact that a process of financial accumulation can take place at a different pace from that of real capital formation is evidenced by the historical experience of developed countries, where for long periods there were increases in public and private debt at a rate significantly higher than the growth in national income and capital stock[11].

It should be noted, however, that a divergent evolution of the real and financial spheres requires, in order to be compatible with the dynamic sustainability of the economy, a relative stability in the companies' net profit rate and in the average return of bonds. In fact, a sharp divergence between the growth trends of the variables in the real and financial spheres has always been considered a source of disturbances and, eventually, of crises.

These divergent movements can result from different causes that affect either the rate of return on securities or the company's rate of profit.

Historically, two procedures have been used to imply greater control and centralization of financial capital to avoid sharp fluctuations in bond

11 See Goldsmith, La estructura financiera y el crecimiento económico, ed. CEMLA.

profitability. The first rests on an increase in the "weight" of public financial institutions regarding the degree of effective participation in the money, credit and capital markets (such as France, Italy, Mexico and Japan)[12]. The second consists of the progressive transfer of control and financial accumulation to the "steady hands" of the large institutional savings-investor agencies – this is basically the case in Anglo-Saxon countries[13].

This centralization movement alone does not solve the problem of disparity between financial and real profitability and between different accumulation rhythms; however, it prevents divergent trends from manifesting in business cycles or even in acute financial crises.

With regard to the companies' expected rate of return, or their effective rate of profit, there are much fewer possibilities for control. The very increase in business concentration and the shift to a strongly oligopolistic productive structure[14] is not a solution to the problem of stability in the rate of profit. On the contrary, it can even be argued that an increase in the degree of monopoly of the business sector destabilizes the rate of profit, divorcing it from the equilibrium rate, that is, the rate that would be capable of producing a pace of real accumulation sufficient to absorb the potential for internal accumulation of companies. An increase in the profit margin per unit of production, that is, in the degree of monopoly, corresponds to an increase in the accumulation potential of oligopolistic companies, which, if conditions of global demand were maintained, would only be compatible with a stable profit rate through an increase in capital intensity, a decrease in the companies' external indebtedness rate, or an increase in planned idle capacity (the one that corresponds to the expansion strategy of large companies)[15].

If we admit, however, a relative stability of the oligopolistic structure, the maintenance of an equilibrium profit rate will fundamentally depend on the pace of expansion of consumption by middle and upper social groups and on the investment of capitalists[16]. Temporarily, any dynamic insufficiency

12 In Brazil, the participation and control of public institutions is important in the money and credit market, but their participation in the capital market has so far been done more through fundraising instruments (ORTN and shares of public companies) than properly by market regulatory mechanisms or institutions.

13 See Gurley & Shaw, "Financial Aspects of Development," The American Economic Review, September, 1955, no. 4

14 In which the forms of competition change sharply and leading companies can, in principle, maintain a high differential profit margin that protects them from an unfavorable market situation.

15 See Steindl, Maturity and Stagnation in American Capitalism, Oxford, Ch. IX, on the model of accumulation under oligopolistic conditions.

16 Kalecki, Economic Dynamics. The consumption of capitalists in Kalecki's simplified model would be equivalent to the urban consumption of the upper and middle classes. The model assumes that wage-earning consumption is approximately equivalent to the cost of wages and, as such, there is no estimateable savings. This simplifying hypothesis can be accepted with a certain degree of realism if we assume that the only significant popular savings are linked to a specific financing subsystem - housing – in fact, institutional savings.

in investment can be compensated for, even under accelerating growth rate, through a more than proportional increase in the consumption of high-income classes, the public deficit or the current trade balance surplus, but in the long run there seems to be a consensus that the investment rate is the crucial variable.

Articulation of Real and Financial Accumulation - The Conglomerate

This consensus on the importance of maintaining or raising the investment rate has led not only to increasing degrees of state intervention in promoting and guiding investments in key sectors, but, above all, in countries where the private sector is dominated by large oligopolistic companies., to accentuated changes in the structure of companies, as well as in their forms of organization and expansion strategy.

One of the most notorious expressions of these changes resides in a new form of business organization that came to be known as “conglomerate” and gained prestige from the Japanese and German experiences. Its fundamental characteristic consists of a greater articulation between the real and financial spheres, through which, historically, financial capital has been given a predominant role in the articulation of business interests in the global accumulation process[17].

The Japanese conglomerate (Keiretsu) case and the meaning of its internal dynamics have already been briefly described in the second chapter of the research supporting this essay, “Financial Intermediation in Latin America”[18]. In summary, and for the purposes of this argument, it is only worth pointing out that the conglomerate’s expansion strategy consists of diversifying production and investments in the main dynamic sectors of the economy, taking into account the conditions of the domestic and international market. This expansion takes place from a central financial nucleus that has practically unlimited issuing power in favor of the conglomerated companies and which maintains an immense power of accumulation, thanks to the intersectoral relations within the group and its enormous agglomeration economies.

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17 Although the Brazilian scenario of the early 1970s is substantially different from the scenario of German capitalism at the beginning of the century, part of the analysis made by Hilferding in his Finance Capital, ed. technos, continues to be interesting, especially with regard to the functions of financial capital: allowing the unfreezing of industrial capital, its mobilization and intersectoral transfer through a fusion of interests from all spheres of industrial, commercial and financial accumulation, under the aegis of the latter.

18 For more details, see the reference article “Rapid Economic Growth in Post-War — Japan” in Developing Economics vol. V, No. 2, June 1967.

Thus, the apparently extraordinary degree of external indebtedness of Japanese companies, which would tend to sharply increase their risk rate and depress their expected rate of return, is actually merely accounting and fictitious, since for the purposes of the conglomerate, this debt relation is internal and allows for a high rate of short-term capital turnover that feeds a continuous and programmed expansion process.

In view of these theoretical backgrounds and the brief historical reference with a view to the experience of other countries and, in particular, the financial development cases presented in the study on Financial Intermediation, we will now examine the Brazilian situation. We will focus the analysis on the characteristics of the process of financial accumulation, concentration and centralization of capital in order to identify the main problems that arise for the maintenance of current growth trends.

The Brazilian case

1. Financial accumulation and its meaning in the current stage

As seen in the paragraph on recent trends, the issuance and accumulation of financial assets has been taking place in Brazil, mainly linked to the expansion of the public debt (ORTN), of consumer debt, of companies producing durable goods (bills of exchange) and real estate expansion (real estate bills).

Financial accumulation was maintained, therefore, until 1969/70, through an expansion of the public and private debt and based on a high rate of profitability and negotiability of short and medium-term financial assets, whose value was automatically indexed to inflation or offer an anticipated interest rate that extrapolates inflationary trends. This process has given rise to a sharp increase in the financial costs of companies and to growing needs for working capital that depress their rate of net profit and, consequently, their possibilities for internal accumulation.

The increase in corporate indebtedness has matched the pattern of economic growth since the 1967/68 recovery period, as cost increases have been absorbed by an expansion of sales from sizable margins of idle capacity[19]. However, as companies occupy this capacity and the pace of demand expansion continues with high rates of public and private indebtedness, the possibilities of sustaining a high rate of accumulation come to depend, more and more, on an increase in the investment rate of the private sector and, therefore, in the existence of adequate financing schemes for this purpose. These

19 Under conditions of direct labor costs stabilized at a significantly reduced level (approximately similar to the levels prevailing in the immediate post-war period).

financing schemes that would allow the internal accumulation of companies should be supported by external sources, especially if one takes into account that the reduced wage levels of workers would not allow a significant increase in the internal surplus rate, via an absolute reduction in wages, as occurred in the 1964/68 period.

Until now, the private financial sector has proved incapable of modifying credit modalities in order to substantially increase maturities and reduce interest rates. This is due to the structuring conditions of the financial market, as well as to the fact that its functioning takes place under inflationary conditions that tend to become institutionalized through the generalization of the use of various inflation-indexed systems. This circumstance raises the level at which the structure of interest rates is defined and, in conditions of broad system liquidity, as well as rapid rotation of financial capital, allow maintaining a very high rate of profit in the financial sector, thus accelerating the pace of accumulation and expansion of this sector.

Under these conditions, the creation of private financial institutions specialized in long-term credit is difficult - which is practically dependent on public development agencies - as well as the companies' own working capital financing is problematized.

Faced with this situation, the solution found for the financing problems of companies was the adoption of a policy of strong[20] fiscal and other incentives to investment in equities and IPOs[21].

From 1969 until now, the so-called capital market has become, thus, euphoric, through speculation carried out with existing equities, launching of new shares and, more recently, intensification of IPOs.

In the current conditions of ebullience in the capital market, the IPOs, launching and revaluation of equities are carried out according to accentuated fluctuations in the financial market and even in a parallel market to the Stock Exchange, with the prevalence of the speculative character of financial operations. This has two important consequences: one, on the development and stability of the capital market; the other, on the companies' financing structure, both closely related and expressing the main limitations of the adopted solution.

The first is related to one of the conditions required for the stability of the process of financial accumulation, which is to maintain a rate of return on equities capable of ensuring a balanced long-term growth.

20 For an idea of the modalities and importance of the stimuli used, see Avaliação Crítica dos Incentivos no Mercado de Capitais, publicação IBMEC — Bolsa de Valores do Rio de Janeiro.

21 It should be noted, however, that this procedure for opening the capital of companies is not necessarily aimed at financing the real investment of companies, but it has allowed, for those that do open up, to markedly changes in their indebtedness structure.

In this sense, financial institutions, when operating in open competition for resources and investments, force an increase in bond yields; and, on the other hand, as intermediaries between the primary and secondary securities markets, they arbitrarily raise the value of primary bonds, through already markedly speculative launches[22], which will feed, on the basis of expectations, a sequence of artificial revaluations in the secondary market.

Therefore, the structure and behavior of the capital market is markedly unstable, incapable of guaranteeing a process of financial accumulation that is adequate for sustained long-term growth[23].

The second aspect is related to the way in which the capital of productive companies has been opened, stimulated by the possibility of revaluing their assets, without tax burden and without control of investments, which allows them to raise extremely cheap financial resources, vis-à-vis the high financial costs of credit. The extraordinary valuation of shares allows the internal accumulation capacity of a growing number of companies to become increasingly dependent on new stock dillutions that undeniably reduce the cost of their working capital but imply increasing risk rates, given the commitments to pay dividends, which accumulate and differ over time.

On the other hand, since the market value of shares is completely disconnected from the real replacement cost of fixed assets or the internal rate of return on real investment, there is no possible articulation for economic calculation purposes between real and financial expansion. Apparently, there seems to be a strong accumulation of fictitious (accounting) capital on the part of publicly traded companies with no counterpart in the equivalent expansion of their productive capacity. This jeopardizes the companies' long-term rate of profit and therefore their ability to pay dividends. In other words, it completely increases the uncertainty over the realization of the value of financial capital as a property right over company profits.

The Contradictory Character of the Process

The contradictory character between real and financial expansion is manifested in the impossibility of maintaining a real basis for financial accumulation. The latter, as it has been done, assumes a continuous expansion

22 The founder gain, a component of the speculative profit, is greater the greater the difference between the share issue value and its launch price. Under current market conditions, this difference can exceed 100% of the share's par value.

23 Another indication of the possible instability of the recent process of financial accumulation is the extremely high price-earnings ratios of most stocks traded on the stock exchange, which demonstrate the strongly speculative nature of financial operations based more on expectations of (fictitious) capital appreciation than on rate of return implicit in this ratio.

of the short and medium-term debt of companies and families, as well as of the public debt. However, it is difficult to imagine that public debt and consumer´s debt could continue to expand at a rate remotely comparable to the 1966/70 period, given the proportions already reached by its gross volume and taking into account the terms and costs of the service of debt[24]. The normal trend would be for the growth rates of these two debt modalities to approach, respectively, the growth of gross domestic income and household disposable income, not continuing, therefore, to play a significant role as autonomous components of the internal demand expansion. In this case, the alternative for maintaining the economy's dynamism, in the long run, would lie in an acceleration of investment in fixed capital.

However, this alternative is held back due to microeconomic profitability criteria that affect both the decisions of savers (personal or institutional) and the investment decisions of companies.

Partly due to the speculative movement, financial investments continue to be the most profitable for savers. Furthermore, the high degree of negotiability and liquidity of the securities facilitates the transfer of surpluses between companies and across sectors, which continues to benefit accumulation in the financial sector. As a consequence, there is a rigidity of the financial cost structure that will increasingly weight on the real rate of profit of productive activities.

The existing indications on the profit rates of the 615 largest Brazilian companies seem to confirm this hypothesis, as the difference between the average rate of profitability of the financial sector and that of productive sectors is enormous. Thus, while state and investment banks present in their 1970 balance sheets net profit rates above 50%, and the other financial institutions, rates above 30%, the average profitability for the group of companies in the sample is of only 11.5%, with some sectors, such as chemical, pharmaceutical and plastic, showing negative rates[25].

This speculative expansion process maintains a permanent inflationary tension and violently distorts the allocation of private sector resources, favoring, above all, activities related to consumption diversification, and thus sterilizing, from a macroeconomic point of view, growing volumes of savings, in a veritable vicious circle of unproductive accumulation.

Likewise, from the perspective of investment decisions, in addition to the fact that the structure of profit rates cumulatively favors the financial sector, the form of indebtedness used by companies, as noted above, has increased

24 In 1970, the balances of ORTN (main public debt financing instruments) reached an amount equivalent to the total amount of currency in circulation and that year's issuances have practically exceeded the redemption value of bonds issued by the Treasury in recent years.

25 See, in this regard, Anuário BANAS — Brasil Financeiro, 1970.

the risk rate for long-term investments, which depresses the expected rate of return per unit of real investment.

In summary, the problem of structural instability in this process of financial expansion is not just the divergence of accumulation rhythms between real and financial assets, but the recurrent character of the ongoing process, which tends to a continuous redistribution of the surplus in favor of the financial orbit. If this is kept beyond its real basis, the structural instability could bring about a critical break in economic expansion. There seems to be a certain consensus that in order to avoid this rupture, speculation needs to be reduced, forcing a greater centralization of financial capital, through which the large financial institutions control IPOs, intervene in a coordinated manner in the manipulation of financial operations and promote the channeling of resources to sectors with the greatest investment opportunities.

The achievement of these measures would obviously mean a greater integration between the real and financial spheres, which would allow the conversion of financial capital into "productive" capital adequate to an acceleration of the real rate of savings-investment. However, this very convenient integration does not depend only on the centralization of capital, but also on a profound reorganization of the existing oligopolistic structure, as well as on a marked modification of the economy's recent growth style.

2. Concentration and centralization of capital; possibility of articulation of a new integrated oligopolistic structure

It seems realistic to take as a starting point the hypothesis that a growth model that concentrates income and capital is under way, and that economic policy attempts will be oriented, as until now, more towards ordering and rationalizing this global process of oligopolistic re-concentration and accumulation than to promote a redistribution of income and economic power.

At the outset, it is important to make it clear that a process of concentration can advance on certain levels without increasing absolute concentration. The increase in relative concentration is theoretically compatible with an increase in the absolute levels of income of the low- and middle-income classes, just as it is with the expansion of production levels and the number of small and medium-sized enterprises; what would happen in this case would be a decrease in their relative participation over increases in product, income and productivity. That is, the market would expand proportionally in favor of large companies and higher income strata.

With regard to the concentration of income and the expansion of the consumer market, the few existing indications are that, around 1970, the average levels of income and consumption of the salaried classes were below the levels that prevailed at the beginning of the past decade[26], with a sharp loss of position for the lowest-income groups. On the other hand, the consumption levels of the upper classes and the upper sectors of the middle groups probably expanded and sharply diversified, in the case of the latter, due to the rise in their incomes and to an accelerated expansion of their indebtedness.

With regard to the concentration of production and capital, there is evidence that during the 1960s there was a strong process of relative concentration of urban activity, which would have been accentuated with the economic crises of the middle of the decade. More recently, after 1968, a strong centralization of capital in the financial orbit began to be observed[27].

The two processes were not symmetrical, having developed until now with different dynamics. In the same way, there has been no defined articulation between the action of the main financial groups, until recently mostly national, and the action of the largest industrial companies, of the most dynamic branches, predominantly foreign. Except in the case of some international consortia where there are clear associations of industrial, agricultural, commercial and financial interests, the conglomeration seems to be more an object of discussion or projection than a general trend already defined.

The countless mergers of financial groups that have been taking place in recent years have not been articulated with the process of concentration in the real sphere. In fact, they only represent an acute process of centralization of financial capital, mainly due to the highly competitive and speculative nature of the financial market, from the expansion and excessive diversification of financial agents verified in the period 1966-1968[28].

In this way, a markedly asymmetrical oligopolistic structure is being set up, with regard to the relationship of power and articulation between the real and financial orbits. On the one hand, large companies, mostly foreign, solidly established in the market, have a high degree of self-financing, with no visible dependence on private financial power. Nevertheless, they are the favorite customers for the financial sector. At the same time, there is a wide range of companies whose financial and business power is relatively fragile, and which

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26 See growth data on popular consumer goods industries and family budgets for the decade, by Fundação Getúlio Vargas — Conjuntura Econômica, Retrospectiva da Década, February 1971.

27 For data on industrial concentration, see Fernando Fajnzylber, Sistema industrial y exportación de manufacturas, ECLAC, 1970. For data on financial concentration, see BANAS, 1970, and Index, April, 1971.

28 Since 1968, the Government has tried to avoid the proliferation of financial institutions with minimal scales of operation and competing at the margin for resources and applications. This was aimed more at preventing fraudulent bankruptcies and regularizing the market than at lowering financial costs (as many assumed), since the prices of financial services in an oligopolistic market are determined by the dominant firms and not by the marginal ones, although they do influence in the differential rates of profit of the entire oligopolistic structure.

are therefore heavily dependent on external sources of funds. Despite this, they have not had real possibilities to expand and modernize with the solid support of the large financial groups.

On the other hand, large companies seem very unwilling to go public in a way that would lead them to lose control to financial groups that are not their “natural allies” (although such a scheme would effectively point to the so-called conglomerate). On the other hand, the opening of capital of the weakest companies, and their association with financial groups, only seems to take place under “favorable” conditions while the speculative movement persists. Even in this case, there are doubts about its possibilities of transitioning to a significantly higher scale of operations and efficiency, as one thing is that financial groups are interested in their underwriting operations, with high IPOs commissions, quite another thing is if they are willing to partner closely with them in a joint policy of business reorganization and resource allocation. Thus, with regard to medium and small companies, the concentration process tends to be irregular and advances more through breaks and disappearances in depressive phases than through re-concentration and general increase in the scale of production and efficiency in peak periods.

Paradoxically, in the public companies sector, the process of expansion and concentration is more stable and structured, precisely because the problem of asymmetry between business and financial power, or between real investment and financial accumulation does not arise with the same force.

Therefore, with regard to the process of accumulation and concentration of the private sector, Brazil still seems to lack two basic conditions for the centralization of capital that are present in most developed countries today.

The first condition would correspond to a more effective control of the financial market by powerful public financial agencies (Mexico, France, Italy and Japan), which not only avoided financial speculation but also more effectively controlled the intersectoral transfer of financial resources and the allocation of real resources. The second concerns a more organic articulation between financial groups and industrial companies (of the Japanese or German conglomerate type), or, at least, a greater balance of forces between the oligopolistic financial and productive structure (US).

These two aspects of centralization are relevant to simultaneously solve the problems of financial stability and the orientation of accumulation.

Thus, for example, the problem of financial stability cannot be adequately resolved as long as the financial authorities behave, above all, as monetary and supervisory authorities, that is, with their effective control power basically limited to the expansion of means of payment and general banking credit and without greater operational capacity in the capital market. The regulation of the latter has been carried out through successive changes in the rules of the game and through the continuous and corrective issuance of instructions and regulations by the Central Bank. While it is true that a financial policy of this style allows for a greater dose of pragmatism and adaptation to contingent changes in the market, it is no less certain that it prevents a more rational macroeconomic orientation of financial accumulation, and tolerates the occurrence of strong speculative movements. In addition, mergers and associations of national and foreign financial and business groups take place according to merely contingent interests[29].

Here the other central problem arises: that of the articulation of the private productive and financial sectors, whose organizational capacity is much projected under the recent laws incentivizings capitalization, asset revaluation and mergers.

Given their privileged position in the capital market, it would be expected that investment banks would assume the central role in this more organic articulation between the real and financial orbit and, in particular, promote the financing of the productive expansion of companies.

However, until recently, the way in which investment banks operate was not markedly different from that of any common and current "financial company." The fact that legal instruments were placed at their disposal that would allow them to act more effectively as the main agencies of the capital market only moderately affected their way of operating in the securities market[30].

On the other hand, even in their task of launching shares through underwriting operations, they are guided much more by the speculative nature of the operation than by the long-term interests of the client companies. The very forms of articulation of interests, even when there are crossovers of

29 In the 1965 and 1966 discussions on the structuring of the capital market, several alternatives were suggested, one of which was the conversion of the BNDE into a sort of Central Bank of Investment Banks and of state and regional development agencies. There were already old precedents for the state's presence in the financial market, such as the Italian Furniture Institute and the Mexican National Financial Agency, but these solutions are not even considered. The solution proposed by the then president of the BNDE was to convert FINAME into a financial agency that would be for the Development Bank like the CFI for the World Bank. (Something similar was proposed and accepted in Colombia and later in Peru.) However, the Central Bank's liberalizing orientation of allowing the unstructured creation of a multiplicity of private financial entities prevailed, under which investment banks standed out. Basically, the BNDE continued to play the role of financing agency for long-term credit for both the public and private sectors in areas considered as priority.

30 The very statement by Roberto Campos, president of Investbanco, on "our investment banking mix" (Cadernos Halles, no. 5), recognizes that "investment banks, originally conceived in the sense of specialization of functions as investment agencies in long-term financing and support for business investments, actually work in the short and medium term and the only specialization that occurred was that of reserving financing for consumption and for financial institutions the financing of working capital" (our translation). In practice, this does not make much difference either as to the main form of credit instruments or as to the general function of the working capital of companies.

directors between banks and companies, or even shareholding, allowed by recent changes in the banking law, are governed more by financial considerations than by a global strategy of expansion of conglomerate or international consortium type.

Even in the case of the DELTEC group - whose financial head in Brazil is the BIB - despite its tradition as an international consortium, and its web of business interests (ranging from petrochemicals to cattle) passing through a whole range of participations in industrial and commercial activities within Brazil[31], its mode of operation is not even remotely structured in the same way as the Japanese conglomerate. This, as we have already seen, has its business organization as a "star" around a large bank, which, based on a practically unlimited issuing power in favor of the group companies, globally controls the financial accumulation and reproduction of the conglomerate capital, in addition to guiding the investment criteria, technology selection and market expansion.

In the case of international conglomerates operating in Brazil, integrated decisions regarding matters as relevant as those mentioned above are taken at their central offices, considering the global strategy of the conglomerate and its regionalization. In this way, the local investment bank tends to be just a financial agency with a certain degree of flexibility to articulate real and financial operations, whose dimension did not transcend the local scale. Its strategy is centered, above all, on the diversification of investments, aiming at reducing the global risk rate of the invested capital. It is true that as this capital represents only a percentage of the global investments of the international "conglomerate," its Brazilian branches can seek new investment opportunities with a greater risk level than domestic companies. That is, however, practically irrelevant when the policy of fiscal incentives and financial subsidies does not discriminate between national and foreign capitals, for the purpose of investments in priority areas for national development.

Much more limited in their orbit of applications are the national investment banks which, with few exceptions, are limited to strengthening the financial power of old commercial banks and operating in the securities market through a linked chain of financial, brokerage and securities distributors.

Thus, that articulation between financial and industrial capital that would allow something similar to an integrated process of accumulation in the "capitalistic" pole of the economy does not yet seem to be in process in Brazil.

The oligopolistic structure prior to 1963, which is the object of reorganization attempts, had characteristics of rigidity regarding the origin and interests of pre-existing groups, given their position in the internal productive structure

31 See Relatórios da DELTEC Internacional, 1969/70.

and vis-à-vis the international market, which has hindered a simultaneous re-articulation in the productive and financial orbit.

In fact, it is relatively easy to bring together a number of international financial groups from all backgrounds to participate in founding a large investment bank like INVESTBANCO, which is intended to operate in the open financial market, as an institutional financial investor[32]. But it is much more difficult to get these founding groups to agree to jointly deal with investment projects in areas where perhaps affiliate companies of large international consortia that compete with each other in the domestic or international market may already be dominant[33].

Thus, the possible articulations between financial capital and industrial capital appear so far limited to three types of areas, all related to the conquest of new markets, and not to the re-assignment of activities in preexisting markets. The first of them is the petrochemical branch, in which the União group (DELTEC — Rockefeller group) managed to cooperate with the state petrochemical company and to form an association with national minority groups. The second is the iron ore-steel complex, in which various international groups in association or division of labor with large state-owned companies are articulated with a view to exporting to the world market, and in which BNDE is the main financial agent. Finally, the third is the association of national and foreign capital, with a marked predominance of the latter, especially to explore the frontier of natural resources exploring the advantages granted by the tax incentive laws, basically for export purposes and in which more heterodox associations (from the point of view of the origin of the participating groups) are produced.

On the other hand, in the manufacturing sectors where branches of large integrated foreign companies predominate (electrical equipment, transport equipment and metal-mechanics), it is difficult to foresee a closer articulation between these companies and financial groups (sometimes rivals) that do not assume the strict control of those. IPOs that put the loss of equity control by the parent company at risk are not predictable.

In short, the concentration and centralization of capital in progress and foreseen for a reasonable period concerns capital associations for the purposes of financial speculation or foreign associations and, only in special cases, to compete or re-divide the internal market for goods and services.

32 Especially in the recent conditions of the international market and with the excess of dollars existing in the European and Japanese markets.

33 The apparent failure of INVESTEXPORT, the special section of INVESTBANK designed to promote a pool of export projects, is quite symptomatic.

It is true that the Government has revealed its clear intention, with regard to national companies, to help their merger or centralization under the sponsorship of a bank, in order to increase their competitive power vis-à-vis foreign capital. Hence the recent discussion at the Congress of Banks in Brasília on the form of association (holding or financial corporation) and on who would play the leading role of the group - commercial or investment banks[34].

Financial Capitalism and Dependent "Internationalization"

Finally, it could be emphasized that the there is only a superficial similarity between the phenomena of financial accumulation, concentration and centralization of capital going on in Brazil with historical processes in developed capitalist economies. To attribute a deeper meaning to this similarity would be to forget the unequal nature of the concentration observed in Brazil, as well as the heterogeneity of the various business and financial groups regarding the origin and objective interests of their capital and the degree of internal monopoly power. We would also be forgetting that financial capitalism represented for the Core countries a more advanced stage in the development of internal productive forces in their monopoly expansion on a world scale, while in the Brazilian case it only corresponds to an attempt to readaptation of the internal oligopolistic structure to the new rules of the international financial economic game.

In this readaptation, a process is configured whose character supposes the establishment of a new articulation scheme between public and private, national and foreign companies, in which international financial capital plays a decisive role, and which corresponds to a new form of insertion of key sectors of the Brazilian economy in a distinct framework of dependency relations. The dominant characteristics of these new relations are given by the dynamics of competition between the large international monopoly companies, in a world

34 The arguments of the national banking sector would be in favor of the first form under the allegation that investment banks have greater foreign participation. In fact, almost all the big commercial banks are linked to the 30 existing investment banks, of which, although only 10 have ostensible links with foreign groups, only two of the strongest appear to be exclusively domestic. The problem is, once again, that the entire financial sector finds itself in an accelerated expansion and re-concentration, in which it is difficult to prevent the penetration of foreign capital, especially with the avalanche of short and medium-term capital that has entered the country in recent years. In addition, the strong IPO process of national companies, accompanied by the growing participation of financial institutions in stock exchange operations, will probably lead to a loss of equity control by smaller companies, even though what truly interests them is not guaranteed, that is, a form of conglomeration in which the controlling bank has unlimited issuing power in its favor. This would make it possible to convert external indebtedness into intergroup debt, which would reduce the risk rate for the integrated accumulation process of affiliated companies.

market that is also in re-articulation[35]. The competitive eagerness to conquer new markets, the need to control and schedule the introduction of technical progress in a process of capital accumulation on a world scale, have led to the emergence of new forms of business organization in conglomerates that often acquire "multinational" character.

The merger of interests of industrial, financial and commercial groups of different origins that is now taking place in Brazil, and which allows for greater internationalization of the "Brazilian" productive enterprise through new forms of association promoted by finance capital, corresponds to a rearrangement of the internal oligopolistic structure to better adapt to the new rules of the international economic game.

In this sense, the fundamental character of financial capitalism in rapid expansion in Brazil acquires, from the start, a different functionality from the old German "financial capital" or from the vertiginous growth of the American financial accumulation of the beginning of the 20th century, although it bears a certain similarity with this one due to its speculative character. Much greater is the difference in relation to the Japanese post-war "model," in terms of the structure and direction of growth, and of the autonomous character of accumulation and centralization of capital and, finally, the hegemonic role of a national bourgeoisie and state. We will return to this problem in the final notes to clarify in more detail the main differences that can be observed between the Japanese and Brazilian models.

III. Notes for a discussion on the Brazilian model of development

In recent discussions about the current stage of accelerated growth of the Brazilian economy there have been successive references to possible similarities with the Japanese post-war development model.

It seems to us that an analysis, even a summary one, of the presumed similarities would highlight the weakness of this hypothesis, while at the same time allowing for clarification of certain aspects of the recent Brazilian experience.

The similarities most frequently alluded to refer to the recent high rate of growth, the low cost of labor, the highly concentrated distribution of income, and the centralized style of state intervention.

We believe that the scarce significance of these similarities can be highlighted by focusing the argument on the main characteristics of the structure

35 In this regard, see the special chapter on "Empresas Internacionais", Estúdio económico de América Latina, 1970, ECLAC, and El nuevo esquema centroperiferia, by Anibal Pinto and J. Knackal, Santiago, 1971.

and dynamics of growth in both countries, as well as the degree of organization and nature of economic power.

Japan has been growing, sustainably and at very high rates since the post-war period, based on the highest internal coefficient of savings and investment in the capitalist world (around 30% of GDP)[36]. Brazil managed to reach its historic growth rate (around 6%) in the 1960s, only due to the acceleration verified at the end of the decade, from a more intense use of idle productive capacity. The domestic savings rate (16%) remained, however, relatively low, while the investment rate rose slightly thanks to a strong share of state investments and a substantial increase in the net inflow of foreign capital.

Japan's conquest of foreign markets was brought about by a business power that developed under remarkably harmonious industrial, technological and foreign trade protection policies. From this internal base, the main industrial groups were able to launch themselves in the conquest of the world market with an economic and technological aggressiveness unparalleled in the post-war period. Brazil's external opening is taking place in the "gaps" of a world market undergoing restructuring, subject to acute international competition.

The main foreign groups installed in the country have taken advantage of the possibilities of cheap exploitation of natural resources and labor, as well as the huge subsidies and tax exemptions for exports, and the protection of an internal market that allows them to use second-order technology. Likewise, the growing regional division of labor between the main foreign affiliates operating in Latin America has acquired relevance in this scheme[37].

Despite the external opening, Japan maintained its fundamental expansion impulse through a vigorous development of the productive forces aimed at the internal market. The sector driving development is that of production goods, whose share in the industrial structure reached in 1961 more than 60% of the added value of the manufacturing industry[38]. This also allowed it to obtain important growth rates in the consumer goods industry, both durable and non-durable, in addition to a high rate of investment.

36 See, for these and other data on Japanese economic structure, Structural Changes in Japan's Economic Development, Miyohei Shimohara, ed. from the Institute of Economic Research, Hitotsubashi University.

37 See Fernando Fajnzylber, "Estúdio de algunos aspectos básicos para la formulación de una estratégia de exportaciones de produtos manufacturados en Brasil", ECLAC/IPEA, nov., 1969. See also Carlos Von Doellinger, "Exportações Brasileiras: Diagnósticos e Perspectivas", Revista do IPEA, No. 1, June 1971. With regard to the aforementioned similarity of low labor costs in Japan and Brazil, see data on wages in the manufacturing industry in several countries (Chart 15, p. 130), which show that in 1967, average hourly wages in Brazil were 30% lower than in Japan.

38 In Japan, the production goods sector, which comprises the chemical, metallurgy and machinery sectors, accounts for more than 60% of the industrial product. The machinery sector alone is responsible for 30% of the industrial sector's product. In Brazil, the aggregate value of the chemical, metallurgy and machinery branches, together, did not exceed, in 1967, 30% of the total industrial added value, and the added value of the machinery branch, including electrical equipment, was around 10% of total.

In Brazil, the impulse for recovery was based on an unbalanced industrial expansion, in which the durable goods and construction sectors were the "high-end" sectors, without their high growth rates being generalized to other sectors, in particular those of non-durable consumer goods. The acceleration of growth induced a moderate expansion in the sectors producing capital goods, which, however, did not experience substantial changes in their production structure, organizational level and technological advancement[39].

With regard to income distribution, both countries have a very high concentration both in personal and functional terms (low participation of wages in the added value), circumstances that reflect the existence of cheap labor and a high concentration of property rents. However, this similarity hides profoundly different movements and transformations. First of all, the Japanese economy has exhibited a vigorous rate of incorporation of labor into the manufacturing industry, resulting in a rapid change in the structure of occupation in recent decades[40]. In Brazil, the pace of industrial labor absorption has been relatively low in the last two decades (below the population growth rate) and the weight of structural unemployment and underemployment in agriculture remains immense.

Another contrast stems from the extremely high rates of urban productivity growth in Japan which, despite the considerable increase in employment, allowed for a continuous rise in real wages for low-income categories[41]. In Brazil, high rates of productivity growth were sporadic and concentrated in certain industrial sectors, while real levels of minimum and average wages in manufacturing industry dropped considerably between 1963 and 1968[42]. Finally, it is worth noting that the strong concentration of income corresponds, in the Japanese case, to a very high propensity to save, while in Brazil the middle and upper classes' high propensity to consume stands out.

These basic characteristics of the mode of income generation and distribution summarize the different implications for the structure and pace of

39 For an assessment of modernization problems in technologically backward sectors, see IPEA's "Estado de Máquinas Ferramentas" and "Diagnóstico de Indústrias Tradicionais."

40 Japan's employment structure changed from a participation in agriculture of 44.5% in 1954 to 29.1% in 1963, and in industry, from 21.9% to 30.5% in the same period. In Brazil, the population employed in agriculture dropped from 59.9% in 1950 to 53.7% in 1960, and in industry, from 13.7% to 13.1% in the same period. See "Proyecciones regionales y sectoriales: Application to the Brazilian economy," ECLAC, May, 1971.

41 See Developing Economics, "Income Distribution in Japan," vol. V, June, 1967, No. 2. In fact, the increase in income concentration between 1956 and 1962 was mainly due to a strong concentration of property income (the 10th decile held 71% of property income in 1962 compared to 48% in 1956) than labor income. These grew strongly in all deciles, despite practically the same degree of inequality. From 1962 onwards, there was a trend towards a reduction in the degree of inequality in the distribution of all incomes, wages, properties and families in general.

42 See Estudo Econômico da América Latina, 1969, ECLAC.

growth of forms of concentration that are only apparently similar. In the Japanese case, concentration leads to increases in savings-investment and a self-sustained pace of economic growth with an increase in the living standards of the popular masses. In the Brazilian case, it leads to a "consumerism" restricted to certain sectors of the population, with maintenance of subhuman living standards for the majority of the rural population and a sometimes negative growth in the average consumption of the urban masses.

As there does not seem to be any prospect of a redistributive policy in favor of marginalized sectors and since the dynamics of expansion and accumulation is not based on accelerating the consumption of the popular classes, but on the deepening and diversification of consumption by the upper classes and in the indebtedness of the middle strata, this stage of accumulation based on "consumerism" could be of short duration. Hence the continuous efforts to external opening and to seek new investment opportunities that are independent of the self-sustained expansion of the pre-existing consumer market.

An attempt to pave the way for a new stage of accumulation is being made with support for the modernization of backward sectors of the manufacturing industry and the spatial expansion of the economic frontier. Both movements represent an investment orientation promoted by state action, towards greater internationalization of the economy. The results obtained in these undertakings, heavily subsidized by the State, were intended, basically, to generate surpluses for the international market.

The first line would therefore be carried out by the modernization of the textile, food, clothing and footwear industries and by the re-equipment of small and medium-sized enterprises. In all cases, it would be a question of raising the efficiency standards of the backward sectors, with a view to increasing their competitiveness, and in search of a certain homogenization of the industrial structure[43].

Here, once again, the difference with the Japanese policy is striking. Japan deliberately maintains a dual industrial structure, supported by dual technological and financial structures, with which it manages to maintain the high rates of labor absorption required by the structural transformation of its labor market. This dualism did not imply, however, a technological freeze, did not prevent the sector of small and medium-sized companies from growing in parallel, nor did it lead to an increase in productivity gaps.

Indeed, Japanese small and medium-sized companies are expanding and modernizing thanks to the purchase of used machinery (at naturally low prices) from large companies. This allowed the industrial sector, as a whole,

43 For this purpose, several special funds were created in BNDE, whose resources will be made available to the private sector for expansion and modernization projects, with low interest rates and long financing terms.

to increase the durationof real depreciation of capital, without implying progressive obsolescence, on the contrary, ensuring that the accelerated pace of modernization of larger companies was carried out at lower costs and transmitted in waves to the smaller firms.

Another mechanism for linking small and medium-sized companies with large ones lies in the progressive increase in subcontracting, which, in many cases, resulted in the establishment of parent company-subsidiary relations. This capacity for association between two productive structures through dual forms of organization, and with the gradual but continuous introduction of the most advanced technology, enabled Japan to have the highest production rates in the capitalist world. Thus, the initial structural disadvantage that resided in a profound "factorial imbalance" between human and natural resources was converted into an advantage.

In Brazil, an attempt to modernize small and medium enterprises or backward industrial sectors, after years of technological stagnation, will inevitably lead to an increase in absolute concentration, with the destruction of companies, capital and employment. Even when these consequences are accepted by the economic policy as the "price" of efficiency, it remains to be seen whether this modernization will be profitable and achievable, in particular if the demand conditions verified so far in the case of most traditional products are maintained. In any circumstance, and to compensate the destruction of productive capacity, income and employment in macroeconomic terms, , it would be necessary for the modernization process to take place within a movement of general reorganization of the manufacturing industry, through a close association and a clear division of the labor between large and small companies in the same field or complementary fields.

This would require a multi-sector form of organization of companies, of the Japanese conglomerate type, already mentioned, or, in its absence, a powerful public intervention with a harmonious policy of employment, financing, technology and business assistance.

The second line of advance would be the opening of new investment opportunities on the economic frontier, through the support of powerful state investments in infrastructure and the granting of fiscal incentives that represent a strong capital subsidy, in an effort to generalize the incentive scheme used in the Northeast to almost all new areas.

Given the high capital intensity and long-term maturity of this project, it would be essential to ensure a long-term financing scheme, which has been achieved through fiscal means and external loans. Assured profitability for investments, through very high subsidies to capital and, in the case of diversified raw materials, given the existence of important foreign markets to which

Brazil is a marginal exporter, this seems to be a range of investments that, despite its low output-initial capital ratio, can guarantee high rates of profit and capital accumulation capable of sustaining a reasonable rate of growth for a relatively long period. Evidently, in a sense that means to reintroduce in the Brazilian economy a dynamism of the primary-exporting model type that, although does not self-promote industrial and urban development, can serve as a support by transferring surpluses and import capacity. The problem is to know how these surpluses will be captured and applied to guarantee an urban dynamism which, in turn, is already finding it difficult to apply its own accumulation potential in productive investments.

Here, once again, there is a glaring difference with the Japanese model. The organization of Japanese economic power depends on a long-established tradition of articulation between the different layers of the rural, commercial, industrial and financial bourgeoisie.

In this context, the Japanese State has always played the role of solidarizing the interests at stake and promoting a constant overcoming of contradictions between different social groups through what they consider a legitimate authoritarian and integrative system. This is what allowed, as we have seen, the most heterodox forms of business organization in the capitalist world; the "excessive competition" between equals (the powerful Keiretsu) instead of the liquidation of the unequals; the principle of a financial policy of equal treatment to large financial groups combined with a policy of subsidy and protection for the weakest and most backward groups. These historical and structural conditions allowed an organic solidarity of interests between the big and the small bourgeoisie and the National State rarely observed in such long periods in any country. There seems to be no doubt that such conditions have not existed in Brazil.

Given the current organizational conditions of national and international private groups, the Brazilian State has managed to promote its temporary solidarity, given the conditions of the internal and external markets, through important concessions in terms of fiscal treatment and financial facilities, from which all large companies, domestic and foreign, productive and financial, have benefited.

The fundamental question is to know what kind of re-articulation, on a permanent basis, can be carried out between large and small domestic and foreign productive companies and large national and foreign financial groups. Furthermore, what degree of control and organization would the Brazilian state apparatus need in order to maintain and guide the current concentrating model? The emergence of a stage of financial capitalism, such as the one we tried to characterize throughout the previous chapters, helped to make the interests at stake fluid and compatible, but it does not seem to be able to solve any of the great orders of problems mentioned. It does seem to favor a greater "openness" towards the internationalization of certain sectors that were until recently dominantly national, or aimed at the domestic market[44]. In the current conditions of dependent development, and with the model's concentrating character maintained, it is difficult for the Brazilian State to assert in "national" terms a hegemony that arbitrates the great interests at stake. Solidarity between the interests of national capital and the internationalization of the economy would seem to demand in Brazil a sui generis model of state capitalism in close alliance with the various international groups.

Their competitive nature and the economic crisis situation may give, for some time, the impression that state capitalism would be hegemonic in negotiations to open up new investment opportunities. The form of organization of large-scale production and the control of foreign markets, however, continue to depend on decisions outside the control of the Brazilian State. In this way, the dynamism (and duration) of the external opening will remain problematic, as long as a new scheme for the international division of labor is not clearly defined, as well as the corresponding adaptation of the internal structure of the economy in terms of distribution of production, income and economic power.

44 This greater openness is essential even as the only possible form of remuneration for the strong inflow of capital in recent years, a good part of which (the so-called "risk capital") is, in fact, speculative financial capital - and by virtue of which the Brazil's short-term debt has risen by U$1,700 million over the past three years against the accumulation of international reserves of U$1,200 million.

CHAPTER 5

NOTES ON THE RECENT INDUSTRIALIZATION PROCESS IN BRAZIL

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Structural conditions of dynamic imbalance

Our general hypothesis for explaining the cyclical character of the Brazilian GDP growth, from the second half of the 1950s onwards, is that this character is inherent to the unbalanced nature of the industrial growth structure.

This general hypothesis unfolds into two others, namely:

1. a heavy industrialization in underdevelopment conditions leads to great instability in the growth rates of the leading industries – durable consumer goods and capital goods –, whose accelerated growth rates cannot be selfsustained for a long time, due to their limited relative weight in the composition of expenditure and in global industrial production;
2. the sharp instability in the balance of payments and the acceleration of inflation that characterize the end of the relatively short periods of expansion, rather than determining the internal crisis, are a manifestation of the exhaustion of the expansionary phase. In other words, the endogenous mechanisms of expansion and dynamic feedback are exhausted, inflationary tensions are aggravated, and the problems of payment of internal and external debt become more acute, and not the other way around, as is common in certain interpretations of the type **external limits of growth** or **credit crunch**. In support of this second hypothesis, it is worth remembering that although the instability in the current account of the balance of payments become more acute in the periods of acceleration of investments, when the demand for imported capital goods increases, there were never any limitations on the part of external suppliers of equipment. Even when the purchasing power of exports was stagnant or declining,

risk capital and the provision of **suppliers´ credit** always reinforced the import capacity, if the economy was growing rapidly.

Heavy industrialization, under the leadership of the durable consumer goods and capital goods industries (in particular the transport equipment and electrical equipment industries), is unable to sustain itself for an extended period. Although the leadership of these industries determine the logic of industrial accumulation and has powerful dynamic effects on the economy – derived from the construction and accelerated expansion of productive capacity –, it also has, however, a reduced effect on the current production of the preexisting industrial structure. To explain better, once these two industries are built (1959/60), or after a period of acceleration of their investment rate (1970/73), the capacity to replenish inter-industrial demand ceases. At this moment, the absolute weight of non-durable consumer goods industries, with their markets outside the manufacturing industry, reappears as the main component of current demand in the manufacturing industry.

Its capacity to grow, nevertheless, depends on the employment growth rate and the wage rate, that is, on the rate of urban accumulation, and therefore it is incapable of maintaining by itself the peak of the cycle.

For greater clarity of the argument, we can resort to the final use categories (capital goods, durable consumer goods, and non-durable consumer goods), assuming that inputs have an expansion logic articulated with each of these **final demand** subindustries.

Let us start with the capital goods and heavy inputs industries of widespread use (mechanics, metallurgy, and construction materials). Their current growth and accumulation rate are determined not only by the economy's general accumulation rate but mainly by the manufacturing industry's own investment rate. The latter, in turn, depends on the articulation of the logic of inter-capitalist competition of large international companies in the metal-mechanical complex and on the capacity of the public sector to promote complementary investments, both in the orbit of large industrial public companies and in the sphere of conventional public investments in transport and energy. This logic corresponds to a same basic pattern since the Plano de Metas, only increasing the absolute weight and relative autonomy of the State and large international companies. The national heavy mechanics industry is dragged along by this movement, and its market is guaranteed by the orders placed on it, on the one hand by State-owned companies and, on the other, by international companies. In this sense, the great development of the capital goods industry, verified in the past decade, has occurred by the more than proportional expansion of the capital/capital goods subsector and not by the capital/

consumer goods subsector. The modernization and expansion of the productive capacity of the main non-durable consumer goods industries (textile and food) take place in leaps, after a period of acceleration of the accumulation rate, at the peak of the cycle, without having, however, important feedback effects on the expansion and modernization of the capital and consumption goods industries.

The demand for expansion and modernization of the productive capacity of this industrial branch leaks abroad in the form of imports of technologically more modern equipment, reflecting the standards of the international competition from producers of equipment for specific industries.[1] Paradoxically, the inverse occurs with the demand derived from capital goods of the large transport and electrical material producers, whose backward effects allowed for the **nationalization** of the supply of universal equipment and parts and pieces, reinforcing the industrial cycle in the expansion stage and driving it to the peak.

Thus, a hypothesis of mass underconsumption to explain the economic cycle of the production goods industry becomes fragile. We reaffirm once again that the cyclical nature of investment can only be understood considering the form of oligopolistic competition in the leading industries and in the performance of the State as a heavy producer and investor. More than that: under conditions of a delayed industrialization, however modern and internationalized it may be, the absolute and relative low weight of the capital goods industry (and not the fact that it is technologically **dependent**) prevents a self-sustained growth à la Tugan-Baranovsky, that is, it prevents the Brazilian miracle from having any resemblance to the so-called Japanese and German miracles.

The durable consumer goods industries are the industries par excellence in the dynamics of recent industrialization. Not only are they the ones who command the recovery of industrial growth, but they are also the ones who allow the acceleration of the accumulation rate at its peak. Although their relative weight in the manufacturing industry's current production is not very expressive, that is, it does not quantitatively **explain** the global growth rate of the manufacturing industry (Table 1), their peculiar insertion in the industrial structure determines an extremely accentuated cyclical elasticity of their backward and forward linkage effects. Their performance has a super-accelerating effect in the expansion stages, which is asymmetric in the deceleration stage. This is because, once a certain level of consumption is reached at each stage

1 The peaks of modernization of the textile and food industries took place in 1951/52, 1960/62, and 1971/73. In all these periods, the import of specific equipment for these industries grew more than the corresponding domestic production.

of expansion, it tends to be defended by the existing solidarity between the supply conditions of the manufacturing industry, the specialized financing mechanisms, and the interests of their core of privileged consumers.

This means that this industry, unlike the capital goods industry, does not require an **exogenous** demand, but has mechanisms capable of adapting its production conditions to those of long-term realization. This does not mean that it is possible to avoid the cycle, for which, on the contrary, this industry is very culpable, especially in the acceleration stage. In declining phases, its behavior is characteristic of a concentrated differentiated oligopoly, which, although managing to maintain an average level of capacity utilization corresponding to each level of production and consumption, gives way, in each expansion period, to the emergence of growing planned idle capacity. That is, overaccumulation is not only recurrent, but it tends to be amplified, leading to longer and longer relative stagnation periods. In addition, in the recessive stage, they are unable to avoid sharp fluctuations in their current demand, which result from a replacement demand that is extremely concentrated in time, since the expansion of the stock of durable goods takes place in leaps in each expansion period. All of this means that, after the construction stage, this industry loses the ability to lead, for longer and longer periods, the global industrial growth.

Table 1 – Participation of the selected sectors in product additions aggregate real Agriculture-Industry (in %)

Sectors	1965/73	1973/77	Mean 1965/77
Agribusiness	2.5	6.4	3.9
Industry	97.5	93.6	96.1
Manufacturing	80.2	61.3	73.2
Durable consumption	18.1	9.5	14.9
Capital	13.5	13.2	13.4
Non-durable consumption	33.2	21.8	29.0
Intermediary	15.4	16.8	15.9
Civil Construction	17.3	32.3	22.9
Total	100.0	100.0	100.0

Source: Werneck & Bonelli (n.d.).

Non-durable consumer goods industries continue to represent more than 40% of industrial production, if we consider their corresponding inputs, which means a considerable weight in **explaining** any growth rate. However, from the point of view of the dynamics of industrial expansion, they cannot be considered leading industries, both because their inter-industry linkage effects are particularly low on the production goods industries and because their ability to generate their own market, by direct employment and intra-sector linkage effects, is negligible. Their backward effects play mainly on agriculture (food and raw materials), for whose dynamism they are, in fact, an important component.

Unlike the durable consumer goods industry, which has a restricted market base, but a periodically accelerated expansion ensured by a concentrated distribution of personal income, these industries have a broad market base whose growth depends, however, on the pace of employment and increase in the wage rate, which only present marked dynamism at the peak of capital accumulation. It is exactly this that does not allow this industry to lead the growth of the economy, but, on the contrary, to be dragged along by it. As Kalecki rightly pointed out, the growth of workers' consumption depends on the growth of capitalist consumption and investment. This does not mean, however, that its long-term growth is compromised, given the rapid rates of urbanization and the fact that the widespread mass consumption of industrial goods is compatible with any type of labor market. Thus, it does not matter how segmented this labor market is and how small is directly productive employment, because even with a low purchasing power, the mass of consumers of industrial products of the large capitalist companies increases inexorably. Much more than the movement of industrial capital, the expansion of the markets of the wage-goods big industry increasingly depends on the movement of accumulation, expansion, and differentiation of urban mercantile capital; this, in turn, depends on its ability to be articulated with the State, at a local or regional level. In this sense, urbanization and industrialization do not correspond to the same movement, since the logic of industrialization is determined by the **heavy industrialization** that may or may not generate its own markets regardless of what happens with the mass market. This is the deep meaning of the fracture existing between the living conditions of the masses and their role as producers and consumers for a capitalist market in an underdeveloped country. In this sense, solving the problem of **industrial backwardness** in a **late capitalism** is not the same as solving the problems of underdevelopment and poverty.

The stages of the recent cycle

The recovery stage (1967/70)

The causes of the recovery of Brazilian manufacturing industry from 1967 onwards are well known and can be briefly summarized:

1. The fiscal and financial reform of 1966 improved the conditions for financing current public spending and traditional investments linked to civil construction.
2. The so-called "tariff truth", that is, the increase and restructuring of the prices of public utility services, combined with the negotiation of the external public debt, allowed for the launch of the electrical energy program, reviving the electric material industry, the big builders, and the engineering firms.
3. The operation of the institutional consumer credit system, coupled with the monetary correction instrument with advance discount on securities, revived the demand from the automobile industry and other durable goods with more widespread consumption.
4. The housing finance system revived and activated residential construction.
5. Export incentives allowed subsidies for textile, footwear, and machinery production, aiding recovery.
6. The wage policy, combined with the financing policy, favor the concentration of personal income, which induces the differentiated consumption of the upper-middle class, as well as the proliferation of personal services.

All these programs have a great impact on employment and on the growth of urban income, boosting current demand. Thus, the resumption of capital accumulation, in particular the growth of productive investment, is due to factors exogenous to the current functioning of the industrial system, which resumes a rapid growth rate long before the idle capacity generated by the investments of the previous period had been used.

Only after the consumption of durable goods, public investment, and construction (1965/67) increased, industrial linkages began to reactivate the demand from other branches of the manufacturing industry from 1967 onwards. The latter starts to lead the global growth of the GDP and reaches the levels of capacity utilization that induce an acceleration of the investment level from 1970 onwards (Table 2).

The acceleration of the growth of the civil construction, transport material and mechanics industries allow, by its linkage effects, to expand the employment rate and the global mass of urban wages (even without raising the average wage rate, which remained the same - with some fluctuations – until 1970). These sectors, along with the related growth of the service sector and the reactivation of commercial credit, are responsible for the recovery of the internal market of non-durable consumer goods industries, in particular the textile, clothing, and footwear ones, which, until 1967/68, even with export incentives, still had not recovered pre-crisis activity levels.

The repercussions on the growth of industrial production of inputs for widespread use and construction materials are also significant, as well as some important segments of the capital goods industry, whose growth rates, extremely unstable in 1965/67, definitively recover thenceforth, growing until 1971, albeit at a slower pace than the durable consumer goods industries.

The peak of the cycle (1970/73)

The period of resumption of accelerated growth in current industrial production ends up resulting in a sharp rise in the rate of capital accumulation in the manufacturing industry itself.

Table 2 – Manufacturing Industry Growth (in %)

Industry	1965/67	1967/70	1970/73		1974/77
I. Consumer goods	4.8	11.6		12.3	4.5
1. Durable goods	13.4	21.9	(1) (21.2)	25.5	5.5
1.1 Transport	13.1	23.9		24.5	–1.0
1.2 Electrical	13.9	17.4		28.0	16.0
2. Non-durable goods	3.6	9.7	(1) (13.3)	9.1	4.2
II. Production goods	9.1	13.7		15.7	8.6
1. Capital	4.5	13.7	(1) (39.0)	22.5	8.4
2. Intermediary	10.8	13.7	(1) (17.0)	13.2	8.7
Total	6.8	12.6	(1) (17.5)	14.0	6.6

Source: INPES, (1) FINEP.

In fact, from 1970/71 onwards, the idle capacity of the manufacturing industry, inherited from the previous stage and used in the recovery period, can be considered exhausted.

The survey carried out at FINEP indicates an acceleration in the accumulation rate from 1970 to 1973, which translates into rapid growth rates in the capital goods industry, accompanied, at a slightly lower pace, by imports of equipment.

In the 1971/73 period, the capital goods industries reach, together, an extraordinary average growth rate, in the order of 39% per year, which evidently invalidates the thesis that the increase in the imports of equipment meant a diversion of demand abroad. In fact, the demand for imports is above all complementary to the domestic supply. The rise of both is, above all, due to the very strong accumulation rate, at the end of the period, of the automobile industry (70% increase in fixed capital in 1973), the resumption and acceleration of the State steel program, and investments in telecommunications, fuels, and petrochemicals. The modernization and expansion of some non-durable consumer goods industries, especially the textile, publishing-printing, and chemical-pharmaceuticals ones, also contribute importantly, as well as the acceleration of the rate of capital accumulation in the heavy equipment industries, led by the large international companies. The structure and dynamics of the main industrial markets and the feedback derived from inter-capitalist competition lead some industrial branches to expand their capacity ahead of the pace of expansion of demand, to guarantee an increasing share of the rapidly expanding market to the leading companies. This is particularly the case in the automobile, electrical, and textile industries.

The 1974/77 slowdown

This investment effort, which brutally raises the rate of capital accumulation in 1970/73, would inevitably lead to a reversal of the cycle.

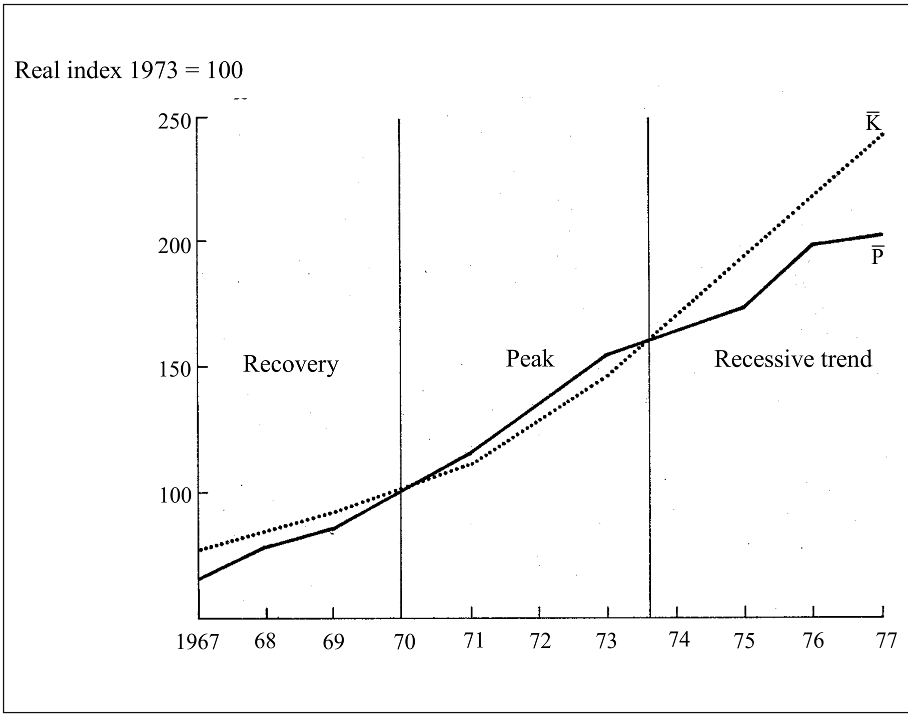
Between 1970 and 1973, the average capital-product ratio remained constant, which implied an acceleration of production growth compatible with the rate of expansion of the capital stock. To maintain the dynamic balance, both rates would have to keep the acceleration of the growth pace. The accumulation rate, however, had already reached, for the manufacturing industry as a whole, around 35% in 1973, which would imply, to maintain the same pace, doubling, in three years, the capacity of the manufacturing industry as a whole.

This cannot take place, but, with the expansion of productive capacity remaining high in the 1974/77 period, a tendency towards overaccumulation is created, which generates a dynamic gap between the productive capacity and the effective demand of the manufacturing industry.

As early as 1974, this becomes evident when, maintaining the pace of capital accumulation, industrial production slows down and a recessive trend begins to take place, with growing dynamic realization problems. Graph 1 shows the overaccumulation gap, as well as the recessive trends of the years 1975/77.

The problem of dynamic realization is extremely complicated to solve, since one does not expect that the current production of durable consumer goods and capital goods, which led industrial growth, can keep pace with the 1970/73 period. The acceleration in the production of durable consumer goods was such (Table 2) that the stocks of goods available to consumers more than quadrupled over a period of six years, and therefore one could not expect that their demand would remain stable. Thus, the growth of this type of goods goes through periods of accentuated fluctuation, with an average negative result for the automobile industry between 1974 and 1977, which would be inexorable regardless of the oil crisis.

Graph 1 – Evolution of production and capital stock of the Manufacturing Industry (Cr$ of 1973)



Maintaining the pace of growth in the capital goods industry is equally problematic. Its capacity was not yet fully utilized in 1973, as its capital/product ratio was still declining in the boom period, but current demand in the industry, coming from orders from the manufacturing industry itself and from state companies, was rising sharply. Perspectives are favorable for the industry to further accelerate its own accumulation rate, especially the national sector of the heavy mechanics industry that had delayed its response during the peak period of the cycle. From 1974, this industry received increasing investment subsidies and gigantic government projects that would guarantee orders for a long period. The transport material and electrical material industries, in turn, which had overaccumulated at the peak, presented a decrease in the rate of investment early in 1974.

Despite the strong growth in the capital accumulation rate, largely guaranteed by the public sector, the relative size of the capital goods industry is insufficient to, on its own, boost the joint demand for production goods and generate an employment expansion capable of ensuring a global pace of growth in industrial production and in productive capacity that remain in dynamic equilibrium. It is not by chance, therefore, that the greater the productive investment in heavy industry, the more widespread is idle capacity, that is, a productive potential much greater than the possibilities for dynamic realization.

However, the recessive trends in the non-durable consumer goods industries are the ones that appear first (Table 3), given that the wage mass does not grow at the same pace as production, both because the pace of growth in urban employment is lower than the rate of productive accumulation and because the average wage rate not only does not keep up with the growth of labor productivity, but also tends to decline in real terms with the inflationary acceleration that takes place at the peak. As the non-durable industry still has a very large relative dimension in industrial production, a sharp drop in its growth rate contributes to reduce the global growth rate of the manufacturing industry.

The government project, announced in the II PND, of maintaining the industrial growth by substituting imports of capital goods and heavy inputs is, therefore, self-defeating. First, because the decrease in imports of capital goods that occurred from 1975 was due less to the restrictions imposed by economic policy and much more to the successive drops in investment rates in the electrical material and communication, textile, food, transport material, and chemical industries. This reversal in investment levels derives, above all, from a drop in the expected rate of return on private investment considering the growth in the manufacturing industry's idle capacity. Secondly because, although public projects already underway were capable of sustaining accumulation rates in important industries of production goods, they were not, however, sufficient to maintain the current production growth rate of heavy industry and, much less, the demand from the rest of the manufacturing industry.

Thus, the hypothesis of strengthening national power or developing the productive forces, by the self-sustained growth of the department of production goods, implies a sui generis modality of State capitalism, since both its real productive base and its social support base are very narrow. The authoritarian National State project announced in 1974 not only does not have popular support, because it has nothing to do with it, but it only relies on, from the point of view of the ruling classes, a restricted sector of the big international capital (the cartelized industries of heavy equipment goods), a fraction of the national heavy mechanics, and the bloc of large engineering and construction firms. All other business sectors that the demand of heavy industry does not favor are excluded from the pact. Hence the cry against nationalization. On the sidelines of the industrial accumulation movement but benefiting from the large companies' non-reinvestable surpluses and taking advantage of the inflationary acceleration, caused by a strong inversion in price trends, the financial sector prospers, being greatly favored by the internal and external indebtedness.

Crisis trends

The endogenous reversal of the cycle does not manifest itself abruptly, as it occurred in the previous period. This is because State investment (companies and government) continued to grow in a sustained manner up to the present, thanks, on the one hand, to the current self-financing capacity of public companies and their own indebtedness capacity in the internal and external financial markets, and, on the other hand, to the federal government's fiscal autonomy, by the handling of special funds.

Despite repeated statements by the Minister of Finance, since 1975, in favor of the need to adjust the internal economic conditions to the new international situation, the effective suspension of investments clashes with the relative autonomy of the sector of state-owned companies combined with the solidary interests of the great international and national capital. On the other hand, despite the dramatic situation of the balance of payments in the current account, neither the inflow of risk capital nor the influx of suppliers' credits ceased, which allowed a growing official indebtedness to maintain the execution of projects of joint interest from the State and the great international capital. The only negotiations that were interrupted concerned industries in which competition from large international groups (mining and steel) is problematic. In the energy sector (electrical and atomic), in which the required imports of capital goods are higher, the projects did not suffer any rupture due to the lack of external credit.

The schedule for the execution of large projects, commanded by the public sector, are only submitted for discussion due to the difficulty of defining the participation of national entrepreneurs and the government's current disbursement scheme. It is evident that, if a fall in the overall level of public spending is superimposed to the recessive trends in current industrial activity in the durable and non-durable consumer goods industries, this will affect the employment rate and the performance of the capital goods sector.

The employment rate is essentially linked to the government's current and construction expenditures at the federal, state, and local levels. Civil construction, in addition to being responsible for maintaining the level of urban employment, despite the manufacturing industry's recessive trends, has become an increasingly important component in sustaining the global effective demand (Table 4). Given the extreme centralization of decisions to invest in metropolitan, sanitation, energy, and transport programs, any **stabilizing** initiative by the central government tends to be transmitted in chain and on a national scale, which would trigger an open recession, with catastrophic social and political effects.

Regarding the performance of the capital goods sector, the possibility of maintaining a high pace of current activity, for the gradual occupation of idle capacity margins, is mainly linked to the continuity of investment programs by large public industrial companies.

Table 4 – Participation of Civil Construction (CC) in Gross Fixed Capital Formation (GFCF) and Gross Domestic Product (GDP) (at 1970 prices)

Year	CC/GFCF	CC/GDP
1965	58.0	11.7
1966	54.0	11.5
1967	55.7	11.7
1968	52.5	11.6
1969	55.1	12.3
1970	52.2	11.6
1971	50.9	11.5
1972	47.8	11.2
1973	45.1	11.3
1974	43.3	11.6
1975	44.8	12.4
1976	46.1	12.8
1977	50.2	13.3

Source: Werneck & Bonelli (s.d.).

This brief description of the interlinked nature of public and private investment in heavy industry shows the inconsistency of the hypothesis that seeks to place the limits to growth on the external sector. Nevertheless, public investment should not be taken as a panacea capable of maintaining a high growth rate for the economy as a whole. Despite the strong share of public investment in total capital formation, the **actively** cyclical component of spending is private investment. Now, as previously emphasized, this, although moved by the laws of inter-capitalist competition, cannot sustain indefinitely the productive capacity growing ahead of the demand. Conventional public investment can, in fact, create additional effective demand; however, from the point of view of the state productive sector, thanks to the discontinuity and size of its investments, the creation of new productive capacity is strongly destabilizing. At its peak, it works as a superaccelerator, raising the desired rates of private investment in the production goods industry beyond what it is capable of sustaining in the medium term with its current demand. In other words, it would be necessary for the government's productive investment to accelerate indefinitely for the capital goods industry to sustain its current investment and production rates.

The reversal of the capital accumulation rate is, therefore, inexorable. Public investment, when properly programmed, can only hold a minimum level of economic growth. If, on the contrary, its destabilizing effects are accentuated, from the point of view of the maintenance of current demand, the economy will plunge into a sharply cyclical process in the short term, that is, of fluctuations around a tendency to relative stagnation. This, in turn, will aggravate the government's current funding problems, by sharp fluctuations in tax revenue, which is one of the classic stop-and-go mechanisms.

The acceleration of inflation and the mechanisms of financial speculation

The resurgence of inflation from the second half of 1973 on was basically determined by the correlation of domestic prices to international prices, in an upward movement. This affected, in a first stage, agricultural prices and, consequently, reinforced the mark-up mechanism of the main companies in the wage-goods industry, whose tendency to increase their relative prices was already evident in the expansion period, in contrast to the drop in margins in the durable consumer goods and capital goods industries. The second movement of exogenous price rise was given by the sharp rise in the prices of oil and other strategic raw materials.

This autonomous price shock occurs when current industrial production is already at a declining pace of growth, stimulating generalized over-pricing policies to defend the gross profit margin, against a falling sales pace. The working capital needs of the companies as a whole increase, therefore, in real terms, due to the detachment between the present value of their working capital and the volume of current profits that will only be realized, at the end of the production period, with the perspective of rising prices. Thus, under penalty of a stoppage in the pace of business, an expansion of commercial bank credit is imposed, which must be at least sufficient to keep up with the rise in prices and the growth in sales. In fact, the commercial credit circuit could not be invoked as the most important mechanism of inflationary feedback. On the contrary, the financial consequences of the public and private debt, both internal and external, have constituted a stronger and more perverse mechanism of mutual feedback between inflation and the accumulation of sterile debt and credit relations.

From 1974 on, the financial feedback mechanisms for inflation are, at the same time, **sterile** from the point of view of financing additional spending, in investment and consumption, and have become a self-accumulating drive of indebtedness for public and private companies and for consumers. This process forced companies and families to accept astonishing levels of indebtedness, causing a sharp rise in interest rates in current credit markets. In addition, it determined a growing financial burden on the net disposable income of all economic agents with little power to change their income, in particular wage earners, small and medium-sized private companies, and public utility companies (whose tariffs suffer a growing lag in relation to inflation).

In contrast, for large monopoly companies, including large public companies, the slowdown is offset by their market power, which allows them to maintain a high volume of current profits, however excessive in view of their productive investment expectations. Here, the articulation between their interests and those of the financial system is established, in favor of a movement of generalized speculation that quickly passes through fictitious patrimonial revaluation and ends up in sole financial speculation. The artifice of monetary correction[2], which made possible the creation of a specialized financial system, coupled with the big banks, finally reveals its perverse face, transforming itself into an overwhelming inflationary projection mechanism and a catapult of speculation.

The issuance of public debt bonds, in particular Treasury bills, was intended to create an open-market mechanism capable of regulating the liquidity of the economy. In particular, it was intended to regulate possible sudden fluctuations in the Treasury's cash positions resulting from destabilizing movements in external and internal debt. In reality, however, given the peculiar way in which the money and financial markets are intertwined, these bonds ended up becoming the main object of speculation.

The null risk and protection against inflation (by inflation indexing) make the bonds issued by the government a prime financial asset. As a result, these bonds serve as a guarantee for all very short-term operations (the so-called overnight). At the same time, the implicit remuneration rate of these bonds (discount plus monetary correction and interest) regulates the rate of return for financial investments in general and, consequently, the cost of money. This is why it is known as the market's prime rate.

2 The institution of inflation indexing for all financial assets in 1964 (note of the revisor).

The uncontrolled expansion of the external debt, on the other hand, has been working as a mechanism for strengthening and growing this short-term financial circuit. The pressing need to obtain new resources, to pay interest and amortize the principal of the external debt already contracted, requires the maintenance of very high internal interest rates, so that it becomes advantageous for international companies and Brazilian banks to take money in large volumes abroad. The growing influx of dollars, above immediate needs, forces the government to disburse *cruzeiros* to cover the surplus of foreign operations. To avoid the pure and simple issuance of paper money, the Central Bank sells government bonds (at an attractive discount), thus drying up the *cruzeiros* required to cover the surplus of those external operations. High interest rates are combined there with an expansion of the internal debt, whose bonds become even more attractive as a refuge for the idle resources of big companies and banks. (*Hic Rhodus, hic salta!*)

This speculative circuit, in addition to feeding on the interest rate differential, represents the most perverse mechanism of inflationary acceleration. This is because, when estimating the profitability of any financial investment, agents calculate a future inflation rate, generally higher than current inflation. Higher interest rates put pressure on business costs, which tend to transfer these pressures to prices. Therefore, inflation accelerates and, with that, in the next moment, the real liquidity requirements to maintain the volume of working capital and, thus, the level of productive activity, increase. But, given the resurgence of inflation, the government reacts by cutting credit and, instead of putting out the fire, ends up adding more fuel to it. This is because loss-making companies, hindered in their search for money, are forced to resort to the financial market, putting pressure on interest rates, whose level is already quite high. On the other hand, companies, and other entities with surpluses, in view of this, shift their balances to the speculative market. The government's attempt to contain credit is, therefore, nullified by the increase in the speed of very short-term financial circulation, carried out in the extrabank system.

This movement would, however, have a short life, were it not for the fact that the cancellation of the active and passive positions of the agents involved in speculation ends up putting pressure on the interbank market, forcing the banking system as a whole to demand an unexpected monetary expansion from the Central Bank, under penalty of widespread default. In this sense, the idea of an autonomous monetary base loses any meaning, and the endogenous money supply (means of payments created within the financial system) starts to regulate not only the volume of liquidity, but also its price.

In these circumstances, the monetary budget that should reflect the deficit or surplus situation of the various economic entities (companies, fiscal budget, balance of payments) ends up becoming a **black box**, where all kinds of pressures erupt. To put it better, companies, the government contract debts (internally and externally) and advance financial positions without the credit and debtor situations of these agents, contrary to what the followers of good logic might imagine, reflecting deficits or surpluses in real transactions. For a long time now, the growth of external debt, internal public debt, and corporate debt itself has ceased to be a clear indicator of the real need for resources and has become, on the contrary, a pure speculative manifestation of a strictly financial nature. Thus, it is no longer known what such a monetary budget means, except for the record of a hellish accounting game that, in fact, means nothing.

The failure of the government's monetary policy has its origins, on the one hand, in the expansion of external indebtedness – with its impact on the internal debt – and, on the other, in the self-expansion capacity that the financial circuit reveals to have. All of this is aggravated by the growing issuance of new bonds, necessary to meet the turnover of the internal debt, whose maturity terms have been shortened. The issuance of new bonds to cover the internal debt service (redemptions plus interest and inflation indexing) reaches around 33% of the accumulated global volume.

The dysfunctional character of the financial system ended up being translated into an absolutely distorted mechanism, which rewards speculation and penalizes productive investment, already depressed, whose economic calculation horizon disappears in the fog of **liquidity preference** sanctioned recurrently by monetary policy.

To get an idea of the complexity of the current crisis, we are obliged to emphasize the dissimilarities with the crisis of the early 1960s. This is not only to point out the order of magnitude of the economic and social problems underlying the crisis, but also to underline the State's greater degree of autonomy to face it.

Thus, the end-of-cycle situation is similar in only very general terms to the past, from the point of view of the problems of overaccumulation of capital and, therefore, of the dynamic realization of industrial productive potential. The underlying financial crisis is, however, much bigger now, but it has not yet erupted into widespread public or private insolvency. The growth of household indebtedness has reached unbelievable levels and the real purchasing power of the basic wage is lower now than in 1963, but the social crisis has not reached the streets. The sharp discontent of certain fractions of big capital is latent, but the power of command of the State is greater than before. In other words, neither the political problems of negotiating between State and the big national and international capital, nor the bargaining power of workers, nor the power to control and **manage** the colossal internal and external debt are anything like those of the 1963/64 crisis. More than that, the structural capacity of resistance to an orthodox stabilization policy, on the part of the large national construction, industrial, and financial companies, both from the private sector and from the public companies themselves, is now remarkable and beats the possible stabilizing interest of a fraction of the official international finance capital.[3] That is why the symptoms of the crisis that were already visible and threatening in 1974 could not be taken into account by the economic policy of the 1974/75 period, and the stop-and-go policy of the past three years has been administered with much more **delicacy** that in the 1963/65 period.

If, however, adequate escape valves are not found for all the accumulated problems, both in national and international terms, it is likely that the size of the crisis will end up reaching economic proportions greater than those of the first half of the 1960s, and that relative stagnation will reach a longer period to allow for the digestion of the large projects that have just been completed and the **devaluation** of the colossal external and internal debt.

3 The concerns of the IMF and the US Treasury do not now find the same echo as they did in 1963/64, given their visible impotence to control the international financial crisis and the Brazilian simultaneously dollar debtor and creditor strong position.

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CHAPTER 6

CRITICAL VIEW OF THE SECOND NATIONAL DEVELOPMENT PLAN[1]

Carlos Lessa

The purpose of my talk is basically to present some clues to try to understand why the country, in March 1974, launched an extremely ambitious economic policy proposal – the Second National Development Plan – and why, less than two years later, the national economic framework presents, at the level of all its indicators, a completely different map from the one projected, with ostentation, two years before.

I believe that, to carry out this inquisition, it would be important, at first, to quickly recapitulate the main orientations of the Plan, and try to speculate a little about the greater meaning of the proposal that was made.

You know that the Brazilian economy, from 1968 to 1974, presented extremely high growth rates of the "per capita" income. Our Gross Domestic Product grew during this period at an average rate above 9% per year, and this is a high rate in any experience of economic growth in the world.

In parallel, we had an industrial development pattern, which has some interesting features, whose numbers I will present to support our discussion. If we look at the Brazilian industrial structure and try to calculate the growth rates of the large industrial groups, we will find the following rates. In the 1966-69 period, the Brazilian capital goods industry grew at an average rate of 7.5% per year. In the 1970-73 period, this same industry grew at 7.2% per year. The durable consumer goods industry (automobiles, refrigerators, household appliances, etc.) grew in 1966-69 at a rate of 16.2%, and, in 1970-73, maintained the rate of 18.4%.

The non-durable consumer goods industry (basically food) grew, between 1966-1970, at the rate of 8.4%, and, between 1970-1973, at the rate of 7.2% a year. And finally, the intermediate goods industry (steel, paper, cement, cellulose, metals, etc.) grew, from 1968 to 1969, about 9.5% a year, and, from 1970 to 1973, at a rate of 11.4%.

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1 The paper is the transcription of a conference.

Anyone looking at these numbers is quite amazed at how our economy resumed industrial growth in 1966. It is not typical of the industrial development of a capitalist economy that the industry that leads the recovery from the crisis observed during 1961 and 1967 and the following expansion is the durable consumer goods industry (automobiles, refrigerators, televisions, etc.).

This is an unusual phenomenon.

In Brazil, this seems to have occurred as a result of some significant reforms that were carried out in the period after 1964.

To remember, these reforms were part of a profound restructuring of the financial sector, a violent compression of wages, and a process of business re-concentration (mergers of companies and a process of income concentration).

These initiatives, together, allowed the durable consumer goods industry in Brazil to recover relatively significant growth rates, starting with a recovery in their activity level. Then, around 1966-67, this industry started to grow. Initially, until 1969, it grew primarily based on the wide margins of idle capacity it possessed. From 1970 onwards, the exhaustion of the idle capacity margins caused the investment process to spillover through the economy, and the various industries began to grow at high rates.

The industry that started to grow at the highest rate was the capital goods industry, which, in the 1970-73 period, grew at a rate of 27% per year. This is an extremely high growth rate, and one should remember that, in the period of Minister Delfim, the equipment industry did not receive any special priority. More important than the 27% per year growth of the capital goods industry is the maintenance of a very high growth rate in the durable consumer goods industry, which maintained, until 1974, growth rates of 18% per year. In the case of the automobile industry, annual growth rates were above 20%. Without any deeper consideration, the simple fact that our economy has gone through a phase of long industrial expansion that generates, as a result, economic growth rates above 9% a year, supported by the durable consumer goods industry – this simple fact accentuates certain discontinuities within the industrial system.

These most notable industrial discontinuities were expressed in the basic industrial inputs industry, which, despite having grown at a high rate, stayed well below the high-end industry.

And Brazil, in 1973 and 1974, started to face more or less generalized shortage problems in the area of all essential industrial inputs. The most notable of all phenomena occurred with steel products, of which the country became a major importer.

With the risk of simplification, one can state that, in this expansion cycle – the era of Minister Delfim –, the Brazilian economy achieved a high "performance" in terms of aggregate growth, but its industrial structure was not able to make it grow in any way the industry that ensures the long-term continuity of the expansion process, which is the industry that produces production means, that is, the industry that produces equipment and the industry that produces basic inputs.

These industries, around 1974, represented a percentage no higher than the one they had in 1960 in the industrial structure. In other words, in 15 years of industrialization, they had not managed to change the industrial structure of the Brazilian economy.

As this period of rapid expansion, which lasts until 1974, was a period in which certain exceptional facilities, on the side of the external sector, allowed and overexcited the process of industrial expansion, our economy, around 1974, reached a rate of unusually high investment. The historical investment rate of the Brazilian economy is something around 16% of the internal income and, in 1974, the investment rate reached 27%.

This, in an optimistic reading, allowed two things: to see in Brazil a miracle, the Brazil-as-Great Power, the Brazil that broke the shackles of underdevelopment and that would soon enter the select club of powers; and, secondly, to see the Brazilian industrialization as analogous to the Japanese industrialization, when the Brazilian business-industrial structure has nothing to do with Japanese economy.

But, anyway, years of euphoria prevailed.

The Second National Development Plan (PND) is formulated in 1974 proposing a correction of the unevenness generated by the previous industrial expansion.

Where were these unevennesses concentrated?

They resided in the Basic Inputs industry and in the capital goods industry.

So what does the Second PND propose?

It proposes that the priorities of Brazilian industrialization be radically altered. From an expansion based on the growth of durable consumer goods, from an expansion based on a highly concentrated pattern, oriented and assigned primarily to high-end consumption, the economy should continue to grow, driven fundamentally by the industry producing means of production, that is, by the equipment industry and by the Basic Inputs industry.

These new priorities received some additional qualifications.

The most expressive of them was linked to the external sector itself. Insofar as the previous industrial expansion did not significantly alter the industrial structure, the proposed maintenance of high growth rates (the Second PND proposed to maintain the 10% growth rate of the annual GDP and reach, in 1979, the $1,000 mark of "per capita" income) was coupled with a total reordering of priorities. The automobile would no longer be the leading industry, the basic industry (steel, non-ferrous metallurgy, basic chemistry, large mining, heavy electronics) and the production of equipment and machines would become the leading industries, which required, given its previous vulnerability, that the economy managed to maintain its imports at a high level.

During the expansion period, Brazilian imports took a prodigious leap. By 1970, our imports were in the order of 2.5 billion dollars; by 1975, they had reached $12.2 billion. Therefore, Brazilian imports, in the space of 5 years, had practically quintupled.

This same period was accompanied by a great expansion of exports. They grew, however, much less than imports. In this period, exports evolved from 2.7 billion dollars to 8.7 billion dollars.

This meant that, in the final years of the expansion phase, the current account deficits in the balance of payments began to multiply in a frightening manner. In 1974, the Brazilian trade balance deficit was in the order of 7 billion dollars.

Maintaining the high growth rate proposed by the Second PND required that the economy necessarily managed to continue expanding its exports. And the hope, in this regard, was that the economy could significantly grow its exports of agricultural-based primary products, with the inclusion of a few mineral products.

However, it was proposed that, in parallel with the change in priorities, the "export-drive" that had characterized the previous phase should be preserved.

There would be a number of other details to point out in the goals of the Second PND, but I believe that this constitutes its strategic core.

Just to emphasize a little more the magnitude of the Second PND proposal, I want to remind that Brazilian steel production, which at the time was around 7 million tons, was proposed to reach 18 million tons in 1980. In other words, our country, which, in 50 years of steelmaking development, had reached the mark of 7 million tons, should reach 18 million additional tons in 5 years. As for aluminum, 100 thousand tons should be tripled. The 12 or 15 thousand tons of zinc should increase to 100 thousand tons. And so on.

It was proposed that our capital goods industry should more than double in the period, and the import coefficient of machinery and equipment should be reduced from 52% to 40% in 1976. Furthermore, the country should be able to export something like 200 million dollars worth of machinery and equipment in 1978.

From these numbers, one can see the magnitude of the proposal.

As this strategic package will have to make way in a world in which the so-called oil crisis had radically changed the relative price structure of the various energy items, the Second PND also contained the proposal that the country should change the energy structure, by a relative increase of consumption not dependent on imported inputs, and by intensive research into new energy sources.

It is clear that changing the energy structure, coupled with new industrial priorities, would also require a radical transformation in the transport structure. And an economy previously based on road transport should be oriented towards a growing mass transport economy based on railways and waterways.

In short, the proposal was as follows: maintaining the "miracle," the growth rate, preserving the high export growth rates of around 20% per year, but at the same time promoting a radical reordering of priorities (down with automobiles, more heavy industry).

Of course that today, when we see Brazilian inflation reaching the official mark of 37.4% until last month (and an unofficial mark probably above 40%), when our balance of payments deficit already reached in 1974-75 the $7 billion mark, and when the growth rate, which was around 10% a year during the 1968-74 period, by 1975 had already dropped to 4.2% a year – neither the growth target, nor the price stabilization target, nor the balance of payments target were achieved.

Obviously, the goals of the Second PND entered a reordering process and, in some cases, were forgotten.

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Let us now try to examine what is the meaning of the Second PND proposal, or rather, its deeper meaning.

When a radical reordering of priorities is proposed, a very essential question is this: Who will be the agent of these new priorities?

Once the change in priorities is proposed, some agents must be able to centralize, assign, and reorient the system, in search of these new priorities.

Therefore, who would be the key actor of the reorganization proposed by the Second PND?

This actor was already explicitly indicated in President Ernesto Geisel's speech on March 15th, 1974, and implicitly, within the goals of the Second National Development Plan.

That actor was the state company.

What are the main goals of the Second PND? Steel industry? These are targets of the state steel industry.

Big mining? Vale do Rio Doce.

Prospecting for new energy sources, changing the energy balance of Brazil? Eletrobrás, Petrobrás, etc.

Basic chemicals? Petroquisa.

A few basic input targets would not be the responsibility of any state-owned company, but the basic core, the key core, the critical core, must be led by a relatively small cast of large companies that had historically been shaped within the Brazilian institutional reality.

Assuming that these companies could, in their decision-making perimeter, push forward the projects that could materialize the goals proposed in the Second PND, they would generate a demand for capital goods, a demand for equipment that would provide the steady horizon that would allow private, national, and foreign companies to invest, expanding the domestic production of capital goods. In other words, the strategic actor is basically the state-owned industrial company. It is up to it to push the minimum package, the basic package, the vital heart of the Plan. To the extent that it succeeds in this task, other companies will carry out the subsidiary goals in the capital goods industry.

There is, therefore, a central actor.

That main actor, to fulfill such desideratum, would require that other industries, which were priorities, to stop being. To put it another way, real financial resources should be diverted from their old allocations, to make it possible for this new actor, this new set of actors, to accomplish the proposed goals.

Such reassignment, at the real and financial level, would therefore require, in parallel with the declaration in favor of new priorities, initiatives that compress, contain, and restrain the expansion of the former priority industries.

In 1974 and early 1975, the Second PND was pursued quite consistently. Several initiatives were implemented, all of them consistent with the set of goals proposed by the Plan.

Allow me to recapitulate some of the most important ones.

The first of these, of an absolutely vital and fundamental nature, was the transfer of PIS and PASEP funds from Caixa Econômica Federal to BNDE. Thus, the National Development Bank (BNDE) received, with this transference, in 1974, a doubling of its investment budget.

BNDE was therefore strengthened by the doubling of the funds at its disposal, by transferring the bulk of the country’s compulsory savings from the working capital financing sphere, and of the consumer credit sphere, both carried out by Caixa Econômica, to the financing of priority projects.

This transfer thus represents a first initiative clearly inscribed within the priorities of the Second PND.

In addition to this brutal strengthening of BNDE, other initiatives were taken. Direct consumer credit, for example, was reduced in 1974 from 48 months to 24 months. Seeking to restrain the expansion rates of consumption of durable goods, the Industrial Development Council (CDI), that same year, did something unprecedented in the history of the country's economic policy. For the first time, the CDI declared which industry was not a priority for it.

In Brazil, the CDI is an absolutely vital agency for any industrial project. Having a project approved by the CDI means, for entrepreneurs, that they will have exemption from customs duties on imported equipment, tax credits for equipment acquired internally, and "accreditation," which is almost a pre-analysis that gives them access to the development banking system. Without CDI approval, these tax and credit favors are closed.

Well. The CDI categorically declared that textile, automobile, household appliance, plastic industries, etc. (the list is very long) were no longer a priority, and therefore could not receive resources from the CDI. While the high-priority select nucleus, according to the Second PND, would receive the favors of that agency in a concentrated manner.

I have only mentioned three, but there are several other initiatives, all of them in the same spirit. However, it is important to bear in mind that, in 1974 and in great part of 1975, there was, on the part of government authorities, an effort to carry out, to turn the Second PND proposal into reality.

At the same time, the Economic Development Council announced numerous sectoral plans that would correspond to the concrete consequences of the general guidelines of the Second Plan, for example, the national fertilizer plan, cement plan, heavy chemical plan, the decision to implement the third petrochemical complex in Rio Grande do Sul, etc.

All of these form a package of initiatives that would give a name and a nickname to the main guidelines of the Second PND.

However, that same year of 1975 was already a year of great deceleration in the growth process.

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Why does the Second PND fail?

The first answer belongs almost to Counselor Acácio's terrain.

Allow me a jocose digression. When I was in college, I had a professor, for whom I repent for being irreverent, who said that "every ascending phase is followed by a descending phase, and every descending phase is followed by an ascending phase." Master Cacuri, of nostalgic memory, said this to point out that it is an inherent characteristic of a market economy, capitalist economies, to behave through cyclical pulsations according to which their growth rates do not remain constant for long periods, but on the contrary, to each ascent phase follows a descent phase in such a way that the behavior of the economy fluctuates over time.

If we add another lesson from master Cacuri, which belongs to popular wisdom, according to which "the higher the climb, the greater the fall," we would have approximately the situation with which the Brazilian economy was faced around 1973-74.

Let us see.

An economy that grew for eight years, at the rate of 10% a year, an economy that managed to maintain a prodigious industrial expansion, supported by a high growth rate of the durable consumer goods industry, an economy that raised its investment rate from 15-16% a year around 1968 to 27% a year in 1974, an economy that has multiplied its imports by five is an economy that has entered into overaccumulation territory.

If this economy, which entered overaccumulation territory, does not carry out significant structural adjustments, but, on the contrary, only confirms trends inscribed in its previous pattern of expansion, it is an economy that necessarily becomes more vulnerable to the Acacian oscillations that master Cacuri saw in the long-term behavior of market economies.

Hence, the previous great "performance" indicated the likely mediocre or even gray subsequent "performance."

It is necessary to bear in mind, moreover, that this trend in cyclical behavior can be reinforced by the economic policy, or it can be relatively mitigated by it. In other words, if the economic policy works in terms of making the ascending phase not so miraculous, it benefits with a less critical character of the descending phase, and the cycle is smoothed. If, on the contrary, the economic policy works in terms of "wow," "let's go!," "now we will be a Great Power," the cycle will become more marked.

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What happened in the 1968-1974 cycle, the country's Delfinian phase?

The following occurred.

Our economy, after the violent readjustments it carried out in the 1964-66 period, after the prodigious flattening of the wage scale, a vigorous business re-concentration, and an increase in the regressiveness in its income distribution, had operated a domestic readjustment of its financing pattern, which modernize it, eliminating the previous pattern that was the highly efficient inflationary mechanism in the 1950s, but already slipping, worn out, in the 1961-1964 crisis.

When the resumption of expansion in Brazil starts (and remember the lesson of master Cacuri: "at any descending phase, an ascending phase follows," that is, around 1964, the economy starts to grow again), there was no thought of a "miracle."

Brazilian Steel Production

Jan/Dec

PRODUCTS	1976	1975	76/75 (%)
Sponge iron	260562	210866	23.6
Pig iron	7845635	7052665	11.2
Total steel	9181596	8308046	10.5
Steel ingots	8071000	7828642	3.1
Continuous Ingots	1110596	479404	131.7
Laminated	7386284	6715893	10.0
Flat	3499965	3143996	11.3
Non-flat	3886319	3571897	8.8

Source: Estado de São Paulo (Newspaper), 1 nov. 1977.

Minister Delfim is one of the signatories of the Strategic Development Program, which proposed, as a goal until 1970, an average annual growth rate of 6%. Shyly, he intended 6%. But he benefited from rates of 9.3% in 1968 and 9% in 1969, pleasantly surprised by an economy that was growing above its proposal. And he discovered, after 1963, that the international market was in an extremely favorable expansion phase. The international financial market for Eurodollars was open to borrowers, and international trade was expanding.

In Brazil, we usually say that it was a "miracle" that Brazilian exports had grown at 20% per year from 1970 onwards. This is nothing miraculous, because, in this same period, world trade as a whole has been growing at around 20% annual rates. In fact, Brazil only participated in a great international trade expansion.

And, at the same time, the country enjoyed an extremely favorable international financial market.

What was the Brazilian "magic" in 1970-75?

It was to link its domestic financing pattern to the international financial market - our famous operation 63.

Allow me here to put together some numbers so that you have an idea of the magnitude of the links made.

In 1970, the Brazilian foreign debt was 5.3 billion dollars. Let us follow the curve of its growth. It went to 6.6 billion, 9.5 billion, 12.6 billion, 17.2 billion, and 22.2 billion dollars.

This growth in the foreign debt corresponds to an increase in foreign reserves, which, from 1.8 billion dollars in 1970, rose to 1.7 billion dollars in 1971, to 4.2 billion dollars in 1972, to 6.4 billion dollars in 1973, 5.3 billion dollars in 1974, and 4.2 billion dollars in 1975.

In the same period, foreign currency inflows were as follows: 1970 = 2.2 billion dollars; 1971 = 3.2 billion dollars; 1972 = 5.5 billion dollars; 1973 = 7.8 billion dollars; 1974 = 11.2 billion dollars; and 1975 = 14.7 billions of dollars.

These numbers show, with absolute clarity, how the "miracle" was accomplished.

The international financial market was extremely inviting. What have we done in the country? We started to allow our private financial sector to contract debit transactions abroad and transfer internally in the form of *cruzeiros*.

These foreign currency inflows were acquired by the Central Bank, with which the expansion of the means of payment, during this period, rested basically on the growth of Brazilian foreign reserves.

What have we done with this debt?

It is very difficult to describe everything that has been done; however, part of it is reflected in the mentioned figures.

We accumulated foreign reserves. For example, while our debt jumped from 9.5 billion in 1972 to 12.6 billion in 1973, thus growing 3.1 billion dollars in one year, our reserves grew, in the same interval, 2.2 billion dollars.

As our reserves grew, we presented an image of greater solvency to the world, which allowed us to contract new debt operations.

It is evident that, as the bulk of these inflows were made in the form of currency, this irrigated the entire financial system, which "sticked" to this foreign debt. And, thus, all the *lato sensu* companies somehow "sticked" to a process of financial amplification derived from this prodigious foreign indebtedness.

This is a wonderful operation, while it can be done.

I will draw a parallel with a gentleman who was penniless and who, with a lot of talk and malice, convinced the manager of bank A and got a good loan from him. Of this loan, he would deposit half in bank B and, with the other half, he would throw a big party, to which he would invite the managers of banks A, B, C, D, E. With the deposit made in bank B and with the magnificent party, the managers of banks C, D and E would say: Here is a good customer. And, in a second moment, he would go to bank C, take out a much larger loan and would make, with one part, deposits in bank D and bank E. He would then throw another party, even bigger than the first one. He would pretend that he was thriving.

This mechanism is remarkable because it allows, over a long period of time, to significantly expand credit lines, without revealing the basic vulnerability. It is enough that you can pay the interest on this debt at the time of maturity for it to be renewed. Now, as international trade was expanding and Brazilian exports grew, also because the volume of tax incentives given to exports came to represent a very powerful stimulus to marginal export industry, it was possible to pay interest.

But the operation is ruinous in the long run for a number of reasons. The most elementary of these, at the micro-accounting level, is that the interest rate on the loan taken out is higher than the interest rate obtained on the deposit. For example, we contracted indebtedness operations in the international market at much higher rates than the rates at which our growing foreign reserves were remunerated. Thus, there was already a direct loss.

A second direct loss comes from the fact that, as these loans are basically used for "parties," their interest rate increases. What would be the "party," on a macro-economic level, similar to the party of the mentioned gentleman? It would be to keep the durable consumer goods industry growing at rates of 16%, 17%, 18% a year. This is a "party" because it is not because of it that the productive base of the economy is significantly expanded.

Therefore, the mechanism works until when one can't pay the interest, that is, until one's balance of payments gets out of balance.

That was the operation we did.

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The Second PND was formulated at a time when there were serious doubts about whether it would be possible to continue borrowing and throwing parties. The conclusion was: "It is no longer possible to throw parties, I now need to do serious things." However, to do serious things we must continue to have credit, that is, continue to be able to pay interest, continue to do imports.

But it turns out that the key variable that defined the previous expansion condition, which was a prodigious external opening, changed course. International trade, as one of the dimensions of the capitalist expansion at the world level, also behaves as master Cacuri said – it has its ascending phases and its descending phases.

The descent had already started before the oil crisis. The so-called "oil crisis" is a folkloric element of that era. In fact, international trade was already changing its course in 1973.

And, at the same time, with the change in course of international trade, and, later on, the spillover of the oil crisis, the international financial market completely changed its course.

So, it was no longer possible to maintain the financial model that had been working in the previous phase.

The Second PND foresaw the possibility of preserving this pattern. With the difference that it did not include the use of resources for "parties" but for the priority construction of the basic industry.

Consequently, the Second PND already faced a fundamental difficulty in its origins – that the “Brazilian miracle” was not a structural miracle. In fact, it was the product of the conjunction of a moment of internal expansion, with extremely favorable external conditions. And both conditions were already reaching their tipping points. That was the first barrier.

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The second barrier is more of a *political* nature.

Napoleon once said that a military officer can do anything he wants, except lean on the tip of a bayonet. By this he meant that any regime, regardless of its degree of political openness, cannot sustain itself. It needs, in some way, to refer to certain social groups that support it.

Now, to carry out a radical change of priorities, whereby the basic input industry and the capital goods industry become the centers of the scenario, become the high expansion industries, become the industries of high accumulation rates and, at the same time, to restrain the expansion of previous leading industries, means in concrete terms losing the support of some in exchange for others. These few, whose support is lost, are all those industries that found themselves recognized within Brazilian society during the previous expansion process. Along the previous pattern of Brazilian industrialization, the political weight of these industries had obviously increased.

Therefore, the inflection meant hurting the interest of these heavier industries within the Brazilian economy in the name of new industries that should come out strengthened at the end of the strategy if it is successful.

Financial reassignment meant strengthening the official development bank system and, to the detriment of a certain loss of substance of an actor who, in Delfim’s euphoric phase, was seen as the possible Brazilian private group capable of giving meaning to our development process, the famous private financial sector, which should now pass to a secondary role.

As a matter of fact, you remember that the beginning of the Geisel government was marked by the explosion of a series of financial conglomerates, which the previous phase of “wow” had allowed to multiply: Halles, União Comercial, Ipiranga, etc, etc, etc.

We therefore have a strategy that does without the support of groups of greater weight within the social system and proposes a new set of priorities, a radical change within society without being supported, at least explicitly, but in the authority of its own proposal (Napoleon would say: on the bayonet itself).

Secondly, one must bear in mind that the Second PND has some other implications that also represent less support for its proposal.

One implication, for example, is at the spatial level.

I will try to recapitulate and locate some of the main goals of our Second Plan. The aluminum industry, the Trombetas project, stopped. The second iron ore export line – Carajás –, the largest Brazilian steelmaker would be built in Itaqui, in Maranhão. The basic chemical industry and the oil prospecting effort would be developed primarily on the northeastern coastal shelf, and the basic chemical complexes would be soda-chlorine in Alagoas, petrochemicals in Bahia and Rio Grande do Sul, potassium fertilizers in Sergipe, copper in inland Bahia, phosphate in inland Minas.

Please note that, regarding the major goals, I never mentioned São Paulo at any time. The key package of the Second PND is a package that implies a new spatial reorganization of the Brazilian economy. This new reorganization has at least two implications: the points of infrastructure and the reconversion of the transport-energy binomial should be informed by this new spatial reality; and, furthermore, the capital goods industry should also necessarily undergo a spatial reassignment, because the capital goods industry that currently exists in the country is basically located in the São Paulo plateau, but had its emergence oriented by the market.

To the extent that the Brazilian economy intended, with the Second PND, to face the development of basic industry, it would necessarily be directed to natural resources. And this movement towards natural resources puts our capital goods industry in a bad spot. It has to be located on the coastline, close to the ports. That is why the three most likely locations should be Baixada Santista, and the Santa Cruz region, in the State of Rio de Janeiro and Espírito Santo.

Interestingly, we have a strategy that affects the interests of the private financial sector, the golden girl, the main actor in the previous phase; a strategy that proposes to contain the expansion of the durable consumer goods industry, of dominant weight within the Brazilian industrial system; a strategy that implies the spatial reorganization that, for the first time, places the peripheral regions as vital to economic expansion, a strategy that, in fact, attacks and affects a whole constellation of extremely powerful interests.

Now, President Geisel, as you all know, is deeply committed to a project of political democratization. In other words, along with the Second PND, there was a proposal that the country should enter into a process of gradual normalization of its formal-democratic institutions.

This opening process takes on many faces. The most visible is the one through which the press increases its degree of autonomy.

In fact, the voices made uneasy by the new priorities managed to channel their verses in such a way as to erect a screen around the barren and to some extent inconsequential discussion about nationalization. It is evident that such a significant shift in the course of industrialization would require a state agent at the heart of the system. And this is understood as nationalization. And this is the form that the political opening process takes.

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Now, one last obstacle.

In any process of intense capitalist expansion as was the case in Brazil from 1968 to 1974, the sphere of speculative operations naturally tends to have growing weight. This is inherent in the game's own rules.

You know that, in 1968-70, we had a ridiculous speculative experience here, linked to the Stock Exchange. In the euphoric state in which Minister Delfim found himself around 1969, he presented a magical proposal that would allow the Brazilian patriarchal company to become a large and modern company, by obtaining risk capital through a large, busy, and dynamic capital market. To this end, a whole range of stimulus initiatives was triggered to generate a violent displacement of funds to investments in equity, provoking the melancholic and somewhat ridiculous episode of stock market speculation of 1969-70.

The great proposal was presented to the country: Save!

I would like to tell you that, in an economy like the Brazilian one, there is no proposal more subversive and more anti-social than saying to the middle class: Save! If our middle class decides to postpone a car purchase or car replacement, we will have a cyclopean-scale recession in a year. This is because the automobile industry, to produce 800,000 vehicles a year, needs a middle class that does not save, but, on the contrary, enters into crazy consumption and even anticipates consumption. That is why there are facilities, such as direct or consumer credit, and others, to induce them to spend more than their income at present and to pay interest for it. This is a middle class that interests a society like ours, not a middle class that tightens its belt and saves pennies to buy stocks. This is absolutely ridiculous.

Voluntary personal savings, in the US economy, do not represent 3% of internal capital formation. However, in Brazil, in 1969-70, the great proposal of "saving" was presented to the middle class. It is evident that the middle class has not saved. What was done was a prodigious speculation around the Stock Exchange, which was the first episode.

Soon after, we had interesting speculative operations with real estate. I don't have any series of real estate prices in my hands, but rural and urban real estate revaluation in Brazil, has moved at rates that were multiples of any inflation rate.

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Finally, from 1974 on, a new invention appeared in Brazil, the open market – that is, speculative operations in the money market.

I will not go into details about the open market, but we must bear in mind that speculative operations represent an additional obstacle to the reconversion proposed by the Second PND.

On the one hand, they significantly increase the profitability of the financial orbit, to the detriment of the profitability of the industrial or, if you like, of the productive orbit. It is evident that, to the extent that a certain mass of profits within an economy cannot expand indefinitely, because the possibility of compressing the remuneration of the workforce is reduced within the country, the amplification of the financial orbit means a redistribution of earnings to favor finance capital against industrial capital. In other words, the profitability of increasing financial operations erodes the profit rate of the directly productive industry.

This is not critical when the economy is expanding. However, when the economic expansion fizzles, financial speculation starts to have a perverse effect. Increasing the profitability differential in favor of the financial sector, a growing profit mass is channelled to the speculative financial system.

Less than fifteen or twenty days ago, the open market in Brazil turned 10% of the total means of payment in a single night. And rates of 5% and 8% have already been verified in the open market.

This gives an idea of the degree to which the speculative process starts, in a descending phase, to dominate any other applications.

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In short, to not further delay our investigation, the Second PND was buried.

What's up now?

We are in a situation that presents quite curious aspects. The "miracle" has disappeared. The prodigious growth rates have been stopped. At the same time, we will have an inflation rate of 40% this year. One must remember that inflation rates of this level were considered criminal by past administrations. Regarding the balance of payments, to get an idea, our current account deficit was 7 billion dollars in 1974. That year, our foreign debt grew by 5 billion dollars. Also in 1974, the debt service reached $2.4 billion. The following year, our deficit was again $7 billion and debt service advanced to $3.5 billion. In other words, high balance of payments deficits mean that, with the indebtedness rate maintained, the new debt virtually corresponds to the service of the previous debt. So this door is closed.

Again, the growth rate slowed and will be kept at a lower rate, the inflation rate exploded, and balance of payments deficits became serious.

How to maintain the heroic proposal of causing a significant change in the industrial development pattern and, simultaneously, preserve high growth rates?

It has been shown that this is not possible.

Given this, what was the official diagnosis?

I must believe that the official diagnosis is verbalized by Minister Simonsen. And Minister Simonsen declares that the Brazilian inflation is a demand-pull inflation. In other words, that Brazilian inflation is caused by a fiscal deficit, when public spending exceeds current public revenues, and the financing pattern presents characteristics that expand the means of payment.

Now, Minister Simonsen's diagnosis is no different from Minister Roberto Campos' diagnosis in 1964.

You know that Minister Campos has been very successful in extinguishing the fiscal deficits. In 1964, these deficits were 4.5% of the domestic product; in 1966, they were 1% of the GDP and fully financed by issues of the inflation-indexed ORTN (Adjustable National Treasury Bonds), that is, without monetary expansion.

However, in those years in which Minister Campos achieved fiscal balance, the inflation rate of the Brazilian economy was around 40% a year. And, in years when fiscal spending expanded – Minister Delfim's golden years –, a falling inflation rate, which reached only 15% in 1972, was compatible with rising fiscal deficits and was also compatible with a prodigious expansion of means of payment.

In other words, Brazilian inflation is not a demand-pull inflation.

This has already been proven *ad nauseam* with the experience of Minister Campos and was stated in Minister Delfim's diagnosis in 1967. And Minister Simonsen himself is the author of the book "Gradulismo e Tratamento de Choque" (Gradualism and Shock Therapy) where he seeks to show that the Brazilian inflation is not a typical demand-pull inflation. Now, as Minister of Finance, he declares that Brazilian inflation is a demand-pull inflation and that the solution is to cut public spending.

Why does Minister Simonsen say this?

I believe there are many reasons. The most elementary of these is that the economic policy´s degree of autonomy is today extremely reduced. Why? Because there is a monster within the economy that cannot be controlled.

The financial sector, which was created within the system, and the speculative operations carried out within this sector, do not allow, prevent and inhibit the handling of a series of economic policy instruments.

For example, currency devaluation could be a solution. But to carry out a currency devaluation in a country in which 15 billion dollars represent private financial system debts with other countries and, indirectly, of companies with the financial system with exchange rate indexing clause, simply means generating a financial "crack."

Vigorously controlling monetary expansion or even adopting a restrictive credit policy is not the solution either. Because, as we have an uncontrolled money market, like a mad beast on the loose, operating in its own range, totally detached from the real orbit but glued to the entire financial system, any liquidity variation represents a more than proportional variation on the open market, which again runs the risk of causing a breakdown in the financial system.

Therefore, the exchange rate cannot be changed significantly and the Brazilian monetary policy is one-way, that is, it can only continue expanding the means of payment.

What to do then?

Trying to control prices. But controlling prices in an economy that slowing down, which has a loose financial sphere, like a mad beast, biting at the profitability rate of the directly productive sector, simply means lowering the productive sector's profit rate even more.

The mechanism for the resumption of expansion in any capitalist economy is basically the investment rate, and it depends not on the voluntary savings of households but on the mass of profits retained by the companies. If the policy is one of violent price compression, the crisis will simply deepen.

So, in fact, the classic economic policy instruments that Minister Simonsen has are instruments that he cannot operate.

What instrument can Minister Simonsen operate?

A single one, which is to reduce public spending. The decrease in public spending, however, has zero efficiency.

The reduction of public investments, in an economy that is already decelerating, means to deepen the deceleration process even more, without this implying any reduction in the inflation rate. On the contrary, according to Brazilian experience, such an initiative should lead to an acceleration of the inflationary process.

In short, Minister Simonsen's degree of autonomy is simply zero. There's nothing to do, nothing to say.

So, he says only one thing: inflation is demand-pull...

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For my part, I hate making predictions or trying to use a crystal ball. I am one of those who believe that economics is a social science, not an analytical technique. And in the area of economics, there is no future in trying to use a crystal ball. Certainly, the autonomy of Brazilian economic policy today, in 1976, is much shorter than the degree of autonomy in 1964. In 1964, our economy had some possibilities.

First, it could still violently compress wages. But today, whose wages can it compress? Only middle class ones. This is possible, but it converts into leaning on more and more on the bayonet, using the image of Napoleon...

Second, as a second maneuver, in 1964, the economy still had the possibility of a substantial reorganization of the financial system. This reorganization was carried out from 1964 to 1966. However, it was irresponsibly and inadvertently linked to foreign indebtedness. As a result, the degree of autonomy for any significant structural change in the financing pattern is greatly reduced.

Unless a proposal is submitted: nationalizing the financial sector and subject the non-nationalized part to strict and draconian controls.

This would be a “solution” in theory. However, in my opinion, it belongs to the same category as putting the bell on the cat’s tail... Clearly, reforming the Brazilian financial system would be possible, but who would do it? In summary, today a situation more or less like 1964 is repeated, with one difference, that is, the degree of autonomy is much smaller. Allow me to detain my considerations here, being at your disposal for any further questions. (Long applause)

Debates

1st Question: – Since the emphasis of the Second PND is focused on the industry of equipment, basic inputs, which invariably present a relative slow return on investments, I ask:

a) Shouldn’t the Plan’s creators have been concerned first with detecting the sources of resources necessary for its financing?
b) Doesn’t it seem that this search is taking place *a posteriori* and, even worse, by a process of foreign indebtedness that will eventually result in another “party,” along the lines of 1970-74? (Eduardo Daher)

ANSWER: – Let’s do some reading. The attempt at reinforcing the BNDE system; the creation of three sisters IBRASA, IBRAMEC, and FIBASE; the efforts for greater discipline in foreign indebtedness operations, they all formed a list of initiatives, where the Geisel administration tried to give content to the projects proposed in the Second PND.

The limitations were, in my judgment, much more at the level of the global movement of the economy than in projecting techniques or specific sectorial initiatives of economic policy. In fact, the Second PND assumed certain historical conditions, none of which existed. This is my thesis. Secondarily, I would say that there are, of course, some significant deficiencies within the initiatives related to the basic inputs industry. The most important of these concerns prices. In fact, the profitability of this industry, to a large extent, depends on rising the prices of basic inputs and holding the prices of other goods. But the author of the question may notice that this is part of the initiatives that "poke the bear."

So the degree of autonomy was too small.

Regarding foreign indebtedness, I would like to draw attention to the fact that the large imbalances in the Brazilian balance of payments, verified in 1974, 75, and 76, especially in 75 and 76, are linked to two main vectors.

On the one hand, a huge increase in debt service. On the other hand, the great important vector was the prodigious expansion of imports of capital goods.

When Minister Simonsen says: "One must slow down the economy, cool down the economy" – in fact, what he is chasing is, by a reduction in the growth rate, a more than proportional reduction in imports of capital goods, as a condition for a nebulous resumption of the expansion, naturally around the 80s.

Therefore, I do not believe that the economy, in the coming years, will be significantly indebted by the Second PND package.

And, most likely, if things continue the way they are now, the economic slowdown will cause us to run relative surpluses in the current account. But at a price: the country is no longer "miraculous," the country will not be a Great Power, etc.

And, by the 80s, maybe, a Minister of a new cycle (master Cacuri said that after each descending phase an ascending phase will come), the economy will resume expansion, with an industrial structure that will not be very different from the one that was "loved" in the second half of the 50s, at the time of the Plano de Metas. And a similar problem will probably appear in the 1980s, as a "Brazilian neo-miracle."

2nd Question: – After all, who is right? Master Cacuri and Counselor Acácio, according to whom "the darkest hour is the one that precedes the dawn," or Minister Veloso, whose sentence, when launching the Second PND, was: "What inspires this Plan is the fact that Brazil is a country that has opportunities," or even the pessimists, who claim that we are simply "broken"? (Antonio Sergio Rezende de Campos)

ANSWER: I confess, in all honesty, that I tend to agree with my master Cacuri. However, I can understand Minister Veloso's position. As Minister of Planning, Veloso has a professional obligation to instill optimism and convey a favorable message, whatever the conditions.

But the problem is not so much pessimism or optimism.

The truth is that there is no capitalist economy in the world that has not behaved in this way. They all go through their prosperity phases and their crisis. Only, some have more disastrous crisis than others, largely due to hyper-optimism...

The great frustrations, when we discover that we are not a Great Power, and probably will not be in 1979, should not obscure the fact that, despite everything, this is a critical system, which, by its own internal logic, maintains its dynamic. That its dynamics can be distorted or predatory, in many aspects, is a price paid for the system's own dynamism.

3rd Question: – In your opinion, what will be the consequences, or what is true in the World Bank's statement about the unfeasibility of the expansion projects of Companhia Siderúrgica Nacional and Companhia Siderúrgica Paulista (COSIPA)? (Carlos Adolfo S. Sarmento Júnior)

ANSWER: Unfortunately, I don't have any other information about it other than that of the newspapers. I don't attend the Power anterooms or rooms... So I don't have any confidential information.

Brazil's steel goals are extremely ambitious and, to a large extent, were inspired by the hypothesis that, with world trade continuing to expand, the country could be an exporter of semi-finished steel products.

It so happens that the worldwide recession was reflected in the international trade of steel products, and the first great goal that was buried was the one of the export steel industry. The goal of Itaqui, in Maranhão, was buried.

I don't have the elements to get in the backstage of the government thinking on the rest of the question.

4th Question: – Would there be any possibility of minimizing the failure of the Second PND? If so, what could be the initiatives to achieve this goal? (Mário Joaquim de Almeida)

ANSWER: I am being compelled to behave like the doctor, who is always obliged to give a prescription... (Laughs).

But I'm only an economist. And I believe that the only title that the economist can hold is that of being the first professional in Latin America, as Columbus was the first economist who arrived here. They say he was an economist, because, when he left Palos, he didn't know where he was going, and when he arrived, he didn't know where he was, but he made assumptions and systematically acted on behalf of the government. (Laughs).

I think it's very difficult to say "what are the initiatives to achieve the objective" referred to in the question.

If I put myself in the situation of the little mouse in the story who suggested putting the bell on the cat's tail, the initiatives are pretty easy to indicate. They would, for example, be an increase in the tax burden, violently burdening high-income groups and eliminating reduced forms of taxation on income. Second, a nationalization or, at least, an extremely strict control of the entire private financial sector. Third, a currency reform with multiple and differentiated exchange rates.

These are three exits. But who will implement these initiatives? Who will "put the bell on the cat's tail"?

5th Question. – Would it not be useful for Brazil to enact a program to develop industries that would make it more independent, or less vulnerable to external crises, leaving behind heavy industry, which requires imports? Wouldn't it be more appropriate to dedicate the country to modernized, mechanized agriculture? (Jaime Vicente Dellandrea)

ANSWER: – Dedicate the country more to agriculture, but for whom?

If it's for export, assuming we could export, that would make us even more vulnerable to the international context.

If it goes to the domestic market, a significant increase in the population's income is necessary. And this increase would only be possible if the economy managed to accelerate its industrialization process. The manufacturing industry is the locomotive that drives the expansion of the system. Agriculture never was. In fact, agriculture is just a wagon with free wheels: if the locomotive runs at high speed, agriculture responds anyway. But it never pulls the composition.

On the other hand, I do not see how a proposal for autarchic development would be viable in a world where capital accumulation is increasingly operating on a global scale. In a world where the accumulation of technical progress has been dissolving the barriers of nations.

How could Brazil choose a strategy to break and move away from this pattern? I think it's extremely difficult.

6th Question: – After the slowdown of our economy, we should, according to your assertion, enter an acceleration phase. How will this happen if we do not have the means to overcome the crisis? (Mario Bruno).

ANSWER: – The statement regarding the cycles is not mine, but by master Cacuri... But in the cycle, the descending phase is as necessary for a capitalist economy as the ascending phase.

I'm going to try to offer a pretty shallow prognosis of what is likely to happen in the next few years.

The decrease in the growth rate and an economic policy that will necessarily have to be restrictive, and to some extent confused regarding capping growth, will provoke a process of income reconcentration within the economy.

Every time an economy is not expanding, the strongest grow at the expense of the weakest, either by bankruptcy or by absorption. Who are the strongest within the Brazilian economy? Basically, the most solvent companies, which are companies that have foreign connections. So, it is elementary that the degree of industrial concentration of the economy will grow and the degree of denationalization will probably grow in the coming years. These two facts must occur.

This process of concentration is one of the necessary passages for us to resume expansion. From 1964 to 1966, the country went through a vigorous process of concentration and an accelerated process of denationalization, which was followed by a period of expansion.

This means that the acceleration that will come will pass through the purgatory of a crisis that is extremely reduced at this moment, in my opinion.

Now, going through purgatory or hell is the price you pay for going through a euphoric phase of "wow," "let's go," "nobody can stop you," etc.

7th Question: – You said that the government shouldn't have given so much incentive to saving, as it would be necessary or more important to consume than to save.

Knowing that the entire civil construction industry is fed with resources from the FGTS and Savings Accounts, wouldn't we have the serious problem of unemployment and the consequent emergence of underemployment leading to a drop in consumption? (Dilson Gerent)

ANSWER: This question deserves several answers. First of all, one must bear in mind (and I'm not the one who says) that the so-called advertising, the several techniques by which consumers are compelled to consume more, is not something perverse and vicious compared to healthy habits of savings.

On the contrary, they are fundamental institutions to maintain the expansion dynamics of capitalist economies.

What I have stated is that voluntary personal saving is not important to the process of capitalist expansion. I did not say that savings are expendable, because corporate savings are essential and personal savings are compulsory (Guarantee Fund for Time of Service, PIS, PASEP, etc.), these are indeed necessary.

What is questioned is the possibility of an economy, at the stage in which the Brazilian economy is, to be able to capitalize its companies by voluntary renunciation of present consumption. That's what's unfeasible.

And the incentives given in Brazil to saving, in reality, do not encourage saving at all. All they do is give a more beneficial tax treatment to capital income.

As far as I know, no one, in the range of 3, 4, 10 minimum wages, compressed consumption to subscribe to shares, or significantly compressed consumption to put money in savings accounts, thinking about tax advantages.

It is the high-income groups that, among the options to pay higher taxes, or subscribe to shares, or make fixed-term deposits or invest in certain stimulated industry, do this to reduce their tax burden.

And that's good because, I repeat, if we middle class, decided to save significantly for a year, we would generate a crisis of cyclopean proportions, then yes, there would be significant unemployment.

8th Question: Admitting state companies as the nucleus of the change contained in the Second PND towards the fundamental industries of the economy, would it not be dangerous to proceed with the much-debated privatization? (Eros Antonio de. Almeida).

ANSWER: – I have watched these debates on nationalization and privatization three or four times in my forty years of life.

It is part of the ideological reading to suppose that "the entrepreneur is the good, the State is the evil," that the entrepreneur is the "hero" who, with his superman qualities, organizes the factors of production and, with his genius and heroic decisions, develop the productive forces – and that the State is the bureaucratic, castrating, irritating, inefficient, etc. agent.

It is curious that this Manichean vision has always worked in tandem with the progressive and gradual expansion of the State in any and all modern capitalist economy.

Nationalization is not a phenomenon limited to Brazil. There is nationalization in Western Europe, as there is in the United States, etc; a more or less universal phenomenon within the capitalist world.

Why?

Because the State plays a fundamental role in capital accumulation. I will crudely illustrate this role played by the State, with the joke of two men, from Minas Gerais and São Paulo, who, in partnership, bought a cow. In the joke, the man from Minas is the "smartass" and the one from São Paulo is the "muggle." The latter got the front end of the cow and the former got the rear end. So, the guy from Minas was entitled to the calves, milk, and, as an additional bonus, the natural fertilizer produced; while the guy from São Paulo was left with the obligation to feed the cow, drive it to the pasture, and his "bonus" would be being eventually gored... (Laughs).

The division of labor between the State and private enterprise is more or less of this type. It is up to the State, within a country like ours, to carry out basic investments, orient the accumulation process, centralize capital, change the structure of prices and costs to raise the profitability rate of companies, ensure demand for companies, etc. In other words, to "feed the cow." It is up to the private company to place itself "in the rear end of the cow," that is, to place itself in directly profitable activities, etc. What is the added bonus? The companies get it, and the State has the additional burden of receiving the epithet of incompetent, etc. But no cow can walk if it is not fed...

Nationalization in Brazil is a phenomenon that is not new, but starts at the beginning of the century. And despite all the repeated declarations of faith and trust in the private sector, despite the eternal ritual performed by public men to say that they will not allow nationalization to increase, it has increased at the hands of those most hostile to the State.

The period in which the Brazilian economy was most nationalized was the period of Minister Roberto Campos, who, as you know, was notable for being a controversial opponent of President Juscelino Kubitschek, who he accused of being a great statist. Campos was more of a statist than Juscelino, if we measure nationalization by the criteria that he, Campos, used to judge himself. The State's participation in the domestic formation of capital, at the time Juscelino, was 50%; at the time of Campos, it was 65% and reached 70% in one year.

However, the debate, the topic of nationalization lends itself to a thousand wonders whenever it is necessary to say the following: "Cow, feed me, not the other." In other words, the problem is not so much the weight of the State in the economy, but knowing who benefits from that weight.

In the Second PND proposal, it is unquestionable that, provisionally, the cow intended not to feed so many (the private company) and to concentrate forces, not to socialize the economy, but to allow – this was its desideratum – that capitalism in Brazil could be stronger and more vigorous in the future.

There is a brutal contradiction here, since, in the immediate term, this would mean temporarily reducing the advantages of the man from Minas Gerais from the joke. And he soon complains: nationalization!

It is basically a mere ideological operation.

9th Question: If the Second PND had been based on private initiative at its core, instead of depending on government investments, could the result of the process have been different? Wouldn't there be an even greater denationalization of our economy? (Manoel Luiz da Costa Marques)

ANSWER: The student's question concerns the national private entrepreneur, the so-called national bourgeoisie.

In the 50s and beginning of the 60s, I watched many debates about national entrepreneurship. The factions that said it existed and that it would be able to confirm and carry out its National project always presented as examples Pignatari, José Ermírio de Moraes, Matarazzo, Gasparian, and I believe the list is finished. These were the historical examples.

I'm going to give you a number so you can have an idea on the subject. All stock issues carried out in 1969 and 1970, during the stock market boom, totaled 900 million *cruzeiros*. A 4 million ton steel plant, alone, represents investments three times higher.

This gives an idea of disproportion. It is evident that the national private entrepreneur does not have the resources nor breath to face the strategic package. So, assuming that the State renounces this package, the vacuum can only be filled by another type of company – a foreign company.

What is questionable is whether the foreign company is interested in this vacuum. In fact, it is much more interesting for the State to invest in steel mills and the private sector to invest in the automobile industry and receive steel plate at lower prices and therefore higher profits.

In the division of labor between the State and the multinational company, the paradigm of the story I told of the society between São Paulo and Minas Gerais also works. I am convinced that what takes place is this division that we are currently having in Brazil, much more than the one in which misters Pignatari, Matarazzo, Gasparian, etc. were presented as examples of the national business community.

Minister Delfim, already a little desperate by not finding the national industrial entrepreneurs, presented the proposal that they would only exist in the financial sector. And then, it would be necessary to strengthen the private financial groups as much as possible, reducing them in number and strengthening them, so that, at a given moment, they could link up with the industrial sector.

It was the thesis of the financial conglomerate as the embryo of the great national private conglomerate. Minister Delfim's financial conglomerate gave two results: The mushrooms that popped up shortly after the expansion signal changed and, secondly, a fascinating vocation for speculative operations strictly confined to the financial orbit.

Concretely, there is no national domestic business capable of carrying out a proposal like the Second PND. In fact, what we discussed here was the demonstration that the State itself, like the businessmen, is not able to do it either.

So, answering the student who asked the question, if the State renounced this package, we would enter the terrain of doubt, to find out whether the multinational company would be interested in stop being "the guy from Minas Gerais" and start being "the guy from São Paulo" in the story. And this is doubtful.

Consider the risk contracts, in which only two multinational companies appeared, with extremely modest proposals.

10th Question: – If it were up to you to give a solution to the Brazilian economy (or to "put the bell in the cat's tail"), what would be the most viable alternative within the world context? (Rosário M. de Souza).

ANSWER: – I believe that I would give this question an answer *à la* Manuel Bandeira: "It's better to dance an Argentinian tango…" I want to say that I do not see today, in the Brazilian economy, any degree autonomy that would make it escape its recessive phase.

The most I would see would be a few maneuvers to make the recessive process only a purgatory. I don't see how to escape a certain predestination to pass through the purgatory. (Long applause).

CHAPTER 7

DETERMINANTS OF POVERTY IN BRAZIL[1] – A STUDY GUIDE

Carlos Alonso Barbosa de Oliveira[2]
Wilnês Henrique

Recent studies and research on poverty in Brazil, if, on the one hand, deepen specific knowledge on the subject, on the other hand, leave a fundamental question: why are there so many miserable people in the country? The labor market, the behavior of the poor, their culture, etc. are studied, but perhaps because of the segmentation and specialization of academic knowledge, the general determinants of the misery of the Brazilian people are ignored.

This question was central to ECLAC, arguably the leading school in Latin American social thought. In the seminal 1948 study, Prebish[3] demonstrated how the limitations inherent in the primary-export model implied social exclusion and condemnation of a large part of the population to miserable living conditions.

The inability of the primary export sector to grow continuously at adequate rates limited the incorporation of labor into the modern part of the economy, which operated with advanced technology and high productivity levels. Thus, a considerable portion of the population vegetated in the traditional sector with very low levels of productivity and archaic technologies, condemning these populations to precarious consumption patterns and penury. The coexistence of the backward sector with the modern export sector determined the formation of a labor market unfavorable to workers in the modern sector, since the unlimited supply of labor willing to abandon the traditional sector pressured the labor market of the exporting capitalist nucleus, preventing the wages of this sector from growing with productivity increases.

ECLAC's rigorous analysis of the primary-export model not only dealt with the determinants of poverty among the Latin American masses, but also pointed out ways to solve the issue: only industrialization could guarantee the restructuring of the economy and society of Latin America, opening a route to overcome misery.

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2 Professors from the Institute of Economics at Unicamp and researchers from CESIT – Center for Union Studies and Labor Economics. The authors are grateful for the observations made by Professor Paulo Baltar.

3 Prebish, Raul. Interpretação do processo de desenvolvimento econômico. Revista Brasileira de Economia, ano 5, n. 1, mar. 1951.

However, the hopes of the developmentalist ideology, implicit in ECLAC's thought, began to be dashed from the 1960s onwards. Several countries in Latin America had gone through an accentuated process of industrialization; however, social exclusion, poverty and social inequalities not only continued to manifest themselves, but in some countries they became more acute.

ECLAC then turned to the critique of the "development model" or "development style." An exhaustive analysis of this literature would not fit here. However, at the risk of injustice or even erasing the various nuances present in the contributions of different authors, we will try to identify the determinants of social exclusion pointed out in ECLAC's critique of the Latin American development model.

In summary terms, ECLAC's criticism was to find the determinants of social exclusion in the productive structure that had been shaped in Latin America from the second half of the 1950s onwards, with the establishment of industries of consumer durable goods. The economic leadership assumed by the industries (dominated by multinationals) producing consumer durable goods, of high unitary value, in countries with low levels of per capita income, reiterated the inequalities in income distribution, while demanding economic policy initiatives that walked in the same direction. On the other hand, certain authors drew attention to the fact that this development model would not be dynamic enough to create jobs, perpetuating the permanence of populations in the archaic sector of the economy.

However, as Waldir Quadros says: "the direct relationship that is currently established between the so-called durable consumer goods model and the serious picture of shortages and social exclusion that accompanies the Brazilian economic development is problematic"[4]. For, as Paulo Renato Costa Souza sums up well: "there must always be some correspondence between the pattern of accumulation, the productive structure, and the wage pattern… It is necessary to abandon the idea that only one solution must be found for these interrelationships, deriving only from the game of economic forces without any responsibility for the negotiation between social classes."[5] And, with regard to the productive structure itself, Aníbal Pinto, commenting on the trend towards homogeneity in Core countries, concluded that "the influence

4 Quadros, Waldir. Mobilidade estrutural e grupos ascendentes: nova classe média. Relatório de Pesquisa: Urbanização estrutura ocupacional e regional do estado de São Paulo/1970-80. São Paulo: Convênio CEPLAM/ CECAMP. p. 143.

5 Souza, Paulo Renato C. Salário e mão-de-obra excelente. In: Souza, P. R. C. Empregos, salários e pobreza. São Paulo: Ed. Hucitec / Funcamp, 1980. p. 15.

of economic and social policies, especially in the post-war period, is a main factor in the process"[6].

In short, the determinants of poverty and social exclusion cannot be deduced from the economic structure and some historical examples can clarify this position. It is sometimes said that in certain phases of industrialization, the penetration of capitalism in the countryside generates a population surplus that puts pressure on the labor market, making it unfavorable to workers. And it is concluded that this phenomenon, visible in Latin America, would also have manifested itself in nineteenth-century Europe, but with a difference: European countries were able to get rid of the problem through emigration.

In fact, emigration movements took place in several European countries. But why the French in the nineteenth century did not have to submit to the painful conditions of mass emigration? Why did employers' complaints about the lack of labor become widespread in nineteenth-century France, in a country that, in the eighteenth century, was infested by hordes of vagabonds and declassified people, that is, by an expressive "surplus population? " In short, because, in the industrialization process, part of the French people was not forced to emigrate in ship´s holds, unlike the Germans, Italians, etc.?

To answer this question, we would have to show not only how the French Revolution guaranteed and consolidated peasant property, but also how peasant production was protected from international competition by customs tariffs. In fact, throughout the nineteenth century the French bourgeoisie, harassed by proletarian movements, sought support from the peasantry, through a tariff policy that prevented the importation of agricultural products, thus preserving small independent production in the countryside and blocking the process of proletarianization. Therefore, French history indicates that the emergence of "surplus population" throughout the process of industrialization is not inexorable.

Another illustrative example concerns how, in Core countries, the miserable living conditions of expressive parts of the population in the post-war period were overcome. The rise in the standard of living of the masses was guaranteed by the generalization of trade unions and by the state's social expenditures and, in this process, the economic dynamism of the "thirty glorious years" was a necessary but not sufficient condition to explain the direction given to the social issue.

The generalization of trade union presence took the determination of wage levels away from the free market, and this was a condition to sustain the increase in workers' real income, accompanying the increases in labor productivity. On the other hand, not even favorable conditions for workers in

6 Pinto, Anibal. Heterogeneidade estrutural e modelo de desenvolvimento recente. In: América Latina – ensaios de interpretação econômica, p. 49.

the labor market were an immediate result of the process of economic growth, as the performance of the public sector was decisive in creating jobs. Thus, public employment reached, in 1975, in Sweden and England, respectively, 21.5% and 29.8% of the economically active population. A quarter or a third of the workers, therefore, were not directly subjected to the capitalist relationship, in a process that does not respond to a purely economic determination, since most of the employees in the public sector are dedicated to social activities.

Finally, income redistribution mechanisms derived from state action were also essential for overcoming poverty. The tax burden in countries like Germany, England and Sweden exceeds 40% of GDP and allows the State to maintain a multitude of social programs, which represent a powerful mechanism for distributing income. To illustrate the importance of this mechanism in overcoming poverty, it would be enough to cite a recent study on England[7], which showed that, in 1975, 4.4% of families lived below the poverty line and that this proportion would reach 30.6% of families if the State's social spending were cut, even not considering the indirect effects of this cut.

Now, these historical examples indicate that the issue of poverty cannot be analyzed simply by considering the specificity of the economic structure. In fact, political processes, the greater or lesser presence of the subaltern social stratum´s interests in the State's policies constitute necessary moments in the analysis of the determinants of poverty.

In view of the above considerations, we must point out certain general features of the Brazilian economy, so that the issue of poverty in the country can be placed. First of all, the massive presence of the poor cannot be explained by a supposedly low level of national development, in a vision dear to the followers of the "cake theory": it would be necessary to grow and then distribute it.

Unlike what happened in most Latin American countries, whose economies are agrarian and less dynamic, Brazilian capitalism showed a remarkable capacity for growth in the post-war period, characterized today by its integrated productive structure, dominated by the manufacturing industry. Now, it is evident that this economic growth could have been accompanied by widespread improvements in the population's living standards and, currently, the country's productive capacity, considered dynamically, would support poverty eradication programs, as demonstrated by recent research conducted by Carlos Lessa[8]. In summary, today in Brazil there is a glaring mismatch between the degree of development of the productive forces and the consumption patterns of a large part of the population.

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7 Beckerman, W. The impact of income maintenance on programmes on poverty. Britain. Ilo-Genebra,1977.

8 Lessa, Carlos. Brasil anos 90: a questão social. São Paulo: Fundap, 1990.

However, if on the one hand, the rapid post-war economic growth produced this mismatch between the capacity to produce material wealth and the misery of the masses, on the other, it was a condition for the improvement in the consumption patterns of expressive portions of the population. The rapid economic growth and the consequent alteration of the social structure enabled the social ascension of portions of the population and, together with other factors, induced a social behavior based on individual competition. In this way, social tensions were cooled, since while the process of economic growth was exclusionary, it opened the way for the improvement of living conditions for part of the population.

Against the background of these general characteristics of the Brazilian economy, the reasons for the reproduction of poverty in the country will be sought from three explanatory axes: the way in which the agrarian issue was addressed, the specificity of the labor market and the nature of social policies considered in their structural-historical traits. And, before situating these three issues, we want to insist that we are dealing here simply with establishing a study guide.

It is a fact that Brazilian agriculture was dynamic, responding to the needs of industrialization and the urbanization process. However, the legacies of colonial slavery are striking: very low living standards of the rural population, archaic forms of domination persist to this day in certain regions and, more importantly, a landholding structure based on the reproduction of large property, even in areas of expansion of the agricultural frontier. Thus, the Brazilian agrarian structure is characterized by its undemocratic character, as despite the existence of small to medium property, large property dominates in the countryside, barring access to land ownership to the majority of the population. As the reproduction of small and medium-sized properties is not totally restricted, the expansion of the frontier allows for some accommodation and social ascension in the countryside, but the restricted and limited dimension of this process does not detract from the undemocratic nature of the recent colonization movement in the country. And the lack of democracy in the social structure of the Brazilian countryside is not only visible due to the predominance of large properties, as unionization processes and other forms of organization of rural workers have always been blocked.

The dominance of the large property; the modernization process driven by government action, which increases labor productivity and reduces the capacity to absorb labor in frontier areas; the survival, in certain areas, of the traditional latifundium; the disarticulation of the latifundium-minifundium relations; the poverty of rural masses; the overexploitation, the ban on unions, the absence of social policies in the countryside – all these factors resulted in an astonishing rural exodus.

This movement resulted in an urbanization process that was characterized by high speed. In three or four decades, the proportion between rural and urban population was inverted. In other words, the country's urbanization took place in a short period, with a speed unparalleled in the history of other nations.

In the United States, slavery and large land ownership were subordinate elements in a structure dominated by small property, while in Brazil large property always prevailed. In the U.S., the process of expansion of the agricultural frontier was vigorously driven by the small property, whereas in Brazil this movement has always been commanded by the large landowners. Thus, it is evident that in the United States, as in France, the capacity of the countryside to retain the population was always greater, which resulted in an urbanization process that evolved more slowly. Finally, however low the standards of living of French peasants or small North American farmers were, they were undoubtedly significantly higher standards than those prevailing to date among the rural population of Brazil.

The fragility of the Brazilian industrial bourgeoisie, which kept the agrarian structure in the country untouched, did not only sacrifice the great mass of the rural population. The speed of migratory processes also determined the formation of an urban labor market that was extremely unfavorable to workers.

As we have already mentioned, the Brazilian industry was highly dynamic in the post-war period. Despite its disappointing behavior in the 1950s, industrial employment grew at very high rates in the 1960s and, in particular, the 1970s. Industrial development was accompanied by a diversification of the structure of urban employment and the modern tertiary sector also rapidly expanded the supply of jobs. In this way, whatever the criterion used, we can characterize the urban labor market in Brazil as extraordinarily dynamic.

However, despite the dynamism of job creation, the speed of the migration process has dumped a contingent of population into the cities that cannot be fully absorbed into the formal capitalist labor market. Thus, large masses of "excess population" accumulate in cities, surviving by receiving scraps of the income generated by the capitalist nucleus.

The very dynamics of capitalist accumulation creates opportunities for small mercantile activities, to which informal workers are dedicated. However, unbridled competition reigns in these activities and, in regions or cities which combine reduced income generated by capitalist activities and many informal workers, poverty is manifested in this social stratum. On the other hand, the participation of wage labor is growing and, increasingly, urban poverty is associated with low wages. That is to say, wage-earners, and not the self-employed in the informal market, predominate in the mass of the urban poor.

It is evident that an unlimited supply of work is a condition for keeping wages at low levels. But in capitalism, to a greater or lesser degree, the labor market is always unfavorable to workers and the reasons for low wages in Brazil must be sought both in the absence or weakness of the trade union movement, as well as in the government's wage policies. The Brazilian union movement has always been fragile and, after 1964, conservative legislation practically proscribed union action.

In periods of economic expansion, an active union movement in large companies would have raised the wages of broad categories of workers, at a pace that would accompany increases in productivity.

Thus, in the post-war period, while in Brazil the state coopted the union movement or outlawed it, in Europe union presence became widespread, which was a condition for raising wages.

Wage policy, on the other hand, after 1964, clearly moved towards wage tightening. In fact, in the Brazilian urban environment there was a reproduction of economic-productive heterogeneity, in which low wages are a condition and a result of the permanence of the backwardness of some and the super profits of others, in addition to making room for a blatant wage differentiation.

From another angle – we insist again – the rapid economic growth enabled remarkable social mobility. Many jobs typical of the middle class have been created, small and medium-sized companies proliferate, of which a portion operates with large profits, and another has their living conditions guaranteed by low wages and tax evasion. And, among the self-employed in the informal sector, some achieved a significant increase in their earnings. These opportunities opened by economic growth encourage individualistic behavior, weakening forms of collective action.

Finally, the third point to be considered concerns social policies. While in Europe high taxation and state social programs functioned as a powerful income distribution mechanism, the Brazilian welfare state's face is distorted and ineffective.

If, from a historical perspective, the Brazilian State did little to act in the social field, after 1964 it acted in a limited and non-compensatory way. In a limited way, because the effective tax collection in the country is reduced, and also because the resources were preferentially directed to meet and stimulate economic growth and not to the social area.

Thus, social policies were financed mainly through social contributions paid by the workers themselves. Hence their non-compensatory character, as they validate the primary income distribution structure, covering, in an extreme limited way, the groups (or areas) of lower income.

And, in the field of State social spending, it is necessary to remember that the definition and implementation of policies were conditioned by private interests and rules of appropriation. Not only to bureaucratic, corporate and clientelistic interests, but also serving the private hospital network, input and equipment suppliers, contractors, urban landowners, financial agents, etc.

In short, the reproduction of poverty in the country is the mirror of a conservative society and a conservative State, dominated by private interests and by a class coalition that excludes the presence of subordinate social strata.

CHAPTER 8

LAND REFORM AND INCOME DISTRIBUTION[1]

Ademar Ribeiro Romeiro[2]

Introduction

This paper aims to reflect on the historical importance of rural employment in defining the profile of income distribution in industrializing economies. In our opinion, this issue has been addressed in an unsatisfactory manner by most analysts from different theoretical currents. For example, rural exodus results naturally from expanding employment opportunities in the urban-industrial sector for neoclassical economists. They assume that, at the existing techniques, there is no unemployment in the rural sector at the beginning of the industrialization process. Thus, for rural workers to migrate, urban wages must rise above rural wages. The departure of rural workers, in turn, raises rural wages, stimulating agricultural modernization. As we will see, this analytical framework corresponds, in general terms, to what happened in the leading capitalist countries. In those countries, the factors attracting workers to the cities were indeed more important than the factors that could have forced them to leave the countryside.

Nevertheless, neoclassical economists did not consider that this was due to several political-institutional factors ensuring widespread access to land. This methodological approach of neoclassical economists led them to make a series of mistakes when analyzing the case of late industrialized countries, such as Brazil. They explained the rural exodus in those countries similarly, despite the growing poverty in large urban centers.

The structuralists, in turn, understood the difference regarding underdevelopment countries in Latin America. They saw unemployment and income concentration as the result of specific structural problems of those economies. The first structural specificity was a surplus of labor in the countryside living at

1 Paper presented at the XVIII Brazilian Congress of Rural Economics and Sociology, (SC), from July 22 to 27, 1990. Published by the *Quinzena* newsletter of Centro Pastoral Vergueiro, on January 15, 1992, n. 130.

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the subsistence level. In other words, rural labor was not effectively employed and thus could migrate to the urban-industrial sector without affecting rural wages. It would be enough for the rural exodus to occur slightly higher wages in the urban sector, resulting in an "unlimited supply" of labor for the urban-industrial sector. Thus, as long as this labor surplus was not absorbed, real wages would remain constant as productivity increased and profits rose. Greater profitability, in turn, would accelerate the process of capital accumulation, eventually leading to the absorption of this labor surplus and rising real wages. However, because of another structural specificity of these economies, the absorption of the labor surplus will be delayed, or even never be done, as they depend on labor-saving machinery and equipment imported from developed countries. It follows, thus, as a necessary condition for raising wages, the development of the domestic industry of labor-using capital goods.

There are two problems with this structuralist analysis. First, they did not consider the fact that rural labor surplus might result from large landowners' actions preventing the access of rural workers to land. Second, nationalizing the manufacturing capital goods does not significantly alter the labor/capital ratio. Overall, technical progress that improves equipment performance (greater energy efficiency, better product quality) is not readily dissociated from increased labor productivity. There is little room for maneuver, not to mention that despite being manufactured domestically, the sources of technological innovation would remain largely foreign. Agriculture is the only sector, at that time, with technological flexibility in terms of absorbing labor. However, for the structuralists, the hypothesis of structural labor surplus in the countryside prevented them from seeing the agrarian reform transforming the agricultural sector into an essential source of employment.

Finally, in classical Marxist analyses, the disintegration of the traditional peasantry was seen as an unavoidable consequence of the penetration of capitalism in the countryside. For them, the resulting rural exodus was the ultimate expression of the so-called primitive accumulation of capital, which is nothing more than the expropriation of small farmers and their transformation into workers with nothing to sell other than their labor. Compared to the expansion of employment opportunities in the urban-industrial sector, the greater speed of this process is part of the capitalist logic of creating a permanent surplus of labor (reserve army) to keep wages low. As we shall see, though, history shows that the experience of developed countries does not fit into this type of analysis. However, as the recent experience of many Latin American countries seemed to corroborate it, this has led many analysts to entertain a certain fatalism, in the sense that this would be an inevitable process to which all capitalist economies were subject. As long as the regime is capitalist, there will be no solution to the observed substantial income inequalities.

This paper comprises two parts. Through a historical-comparative analysis, the first part shows that the agricultural sector played a decisive role in countries where the growth process involved reasonable income distribution by ensuring a rhythm of rural exodus compatible with the expansion of job opportunities in the urban-industrial sector. The goal of the second part is to show that in countries like Brazil, it was not only possible but essential for the agricultural sector to play a similar role of adjustment variable in the balance between labor supply and demand in the economy.

Agriculture and income distribution: a historical approach

The United States and Japan

The example of the two largest and most developed capitalist nations, the United States and Japan, is highly illustrative. They presented the opposite situation regarding land settlement and agricultural modernization but had in common having guaranteed widespread access to land to those who needed it for their survival.

In the United States, where the slaveholding oligarchies were defeated on the battlefield, the elites in the North, descending from immigrants, were aware they were building a nation of freedoms. The 1862 "Homestead Act" made it clear, as it purported to legally guarantee the opening of the West to the great waves of immigrants who were beginning to flow in from Europe. It is extremely revealing to note that a little earlier, the slaveholding elites in Brazil, on the contrary, were seeking to close the agricultural frontier through the 1850 "Land Law." This law provided that unoccupied public land could no longer be freely settled but required the payment of a sum high enough to prevent its access by European immigrants, who were starting to arrive to replace slave labor on the coffee plantations.

On arriving in the United States, immigrants had the option between seeking employment in the urban-industrial sector or "going west" to settle in the agricultural frontier[3]. Of course, settling in the West was not as simple as depicted in many movies. A certain amount of money was needed to cover travel and settlement expenses, and the struggle for effective land tenure was beyond the capacity of many pioneer families. The balance, however, was

3 Habakkuk, H. J. (1962). *American and British technology in the nineteenth century.* Cambridge University Press.

highly positive. The dynamic role played by the vast agricultural sector made up of family farms in the economic development of the US is well known. A noteworthy fact is the permanent shortage of labor caused by this opening of the agricultural frontier. Wages paid in the urban-industrial sector tended to rise. There are studies suggesting this was one of the main factors behind the greater technological dynamism observed in US production activities in general, and the industrial sector in particular, compared to Europe. Faced with this permanent pressure from labor costs, US businessmen sought to innovate, introducing new production methods that increased labor productivity.

In the agricultural sector, from the outset, the relative scarcity of labor and the great abundance of land encouraged the introduction of all kinds of innovations that might increase the working capacity of the American farmer. Thus, the prevalent ratio of land/labor spurred an early process of agricultural mechanization. Therefore, technological dynamism spread out overall production sectors, one of the main drivers being the relative scarcity of labor caused by free access to land.

In this situation, rural exodus followed a balanced pattern, mainly resulting from increased employment opportunities in the urban-industrial sector. In other words, we can say that in the US, the factors of attraction to the cities prevailed over the factors of eviction from the countryside. People leave the countryside for the city not because landowners evict them or because they can no longer survive. The city offers them a wide range of better-paid professional options, besides other attractions related to urban lifestyles, such as cultural activities that do not exist in the countryside.

In Japan, the elites who took power with the Meiji restoration in 1862 are also clearly aware of the challenges and risks faced by Japan at that moment. However, it was not about building a nation like the US, but about modernizing one that already existed and felt threatened by the expanding West. Japan was the only Asian nation to successfully face the scientific and technological challenge of the West at the time. Absorbing Western scientific and technological knowledge was an indispensable condition, which could be achieved in two different ways: a) incorporated in imported machinery and equipment; b) through creating research institutions capable of absorbing fundamental scientific and technological principles. The predominance of one way or another implied the technological and economic dependence or independence of a nation. Moreover, in the case of Japan, it also had political implications: to be subjected or not to the colonial yoke.

The modernization and economic development had to deal with the vast agricultural sector, which occupied the majority of the economically active populations. Regarding this sector, the West offered two different styles of modernization: the European mode, aimed mainly at increasing land yields, and the American model, which focused on increasing labor productivity through the extensive mechanization of agricultural operations. In addition, there was a major institutional innovation: agricultural experiment stations. This institutional innovation emerged in Germany in the mid-nineteenth century and spread rapidly across the European continent. The Japanese quickly absorbed the German model of agricultural research and imported US agricultural machinery and equipment. However, it was clear that using the latter would have a devastating impact on the production structure of Japanese agriculture, based on small farms. The result would have been something close to what happened in Brazil and other Latin American countries: the mass exodus of peasants towards an urban-industrial sector that did not yet offer enough opportunities for employment, housing, and urban facilities in general. Thus, the Japanese rejected the wholesale import of the American model of agricultural mechanization in favor of the domestic development of agricultural machinery and equipment adapted to the specificities of the nation's production structure. The agricultural development case in Japan shows the predominance of overall social rationality over incidental microeconomic rationality at the individual farm level. Incidental because, for Japanese landowners, even if it might be profitable to expel the laborers and extensively mechanize their crops, this was out of the question, as a traditional community bond ('feudal' like) united them with the peasant populations. Compared to the capitalist system, one of the most striking features of the feudal system concerns precisely the personal ties that unite the dominant and dominated classes in a relationship of commitment that implies reciprocal rights and duties and governs the possession and use of existing land resources.

The golden rule of traditional community relationships in Japan was job security. The Japanese elites faced the need to modernize their agriculture in such a *way* as to preserve employment rates. There was also an awareness that keeping high employment rates should not reduce agricultural labor productivity. The expanding urban-industrial sector needed increasing amounts of agricultural raw materials and food. Thus, the increase in employment in the agricultural sector should pair with an increase in labor productivity. Let us see *how* this was possible.

Japanese agriculture: technical progress and welfare[4]

Since the beginning of the Meiji era, rice production underwent an almost continuous improvement in plant varieties and agricultural inputs. Initially, improving rice varieties was mainly carried out by spreading the best quality seeds from each location. The national unification with the end of the feudal system facilitated it. By the end of that phase, the most productive seeds, resistant to pests and low temperatures, were being used in most of the country's rice-growing areas. From then on, seeds improved locally by farmers started being replaced by those developed scientifically in experiment stations.

Regarding fertilizers, initially, farmers used organic products, such as fish meal and oleaginous pies; then, chemical fertilizers were imported but used together with locally produced organic fertilizers. Improved traditional agricultural implements were widely used alongside new mechanical equipment. However, to maintain employment levels, the mechanization of the field operations was delayed. A priority was given to the mechanization of threshing, grinding, irrigation, and drainage operations. In turn, the mechanization of field operations, in itself labor-saving, was designed to increase land use by introducing a second crop. That was possible because it made agricultural operations faster, more precise, and better distributed in time, removing seasonal peaks of labor demand. Also noteworthy was the development of rural industries (mainly sericulture). The order followed in the various steps of the mechanization process of the leading rice crop (irrigation, threshing, processing, plan health protection, plowing, harrowing, seedling transplantation, and harvesting) was consciously designed to allocate all available labor in the agricultural sector efficiently. Considerable emphasis was given on collective irrigation and drainage works carried out at the local community level, with more significant works performed by the State only in the final stages of the modernization process.

Thus, when the use of labor-saving machinery and mechanical equipment began, there was a drop in the amount of work per hectare in individual crops but an increase in overall agricultural employment. The number of person-days per hectare in rice production regularly drops from 278 in 1874 to 214 in 1960. From that date onwards there is a sharp drop to around 146 person-days by 1970. Simultaneously, the amount of work in the agricultural sector increases from 353 person-days per hectare of arable land, in 1874, to its pick of 398 in

4 This section is based on the excellent work by S. Ischikawa: *Essays on technology, employment and institutions in economic development: comparative Asian experience.* Tokyo, Kinokunyia Company Ltd., 1981.

1910; then, it starts falling gradually to 370 by 1960, when a sharp fall was also observed, accompanying the drop in rice production, to 235 by 1970.

What was remarkable about Japanese society is that despite the advance of the market economy, some of the fundamental elements of traditional community relationships remained in place, generating a decisive dynamic force of an agriculture modernization process that was vigorous yet balanced regarding the preservation of employment levels. That prevented an uncontrolled rural exodus and the consequent degradation of living conditions among the population. Thanks to the permanence of these traditional community relationships, Japan could absorb agricultural science and technology imported from the West and adapt them to its natural specificities and availability of human resources. Thus, we can say that rural exodus in Japan was perfectly balanced, with the factors of attraction to the cities prevailing over the factors of eviction from the countryside, as in the United States.

The spirit of these traditional community relationships is present till now in the organization of large industrial corporations where, as is well known, guaranteed employment matches a faithful dedication of workers. Behind the survival of the community relationships lies the cultural profile of a people with a strong sense of national identity, endowed with responsible elites well aware of the challenges the Japanese nation faced. Challenges that could not be faced if the living conditions and level of education of the population degrade.

The Asian "tigers"[5]

The case of the newly industrialized countries in the Far East, the so-called Asian "tigers" (South Korea, Taiwan, Singapore, and Hong Kong), is similar in many ways to what happened in Japan. In all those countries, there was a straightforward national project of inclusive socio-economic development. The ruling elites have been able to mobilize the populations of their respective countries around national development programs in which everyone took pride. The critical element of this mobilization was the general improvement of the population's living conditions. The distribution of the benefits of economic progress was paramount. A dynamic process of income distribution followed the economic growth, which is only possible where there are abundant opportunities for employment and education. One of the

5 On the reasons for the success of these economies, see the interesting papers written by the Brazilian ambassador in Singapore, Amaury Porto de Oliveira. This section is based on the following texts: "The North Pacific in the Industrial Transition," September 1987, and "Recipe for New Industrial Country," March 1988.

features of these countries was precisely the special care taken with education and technical training.

In South Korea and Taiwan, where the bulk of the economically active population concentrated in agriculture at the beginning of the industrialization process, land reform prevented uncontrolled rural exodus from compromising the progressive improvement in the population's quality of life. Their governments planned and executed land reforms with the support of the United States, without pressure from the peasants. By around 1970, the governments of Taipei and Seoul had achieved their goals. Modern and efficient agriculture had emerged, run by small landowners. Farmers had turned into prosperous consumers with a substantial savings capacity (20% in Taiwan).

The case of Taiwan

The Japanese occupied Taiwan for almost 60 years, which emerged from the war with its infrastructure heavily compromised by US bombing. Poor peasants represented two-thirds of the population, subjected to highly unfavorable lease and partnership contracts. Most agricultural workers were sharecroppers, often with contracts that lasted less than a year and required advance payment of at least 50% of the estimated income from the crop, whatever the actual income might be. This situation reveals that the country's rural elites did not commit to the people in general due to colonial rule (and for cultural reasons of their own). This fact means that left to its fate after the war, Taiwan probably would not have followed the path of economic development it ultimately took.

However, in 1949, Chiang Kai-shek landed on the island at the head of 2 million fugitives from the takeover of mainland China by the Chinese Communist Party. Chiang's party, Kuomintang, then took power. It was a reformist party that had promoted the republican revolution in China, having no connection with or commitment to Taiwan's landlords. Quite the contrary, it suited them to break the strength of this rural oligarchy. In addition, the party had the support of the US, which, in the case of land reform, actively cooperated through the Joint Commission on Rural Reconstruction (JCRR), created by the US Congress. JCRR played a decisive role in stimulating an integrated agricultural development process with the significant participation of individual farmers.

Land reform was carried out in three stages. The first stage focused on reducing sharecropping rates and on affording greater security to partnership contracts. The second involved the subdivision and sale of public land suitable for cultivation. Finally, in the third stage, under the motto "land for those who work," the great estates were carved up, with the large landowners receiving monetary compensation from the sale of public land.

By 1953 the land reform was concluded. At the same time, a great effort was made to modernize agricultural production, but in a form compatible with a structure dominated by small farms. Food production started exceeding population growth, raising the population's dietary standards. For 30 years, from 1952 to 1982, for population growth of around 2.5% per year, food production grew 3.6% on average. The daily intake of calories rose from 2,078 to 2,750 calories, and that of proteins leaped from 49 to 77 grams.

The first four-year industrialization plan was launched (1953-1956) only after the conclusion of the land reform. It is worth noting that small, relatively labor-intensive industries dominated the early stages of the industrialization process. In summary, Taiwan was able to grow the economy rapidly while improving the income distribution thanks to the substantial expansion of employment opportunities. The starting point and critical element of the expansion of employment opportunities was the agrarian reform which granted the peasants access to land. It is quite revealing to compare the experiences of these Asian tigers to those of other Asian countries, which modernized their respective agricultures as of the 1960s within the so-called "green revolution."

Green revolution: production and unemployment

Traditional community relationships also existed in many regions of the south and southeast, where the so-called green revolution took place. There existed traditional arrangements between landowners and landless workers in some of these regions to ensure many rules benefiting the formers. In others, although such community arrangements did not exist to a significant degree, there was an explicit communal agreement guaranteeing the hiring of landless workers for seasonal work. In Indonesia, for example, these traditional relationships of commitment to maintaining employment levels had led to what Geertz[6] called "shared poverty." Due to demographic pressure and the lack of innovations to significantly increase agricultural production and employment opportunities, the existing resources were gradually redistributed among the growing number of mouths and arms.

The green revolution brought about significant changes in these traditional communal employment arrangements. First, unlike the case of Japan, scientific and technological innovations were introduced mainly as part of imported (and subsidized by local governments) agricultural machinery and

6 Geertz, C. (1963). *Agricultural involution. The process of ecological change in Indonesia.* University of California Press.

inputs. The number of permanent workers decreased with the use of tractors. A market system in which traders purchased rice before harvesting replaced the communal right of villagers to participate in harvesting. These traders, in turn, introduced technical harvesting innovations that reduced the amount of labor required, causing unemployment. Therefore, unlike Japan and the "Asian tigers", an increase in agricultural production was accompanied by a reduction in employment opportunities, configuring a process of exclusive economic growth.

The question to be asked is why traditional community relationships were not strong enough in these countries, as in Japan, to become a dynamic force in the process of agricultural modernization driven by the quest for community welfare. The answer to this question may lie in the colonial past of those countries. While the Japanese agricultural community became a complementary part of an expanding national industrial system, agricultural communities like the Javanese, for example, became a complementary part of an agro-industrial structure under Dutch colonial control. Moreover, unlike what happened in Korea and Taiwan, the end of the colonial yoke did not mean the end of the political power of traditional rural oligarchies.

Colonial dominance for sure had a significant impact on traditional community relationships between elites and peasant populations. In the case of Indonesia, the colonial power co-opted the local elites. It transformed the traditional right of land tenure, which imposed specific duties on the elites regarding rural workers, into the right of private appropriation of land, exempt from an overarching responsibility towards the peasant population in general.

Thus, the former traditional relationships degraded into patronage-based relationships similar to those observed in Latin American countries. The maintenance of a significant number of workers ceased to be a moral obligation; then on, it will last as long as it suits the interests of the large landowners. Before the new opportunities to earn money bought by Green Revolution, they did not hesitate to break these patronage-based commitments as the need for workers reduced. As a result, unemployment and rural exodus rose, albeit to a lesser degree than Latin American countries.

The case of Brazil

The characteristics of over four centuries of agricultural development in Brazil can be summarized as follows: on the one hand, the commercial success of export crops and, on the other, relative scarcity of food, predatory exploitation of nature and labor, lack of access to land and employment to free peasants, in a country with the largest potential agricultural area in the world (four times the Chinese agricultural land). The export crops monopolized all attention and care, with food production consistently relegated. Part of the food came from within the large estates for the subsistence of their workforce. Another part came from small farms located in border areas between the large estates, where lived a large population forced to supplement their income with work on the estates, given the small area available to them. Finally, there was food production in the constantly expanding agricultural frontier. Furthermore, one must consider the extensive cattle breeding ranches, constituting a decisive land concentration and monopoly element.

In summary, food production occupied residual areas not used for export crops (either within or on the fringes of large estates) or areas not yet under the reach of the more powerful interests in the agricultural frontier. The consequence was the precarious tenure conditions of the land used for food production, causing unstable production and chronic supply problems observed since the 17th century. Such problems were a constant concern of the Portuguese crown, which sought to ensure the supply of cities and towns through legislation: the provision dated April 24, 1642, which provided the mandatory planting of cassava (the "earth bread") in an area equivalent to that used for export crops; the order dated February 25, 1688, which obliged farmers of the Recôncavo Baiano region to plant 500 cassava pits per slave in their service; and others such as the Royal Charter of 1722, which always faced strong opposition from large landowners[7]. This precarious situation of the food production structure, which consisted mainly of small farms, made life easier for intermediaries, whose activities persisted throughout the country's history, keeping prices low for farmers and high for consumers.

With the decline of slavery, the ruling elites tried to ensure control of the land, mainly to prevent the immigrants, who were beginning to arrive in large waves, from establishing themselves as independent farmers. In this context, the 1859 "Land Law" emerged, providing that unoccupied public land could no longer be freely settled but required the payment of a certain amount of money. Except for specific regions in the far south of Brazil, where the State promoted immigration for strategic populating reasons, the agrarian elites took the lead in promoting immigration to solve the labor shortage problem with the end of slavery. A share-cropping system was initially attempted, with immigrants reimbursing landowners for travel and occupation expenses. This system, which amounted to a kind of disguised slavery, failed due to the immigrants' resistance to accepting such conditions and the highly negative

7 See Linhares, M. Y. & Teixeira, F. L. (1981). *História da agricultura brasileira. Combates e controvérsias.* Brasiliense.

image it gave the country in Europe, where the German government banned emigration to Brazil at one point.

The solution adopted to attract immigrants and improve the image abroad of the last country in the Americas to end slavery was to exempt immigrants from refunding travel and occupation costs, with travel tickets financed by the Brazilian government. Furthermore, the share-cropping system gave way to a new system called "**colonato**'. In this new system, there was a payment in cash - a fixed part based on the number of coffee trees tended by each family and a variable sum according to harvest results; in addition, the '**colonos**' (settlers) had access to a piece of land for subsistence crops. Moreover, they could sell the surplus in the market. In other regions of the country where immigration was less significant, other arrangements between large landowners and landless rural workers arose (usually some share-cropping arrangements). The paternalistic relationship ensured to the former a cheap and submissive labor force.

It worth mention that the relative improvement in the living conditions of rural workers under the **colonato** system explains the vigorous process of agricultural diversification that occurred alongside the expansion of coffee crops, a key element in the growth of the economy of the State of São Paulo. From the late 1920s on, with the crisis in exports (in 1929), the diversification of Brazilian agriculture, mainly in São Paulo, gained even more momentum. Part of the land previously devoted to growing export crops, mainly coffee, was used to produce agricultural raw materials for the rapidly expanding urban-industrial market. However, the land ownership structure remained highly concentrated.

The intense industrial growth in the fifties ended with an economic crisis. The industrial growth rate fell sharply. It was a period market marked by imbalances and rising inflation. A great debate took place at the time about the causes of these problems. The concentrated land ownership structure was considered one of the causes of the imbalances and inflationary pressures and an obstacle to the continuity of economic growth. The large estates would be not dynamic enough to allow the agricultural sector to play the same role in the development process as was the case in developed nations, especially regarding the production of cheap food, a necessary condition to reduce the cost of reproduction of the urban-industrial workforce. Land reform was seen as an indispensable prerequisite for the expansion of modern capitalist agriculture.

During this economic crisis, which has developed into a political-institutional crisis, the agricultural sector will undergo substantial changes in terms of labor relations. From the late 1950s, the traditional patronage system of domination started suffering the impact of a twofold movement: on the one hand, the growing pressure from reformist social movements in national politics, whose main demands included land reform; on the other, the emergence and rapid spread of trade unions of small farmers and rural workers. The State's response to the pressure from these movements was the enactment of the Rural Worker Statute (Law 4214, dated March 2, 1963), which extended to rural workers the social legislation that already benefited urban workers. At the same time, the State tried to bring the rural unions under control (and with no right to strike), as was the case with urban unions.

The need for a solution to the Brazilian land problem, which was so clear for the more lucid and responsible elites, was also acknowledged by some segments of the conservative ruling classes. Under the impact of the Cuban Revolution, the Kennedy administration started viewing land reform as an effective instrument of socioeconomic reform capable of dampening the communist revolutionary potential in Latin America. The instrument devised to promote it was the Alliance for Progress. The new military government, which took power after the 1964 coup, will align with the US in this matter and will immediately enact the Land Statute (April, 1964), proposing much broader reforms.

Thus, a new consensus emerged about the causes of the unfair and wretched living conditions of rural workers. The lack of access to land due to unbridled speculation that laid massive idle amounts of land was to blame for it. This consensus, composed of the increased political awareness of the rural workers, started posing a severe threat to the traditional interests of the rural oligarchy, which viewed the private ownership of land as unconditional. In other words, like a personal object, land can be used or not, conserved or destroyed; like jewelry, it can be kept or used as a guarantee to access new sources of capital expansion. The use of land as a speculative asset has historically been one of the most striking features of the Brazilian countryside. The capital invested in the purchase of land will be appreciated regardless of its productive use. Moreover, the subsidized credit policies were based on bare land.

Faced with this tense situation, which persisted due to the threat of land reform throughout the first years after the military coup, the rural oligarchies did not waste time. The first step was the wholesale eviction of rural workers residing on the estates and replacing their food crops mainly with extensive pastures, which was the traditional form of land control with few workers. Rural workers living on the farms became a liability to the liquidity of real estate operations, as they had gained a certain level of legal protection regarding their dismissal (severance pay, reimbursement for improvements, and other benefits).

Part of the evicted workers, as known, will become low wages mobile workers ("*boias-frias*") without contracts. Another part will migrate to the cities due to the lack of job opportunities in the countryside, as a rapid introduction of labor-saving techniques followed this eviction process. For big farmers, the use of mobile workers implied insurmountable problems of control and organization of the work process. In agriculture, due to its natural specificities, it is impossible to organize and control the work process of numerous salaried employees, as in industry. The extension of the crop fields, the seasonal and non-sequential nature of operations, and other specificities of agricultural production make labor supervision difficult and costly. In the previous scheme, the paternalistic relationships with resident workers ensured a submissive workforce that performed agricultural work satisfactorily, without significant problems of control and supervision.

Therefore, with the eviction of resident workers, landowners become interested in reducing as much as possible their dependence on mobile workers. They will be employed only in agricultural operations that are hard to mechanize, such as harvesting certain crops. In turn, these objective needs of large landowners to save labor, reducing the employment of mobile workers, matched the interests of the newly installed equipment industry and the public opinion about the need to raise the technological level of Brazilian agriculture. Thus, the deep-set and reactionary motivations that led large landowners to modernize their plantations were transfigured, in the eyes of society, into progressive modernizing motivations strongly supported by the State through all sorts of subsidies and incentives.

In short, history has shown that the concentrated land ownership structure was not an obstacle to the continuation of the process of economic growth. Instead, it was an obstacle to socio-economic development that raises the population's quality of life in general. The production of agricultural raw materials for the industrial sector grew satisfactorily, as did food production, the latter mainly due to the expansion of the agricultural frontier till the mid-seventies.

That does not mean that food supply problems in urban areas disappeared since food production continued in large part to be the responsibility of small farmers in precarious conditions of land tenure, lack of technology, and access to loans. This food production structure facilitated the work of intermediaries, who kept prices high for consumers and low for the small farmers, contributing to inflationary pressures, leading to frequent control of food prices in periods of failed harvests. However, high food prices did not raise industrial production costs but instead reduced workers' quality of life. They had to spend a more significant portion of their wages on a meager diet, as the wages continued to suffer the lowering pressure of a rural exodus that exceeded the capacity of the urban-industrial sector to generate employment. In this sense, agriculture projected its image on the urban-industrial sector regarding its highly concentrated pattern of the income distribution.

Final Remarks

The radically different agricultural development experiences in the United States and Japan had in common a guaranteed access to land for the rural workers. In European countries, which had a strong peasant tradition, access to land was also generally guaranteed. In more demographically dynamic countries such as Italy and Germany, immigration to America prevented uncontrolled rural exodus from compromising their transformation into economically and socially developed nations. More recently, the example of the so-called Asian "tigers" follows the same path. In the so-called underdeveloped countries, a common feature of countries as distinct as Brazil and Indonesia is that the "land issue" has not been resolved. In fact, it has been satisfactorily resolved regarding the increase in agricultural production required to meet the demands of the urban-industrial sector. However, such demands excluded the most basic needs of a large part of the population. In Brazil, the increase in agricultural production, with its famous "super harvests," which several governments sought to advertise as outstanding achievements, did not improve the Brazilian population's food standard.

Therein lies the major problem that the so-called "conservative modernization" champions cannot or do not want to see. The increase in agricultural production can be a necessary condition for economic growth. However, it is not a sufficient one for socioeconomic development, understood as a process that raises the population's quality of life. Amartya Sen showed, in a remarkable study[8], that even in the great famines that occurred in this century in different regions of the world, the absolute reduction in food supply was not the cause of the catastrophe. In Bengal, in the critical year of 1943, rice production had been the highest in its entire history until then. In Ethiopia in 1972/1973, food production had fallen by only 7%. In Bangladesh in 1974, when the most significant number of people died, rice per capita was the highest in many years. In all these cases, people died because they did not have enough money to buy food. The loss of income was due to unemployment, caused by initial crop failures, high food prices generated by speculators, and other problems in distribution and marketing.

These dramatic examples adequately illustrate the aspect we wish to emphasize related to the role played by the agricultural sector in the process of economic development. As the primary source of employment at the beginning of this process, it tends to define the income distribution profile of the economy. The improvement in the living conditions of the working class in developed countries, before population growth showed a sharp decline, was only possible because there

8 Sen, A. (1981). *Poverty and famines. An essay on entitlements and deprivation.* Oxford: Clarendon Press.

was a relative shortage of labor caused by widespread access to land. The pace of expansion of job opportunities in the urban-industrial sector, no matter how great, would not have been able to absorb the natural increase of the workforce added to an uncontrolled flow of rural labor expelled from the countryside.

The role of the land reform in Brazil today (1990)

Since the end of slavery, Brazil has lost several historic opportunities to resolve its land issue, ensuring the rural population widespread access to land. Unfortunately, the ruling elites, traditionally greed and irresponsible, have always managed to block the attempts to solve the problem proposed by a lucid and responsible minority, who perceived the long-term consequences of the brutal concentration of land resources in the hands of a tiny minority. Such consequences are dramatically experienced nowadays, especially by the population of large metropolitan areas, in the form of urban chaos, in a country of 80 million (two-thirds of the population) malnourished and semi-literate individuals. The historical neglect of elementary education is the flip side of the coin of the oblivious indifference of the ruling elites towards the Brazilian people. At the height of the riches of the coffee period in São Paulo, the attention of visiting scholars noted the low level of public investment in primary education.

The current return to democracy in Brazil has shown that, despite the economic and cultural marginalization, Brazilian people can self-organize and fight with increasing effectiveness for their rights. However, it is precisely in the land reform issue where the improvements do not show. The country still has a quarter of its workforce in the rural sector. So, it is vital to make an effort to improve rural employment. Otherwise, the social movements will have serious difficulties translating the newly gained rights into practical betterment in quality of life since real wages only rise sustainably in the medium and long term if there is a relative shortage of labor. Data on the evolution of wages in the US economy since the beginning of the century show that wages fluctuate according to the economy's cyclical movement, with or without organized and strong unions; that is, if unemployment rises, average wages fall and vice versa.

Table 1 – Relative share of the economically active rural population *in the total workforce*

Years						
1940	***1950***	***1960***	***1970***	***1980***	***1985***	***1990***
66.7	60.5	54.5	44.6	30.1	28.5	24.0

Source: IBGE.

Table 1 shows the evolution of rural exodus in Brazil since 1940. One notes the acceleration of this process in the 1960s and, especially, 1970s. In the latter decade, the strong acceleration of rural exodus is explained by the combination of, on the one hand, increased eviction linked to changes in labor relations in the countryside and, on the other, expansion of employment opportunities in the urban-industrial sector resulting from strong economic growth. In the following decade, the sudden reduction of rural exodus draws attention. It was a decade when the Brazilian economy went through a crisis, with the consequent reduction in employment opportunities, which discouraged migration to cities. However, if the factors of attraction to the urban-industrial sector diminished, it is worth asking what happened regarding the factors of eviction from the countryside.

It must be clear that survival in rural areas is impossible without employment. Without jobs, rural workers will migrate to cities regardless of the employment opportunities they hope to find. Besides unemployment, another factor of displacement from the countryside is quality of life. In cities, the quality of life of the impoverished and underemployed population can nevertheless be better than in the countryside. Rural life meant the hard work from sunrise to sunset, plus the lack of medical care and schooling for their children. Additionally, an important part of the rural workers has no protection by the State against the violence from land grabbers.

As shown in Table 2 below, in the first half of the 1980s, the growth rate of rural employment was two and a half times higher than the previous period, which is a significant reversal of the trend observed since the mid-1960s. It also shows strong growth in agricultural production compared to the previous decade, despite the negative growth rate of the prices received by the farmers[9], increased yield per hectare, and negative growth rate of the agricultural area by an employed person. According to Rezende (1988)[10],[9] the share of food production (beans, corn, cassava) in agricultural production in the 1980s was significant. Domestically, a better policy of guaranteed minimum prices compensated for the unfavorable evolution of the prices.

Table 2 – Annual growth rate (%)

Period	1975-1980	1980-1985
Prices received by farmers	3.29	-0.52
Physical product	1.82	3.01
Yield by area	-0.58	2.36
Agricultural area by employed person	1.60	-1.28
Employed population	0.79	1.92

Source: Dias, G. L. S. “O setor agrícola e a crise de ajustamento da economia brasileira”, XVI National Economics Meeting, Anpec, Belo Horizonte, December 1988.

9 In the case of export products, the problem was the unfavorable evolution of commodity markets in the 1980s. In the case of the domestic market, higher interest rates forced the reduction of the crops stocked.

10 Rezende, G. C. (1988). “Crise externa e agricultura: Brasil nos anos 80”. *Fase*.

Besides a more consistent minimum price policy as an important explanatory factor for the excellent performance of food production, one must also consider the opportunities created for small farmers as an indirect result of the economic crisis and the uncertainties regarding the merely speculative use of land. In the previous decade, small farmers lacked access to subsidized agricultural credit that benefitted large landowners. In addition, easy credit for them gave rise to all sorts of irregularities, including its use to purchase land, which fueled land speculation. Small farmers found themselves on the ropes, facing growing difficulties, leading many to sell their property.

In the 1980s, the growing deficit in public expenditures led the government to cut the subsidies of rural credit. It fell from 38% in 1980 to 2.3% in 1985, due to the introduction of indexation as of 1984. The subsidy rate rose once more in 1986 with the Cruzado Plan, to disappear again from the second half of 1987.

The sharp reduction in the availability of subsidized rural negatively impacted the land prices. They fluctuated intensely and were negative between 1981 and 1983 and in 1987. This fact discouraged the sale of land by small farmers and opened more opportunities for landless rural workers. At the same time, the present decade witnessed an intense reorganization of civil society, followed by the resurgence of the land issue and the strengthening of rural unionism. The risk of land speculation with idle land increased. Without credit and facing growing difficulties with labor, in addition to the threat of invasion, undercapitalized large landowners began to consider land concession, under various forms of contract, a good option to increase the estate's productive area. The 1985 census data on the increase in partnership, lease, and occupation would confirm this view. For capitalized large landowners, the most attractive option was the investment in planted pastures for more intensive cattle breeding, which also positively impacted rural employment. In the 1960s, having resident workers was seen as a threat. In the 1980s, the situation seemed to reverse: not having resident labor was a reason for concern.

In short, in the 1980s, several factors contributed to reverse the previous trend of displacing rural workers. Notably, the end of subsidized rural credit and the disincentive to extensive cattle raising, on the one hand, and better organization and capacity for action of rural workers, on the other, seem to have seriously affected the possibility of speculative use of agricultural land. That increased the opportunities of access to land by rural workers. What we have just seen reveals the excellent job creation potential of Brazilian agriculture. To this end, it is enough to reduce land speculation and keep open access to land by rural workers.

It is worth asking what role agricultural employment could play in Brazilian economic development in the next 15 years. Table 3 shows us some interesting projections made by the Brazilian Development Bank (BNDES). The bank assumed that the pace of rural exodus in the first half of the 1980s would remain unchanged until 2000, even supposing that the economy will grow once more at historical rates (7% p.a.), doubling the domestic product. Nonetheless, the share of the economically active population (EAP) who are unemployed or underemployed in the informal sector of the total urban EAP does not reduce significantly, dropping from 37% in 1985 to 32% in 2000, which is still extremely high.

Therefore, it seems clear the need to reduce the pressure of rural exodus on the labor supply in the urban-industrial areas. Otherwise, a process of dynamic redistribution of income will not be possible. This data is not surprising, as new technologies will sharply reduce the volume of employment per unit of capital invested in the industrial sector and even in the service sector. The agricultural sector is the only one in which job generation per unit of invested capital still presents, in countries like Brazil, certain flexibility to absorb relatively more labor. “Baby boomers” and the increase in the share of women in the labor market will push the growth of the economically active population till the end of the century.

Table 3 – Brazil: economic growth, rural exodus, employment

Years	Real GDP growth (%)	Rural EAP (thou.)	Rur. EAP/ Tot. EAP	Urban EAP		
				Formal sector +	Inf. sector unnocupied (thou.)	Rel. share of inf. + unem. (%)
1985	8.3	15.4	28.6	23.4	15.0	39.0
1986	8.2	15.1	27.2	24.6	15.6	38.8
1987	5.0	15.5	28.2	25.3	16.0	38.7
1988	7.0	15.7	26.9	26.4	16.3	38.1
1989	7.0	15.9	26.6	27.5	16.5	37.5
1990	7.0	16.1	26.2	28.6	16.7	36.9
1991	7.0	16.3	25.9	29.7	17.1	36.5
1992	7.0	16.5	25.6	30.9	17.3	35.9
1993	7.0	16.7	25.2	32.1	17.5	35.3
1994	7.0	17.0	24.9	33.3	17.8	34.8
1995	7.0	17.2	24.6	34.6	18.0	34.2
1996	7.0	17.3	24.3	35.8	18.3	33.8
1997	7.0	17.5	23.9	37.0	18.7	33.5
1998	7.0	17.7	23.6	38.3	19.0	33.1
1999	7.0	17.9	23.2	39.7	19.4	32.8
2000	7.0	18.0	22.9	41.1	19.8	32.5

Brazil: economic growth – rural exodus.

Therefore, if Brazil does not solve the employment problem, it runs the risk of entering the next century with the worst of two worlds: on the one hand, poverty, malnutrition, and low levels of education, characteristic of underdeveloped countries; on the other, social security and healthcare problems due to an aging population.

Thus, land reform in Brazil can still play a crucial role in expanding employment opportunities in the countryside to reduce the pressure of labor supply in the urban-industrial labor market. If not the only one, Brazil is one of the few countries capable of redistributing land without affecting the most dynamic sectors. For the first time in the country's history, there seem to be political and economic conditions to achieve this goal. Despite the persisting difficulties regarding land reform, it is still possible to make it an instrument for more rational land use in economic and social terms. The government's necessary condition is political will, starting with the effective levy of Rural Property Tax.

An effectively levied Rural Property Tax is a solid deterrent to land speculation and may deconcentrate land tenure in a relatively short period. Pressured by progressive solid taxation, the owners of idle or semi-idle land would sell it or enter into some form of concession agreement (lease or partnership). The first hypothesis has a limited scope in the short and medium terms because of the fall in land prices it would cause. The second hypothesis seems to be the most rational for owners once land ownership is guaranteed. One must bear in mind that the end of land speculation does away with the primary motivation for landowners to break with traditional land tenure arrangements and evict resident workers.

Moreover, as mentioned above, the fast rural exodus and the growing organization of temporary rural workers ("*boias-frias*") have caused increasing difficulties in hiring labor during seasonal agricultural peaks in various regions, and growing problems control the work process. These facts have made large landowners more amenable to the idea of stabilizing the supply of rural labor, creating better conditions for people to stay in the countryside. In other words, in the 1960s and 1970s, the presence of resident workers on estates was seen as a threat to land ownership, now and aided by the effective levy of Rural Property Tax, the presence of resident workers contributes, to the contrary, to ensure land ownership.

Thus, we might witness a process of deconcentrating the land structure in the short term, which is crucial, and in a context that would tend to favor rural workers. Faced with tax pressures, on the one hand, and greater organization of workers on the other, landowners would be much less capable of imposing extremely unfavorable lease or partnership contracts. Rural workers would have their bargaining power increased, being able to negotiate more advantageous land tenure contracts. Once the structure of land tenure deconcentrates, land ownership structure may follow suit in the long term. By having the option to purchase, tenants and partners would buy the land they work on, as, with the end of speculation, land prices would tend to reflect only their productive capacity. At the same time, the State would be responsible for ensuring, as in many countries, long-term loans (with low but positive interest rates) for the purchase of land by these farmers.

This pathway to land reform in Brazil does not exclude the expropriation of idle land but rather complements it. We believe that expropriation, which is relatively expensive and contentious, cannot solve the Brazilian land issue in the short term. Time is essential since expanding work opportunities in the countryside is an urgent condition to reduce unskilled labor pressure in the labor market in the coming years. In addition, a considerable number of rural workers would be unable to run a rural micro-business capable of facing the usual problems of any rural enterprise and the problems that would inevitably occur because of failures in the official support system. However, these workers could be successful by entering into some partnership agreement with the landowners that would allow them to use part of the existing infrastructure on the estate. The landowner who, pressured by a land tax, leases a part of his land has an interest in the partner's success, and the support that he or she can provide in terms of infrastructure is not a high cost. For example, the average level of idleness of a large part of agricultural equipment allows its lease at a reduced cost.

However, we recognize that the effectiveness of taxation as an instrument of land reform can be challenged based on the historical reality of the last 26 years of the Land Statute. There are two reasons for that: the first and most important is political, related to the *de facto* power of rural (and urban) oligarchies to oppose the law when their interests are at stake; the second, of a technical nature, concerns the existing difficulties in effectively controlling the degree of idleness of agricultural land in such a vast country like Brazil.

Regarding the technical argument, the difficulties of inspection, despite not having been, historically, a decisive obstacle to tax collection, have undoubtedly served as an excuse for the omission. However, nothing is simpler nowadays than monitoring what goes on in the countryside. The various satellites in service offer imagery with a very high degree of definition. It is even possible to identify the different types of crops. Thus, it would be possible to check the degree of idleness of agricultural land for tax purposes with a good sampling.

Concerning the political argument about the ruling class's power to assert its interest contrary to law, indeed, it seems correct to explain what has happened so far. The Rural Property Tax, which existed for almost three decades, has never been effectively enforced, due either to outright default by landowners (tax evasion) or to the negligible amount calculated by the bodies responsible for issuing the tax (under taxation). Tax evasion is easy simply because the bodies responsible for issuing and collecting the tax, IBRA (Brazilian Institute of Agrarian Reform) and later INCRA (National Institute of Settlement and Agrarian Reform), have never enjoyed political support to levy and punish defaulters effectively.

As for under taxation, its leading cause lies in the fact that the tax is calculated based on the minimum limit of the accepted bare land value (BLV), which does not correspond to the reality of the land market as determined by law. Therefore, the actual bodies responsible for levying the tax have failed to comply with the legal provisions. Another fact that leads to under-taxation is false information submitted by landowners. The tax can be progressive or regressive, depending on the degree of land use and efficiency in using it. Calculating the degree of land use depends on the property area considered usable, which tends to be underestimated, not to say deliberately falsified, by the landowners. Likewise, ascertaining the degree of land use efficiency depends on the levels of productivity reported by landowners, which are deceptively high. This information provided by owners, which is notoriously false, has been accepted without control by the responsible bodies.

In short, both tax evasion and under-taxation stem from the simple fact that successive governments have never had any political will to enforce Rural Property Tax effectively. The tax only existed as a reformist *façade* of deeply reactionary elites operating in a context in which the balance of forces favored them. However, to assume that this balance of forces will always remain the same, especially after the new Constitution and direct presidential elections, seems unrealistic to us.

The conservative bloc's initiatives against land reform, which led to the defeat of the progressive forces in the Brazilian Congress, was accompanied by public recognition of the need to avoid, once and for all, the merely speculative use of agricultural land. The fierce conservative reaction against the original text to be voted resulted from the perception that the news rules to be voted the next government would be sooner or later enforced. The population showed signs of increasing political awareness and organization.

The issue of subsidized credit and tax incentives shows that this is happening. There is a consensus that these funds from the public treasury granted to large landowners and companies have notoriously fueled land speculation. Therefore, the policy of subsidized credit and tax incentives for large landowners was increasingly questioned, and the current government seems determined to eliminate it once and for all. Without those funds, a considerable amount of land would not be appropriated by speculators, thus becoming available to be appropriated by landless workers.

It is now up to the organized sectors of society to take a firm stance in holding the government accountable to its promises. The forces that made the Land Property Tax (LPT) innocuous are the same that have obstructed land expropriation so far. Therefore, if the land reform movement hopes to force the government to speed up land expropriation, it must also transform LPT into a vital instrument to reform Brazil's land structure.

In summary, the agriculture sector must fulfill in Brazil, albeit belatedly, the same role played in developed capitalist countries of a regulating "buffer" of labor supply. Access to land seems to be an indispensable condition for reversing the current context of extreme income concentration that prevents most of the Brazilian population from enjoying minimum standards of quality of life by the end of the century.

CHAPTER 9

THE SPECIFICITY OF THE BRAZILIAN “WELFARE STATE”

Liana Aureliano[1]
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Welfare state: the brazilian case

A - Historiography of the Brazilian Social Policy

In this section, we will seek to underscore the historiographical elements related to the production of social legislation and the formation of the social apparatus of the Brazilian State so, afterward, we carry out a historical analytical treatment of the process of construction of the Welfare State in Brazil.

In relation to the areas of social intervention of the State, we have already seen that there appears to be a relatively common sequence in most Western capitalist countries. The institution of codes, legislation and public (mainly elementary) education networks preceded state actions in the areas of health, social security, and welfare, being, later, followed by the emergence of schemes (and regulations) concerning popular housing. Concerning the core of what is now considered social security, the most common sequence would seem to be that from the legislation and definition of insurance schemes against accidents at work, followed by retirement and pension schemes, almost

1 Professor at the Institute of Economics at UNICAMP. Editor´s note: the chapter selects the second part of the original text, focusing on the Brazilian ‘welfare state’. We decided to keep the Portuguese abbreviations for the state organizations and programs cited, as usual in the literature on the topic. Author´s note for this translation: This essay was written between 1987 and 1988 and published in 1989. For two main reasons, it is important for the reader to keep these dates in mind to better understand both the historical and political context in which it was written and the limits of international and national literature in which it was based. Firstly, the Brazilian constitution of 1988 constituted a decisive landmark, in fact a strong inflection in the process of constitution of the Welfare State in Brazil. It broadened the basis of social rights on which the Welfare State was founded and introduced significant universalist criteria throughout the social protection system. However, such a movement could not have been contemplated by this work, which was completed before the new constitutional definitions. Secondly, the comparative international literature on the processes of constitution and development of Welfare States only began to develop in the 1980s, still remaining strongly dependent on the pioneering work of Titmus, in the 1950s. Esping Anderson's The Three Worlds of the Welfare Capitalism would not be published until 1990. Therefore, its typology and those that followed it were not yet available when this essay was written in the late 1980s.

concomitant with the emergence of health insurance, to finally be supplemented by unemployment protection (usually preceded by some forms of family protection). The sequence in Brazil is not very different, and we will try to observe it considering the areas that characterize the Welfare.

The Educational Policy

The action of the Brazilian State in the field of education has its remote origins in the imperial state. The compulsoriness of primary education, as well as the division of duties among the federal, state, and municipal governments in relation to the institution and provision of education networks at the three levels, are already included in the Constitution of 1891. Until 1930, however, the effective implementation of a national education policy lacked resources of various orders, in particular those relating to an integrated codification as to the national territory, and those relating to the organizational structure of the State to support the policy, in addition, certainly, to the clear definition and allocation of adequate financial resources. Doctrinal-pedagogical centralization, organizational unification and institutionalization would seem, then, to be tasks still to be executed, within the scope of the National State, after 1930. Let us see the main moments of this movement.

As we have already stated in another work (Draibe, 1985; 1986), the effective implementation of an educational policy in modern States would seem to respond, simultaneously, to three processes: the definition of the political-ideological parameters under which the "socialization" of citizens must be processed; the pressure and demands for the extension of citizenship; and, finally, the tasks of ideological reproduction of technical-vocational training of the workforce.

These three aspects, which, in other patterns of formation of capitalist States, unfolded over a period of centuries or at least many decades, were simultaneously present in the movement to structure the Brazilian national education system from 1930 onward. From the introduction of the Ministry of Education and Public Health in the year of the Revolution until the approval of the Law of Guidelines and Bases for National Education in 1961, an area of the State's social apparatus was structured that provided material support for the development of governmental policy on education. Concurrently, a "capitalist" response to the pressures for the expansion of citizenship was considered and formulated, and in parallel, the contours of an area of private investment were delimited.

In 1930, a national question of education was raised, both in terms of unifying the educational system and strengthening the Federal Union, as well as its social contents, expressed in the various platforms of "public and free education" – in response to claims that had gained momentum since the 1920s.

Several aspects were present in this educational issue. There was criticism of the dualism that prevailed in the First Republic, the result of a division of competences between the Federal and the State governments, imposed by the "extreme" federalism in force. This duality would give rise to another one, as Nagle points out, translated into the contrast between "elite schools" (secondary and higher education) and "people's schools" (elementary and technical-vocational education). Beyond the limits of federalism, a more general situation was configured: the traditional, dispersed, and subordinate nature of the administrative apparatus linked to education at the level of the federal government and even at the level of the state administration[2].

Between 1930 and 1945, an intense movement took place in the Federal Executive to introduce a national apparatus for teaching and developing codes and "organic laws," aiming to establish guidelines and organizational structures for the various branches and levels of education in the country.

From the point of view of the process of centralization and integration of a national education system, it is worth remembering its important moments. The creation of the Ministry of Education and Public Health in 1930 was followed by the National Council of Education and the Consultative Council for Commercial Education, both structured within the scope of the ministry and having the attribution of establishing general guidelines for elementary, secondary, and higher education and for vocational education and training. These guidelines were succeeded, during the Estado Novo regime and throughout 1946, by the Organic Laws of Education – partial reforms and plans, which affected each of the branches and levels, without establishing, however, their coordination according to a national criterion of continuity and division of educational labor.

The goal of creating a "code of guidelines for national education" (according to the expression of the time) was pursued throughout the 1930s and under the Estado Novo regime. It was even provided in the 1934 Charter, when the competence of the Federal Government to establish the national education plan was defined – comprising all degrees and branches to coordinate and supervise its execution throughout the country. Nevertheless, thus far, the prevailing centralist impulses have not succeeded.

The 1946 Constitution reaffirmed the Federal Government's competence to establish the bases and guidelines for national education, and in 1948, the long process of the Education Guidelines and Bases Project following the legal

2 Nagle, J. (1977). A educação na Primeira República. In B. Fausto (Org.), *História Geral da Civilização Brasileira* (pp. 261–291). Tomo III, v. 2. Difel.

channels began, which caused heated discussions, a major political movement that was transformed into law only in 1961.

A new step would only be taken in 1953, when Education and Culture separated from Health, constituting a specific ministry.

With the approval of the Education Guidelines and Bases and the creation of the Federal Council of Education, the centralization of the basic provisions of state control over education was completed; thus, a centralized educational apparatus was established, and the Federal Executive provided itself with legal instruments and a general education plan. The national education system acquired an integrated format, and through the central devices, there was the establishment of the margins from which administrative decentralization would take place, the prerogatives of the federative regime, and the relationship between the public school and the private school.

It is not enough, however, to track this movement solely in its aspects of centralization, unification, and control. The constitution of the integrated educational apparatus in Brazil involved, due to the very characteristics of the stage under analysis, other contents that had already been foreshadowed since the 1920s under the more general designations of demands for popular, public, and free education.

The orientation of "popular education" in the post-1930s mirrors the diversity and transformation of the class structure in the industrialization process. To the popular demands for the extension of citizenship, the material and legal structuring of the education apparatus responded with the reaffirmation of the universal, free-of-charge and compulsory nature of elementary education but, at the same time, with the organization of a parallel network focused on the education of the "underprivileged classes"; thus, the "incomplete citizenship" of the wage-earning sectors was configured in the dual stratification of the school apparatus in systems that differentially organized the elementary-secondary and higher education levels and, on the other hand, the elementary-prevocational and vocational education levels.

In the early 1930s, after the creation of the Consultative Council for Commercial Education, the Inspectorate of Vocational and Technical Education and the Division of Industrial Education were structured in the Ministry of Education. The reform of commercial education in 1931 started the process of implementing the technical-vocational education network, which would culminate between 1942 and 1946 with the Organic Laws of Industrial and Commercial Education (1942 and 1943, respectively) and with the institution of the SENAI-SENAC system of a school-company association for the education and training of urban workers.

If this aspect of the organization of the education apparatus already has, in its very structure, the most general feature of the class character of the Brazilian economy and society in the phase of constitution of "industrial capitalism," the delimitation of relations between public schools and private schools also reveals peculiar contents. The polarizations between freedom of education and the state monopoly on education, repeatedly present in Western Europe in disputes over competence between the State and the Church, became entangled here in another issue; although in an embryonic manner, it was about the delimitation of a specific area of capital accumulation. In addition to the tensions between the state and social sectors that competed for the "formation of 'individualities,' the right of private capital to a space for investment in the educational enterprise was also debated"[3].

To a certain extent, the 1961 Law of Education Guidelines and Bases defined the key structure through which the system would expand, especially in the post-1964 period. The reorganization of this system between the late 1960s and the early 1970s (university reform, introduction of vocational training in elementary and secondary education) did not deviate much from that matrix. An important measure was the extension of compulsory education to eight years (basic cycle), defined in the late 1960s.

Due to being unable to conduct, here, an examination of this expansion and reorganization process, observing its most significant numbers, as well as some specific characteristics[4], we only point out some important aspects, in relation to education, in the period spanning from 1964 to the early 1980s:

- the remarkable global quantitative expansion of the system, practically in its three levels, configuring a very accentuated pattern of mass education. In terms of coverage, in the mid-1970s, hypothetically the supply covers, 90% of the age group corresponding to basic education; the university population grows from its historical percentage of 1% to 3% or 4% of the population in the 1980s. However, the global figures hide a reality, also numerical, that is very perverse. According to some estimates, in the early 1980s, eight million school-aged children were still not attending school, with dropout rates after the first two grades of basic education exceeding 50%, which tended to narrow the educational pyramid; the coverage of secondary education remained very low, the contingent of lay

3 See. Draibe, S. (1995). *Rumos e Metamorfoses: um estudo sobre a constituição do Estado e as alternativas da industrialização no Brasil, 1930/1960* (pp. 68–72). Paz e Terra.

4 For a summary, see Brasil (1985). Relatório sobre a situação social do país. NEPP, UNICAMP, v.2.

teachers in elementary education, mainly in the Northeast region, remained above tolerable levels, etc.

- At practically all levels, the accelerated expansion seems to have been associated with a very strong trend toward the deterioration of the quality of education, and this is correlated with a set of causes ranging from low public investment in the system to low teacher salaries, the short stay of students in schools, and even curricular and pedagogical issues, introducing a quite resistant sort of vicious circle in the system in addition to high degrees of ineffectiveness, inoperability, etc.
- The expansion of the public network was followed up and even surpassed, in some levels of education and/or regions of the country, by the accentuated growth of the private network. On the other hand, it also seems certain that such expansion obeyed to a great extent clientelistic criteria of allocation and no definition of priorities in the system, in addition to the growing corporatist influence of some professional categories better situated in the political bargain, particularly the segment of university professors or, more strongly, the segments of owners of the private network.

Social Security

The sequence occupational accidents – retirements and pensions – health-maternity/family-unemployment, as risks that were gradually covered by a public social security system, was also relatively observed in Brazil. Regarding beneficiaries, the sequence indicated by the international literature tends to comprise professional categories linked to high-risk professions (miners, for example), followed by (general) categories of urban industrial workers, extending to independent professionals, rural workers and varied middle strata. In Brazil, as we will see, this sequence is quite different: it starts, in fact, with professional categories of workers linked to public services (railway, port, etc.), on the one hand, and later, as in other cases, it includes rural workers.

It was only with the Retirement and Pension Institutes (IAPs) that the establishment of a public social security system began in the 1930s, covering, from the outset, the risks related to the loss of work capacity (old age, illness, death, disability), as well as health care services.

As is known, the prehistory of that moment was marked by the legislation on accidents at work of 1919 and the regulation of the Retirement and Survivors' Pension Funds, according to the Eloy Chaves Law of 1923[5]. The Eloy Chaves Law, in turn, as several authors have already pointed out, only regulated a private contract between employees and employers within the scope of the individual company and, accordingly, alongside mutual aid societies, etc., did not yet represent the beginning of the construction of the public, compulsory social security system.

It is also true that, in the period that opens in 1930, as we will seek to see, that system is not fully consolidated, suffering from quantitative, qualitative, financial, and institutional limitations, which would only be overcome in the later phase. It is worth pointing out, in this historical compilation, the most important legal production related to social protection.

If we look at the chronology from the point of view of the risks covered, it is worth noting that the Retirement Institutes, created by professional categories from 1933 onward, were responsible for covering retirements, pensions and sickness benefits, as well as for the provision of health care services. Having their benefit plans with little uniformity in relation to one another, it is only after the Organic Law of Social Security of 1961 and the effective integration of the institutes into a single body (INPS) in 1966 that those risks become uniformly guaranteed for almost all urban workers. In 1967, the regime relating to accidents at work was incorporated into the INPS. In 1974, another benefit was created – the Monthly Lifelong Income for seniors aged over 70 and disabled people who had not met the typical contribution requirements for retirement.

For family benefits, the introduction of the family allowance dates to 1963, the maternity-wage and the maternity allowance date to 1974, constituting, until the 1980s, the only three benefits "of this kind and exclusive to urban social security."

Until the mid-1980s, unemployment insurance was not instituted. In 1966, the Length-of-Service Guarantee Fund (FGTS) was created, which, geared primarily toward replacing the employment stability clause included in the labor laws, was interpreted by some as corresponding, also, to a type of unemployment insurance. In fact, the first unemployment insurance scheme dates to 1986, organized by the Ministry of Labor, and only recently appears to be receiving financial and organizational definitions.

From the point of view of the categories of workers, between 1933 and 1953, the IAPs covered most urban workers; 1933 - IAP of seafarers; 1934 - IAP of commerce workers; 1937/38 - IAP of industrial workers, cargo workers, federal civil servants - IPASE. The railway workers, who maintained

5 The law on compensation for accidents at work (transport, construction, and factories) did not provide a public insurance scheme; it regulated the operation of private labor insurance companies.

the structure of the CAPs for a long time, in 1953 have all of them unified into a single structure, like the institutions: the CAPFESP. Other professional categories were incorporated much later, in the 1970s. In 1971, PRORURAL/FUNRURAL was created, which extends a few benefits (six at that time, when the urban benefit plan already had 18) to rural workers. Domestic workers were incorporated in 1972, self-employed workers in 1973, in addition to some specific categories (religious workers, students, etc.).

From the point of view of financing, organizational structure, and management of this system, it is worth noting certain characteristics. Following the introduction of the Retirement Institutes, an immense and growing machine of services was set up under the control of the Federal Government, although composed of a fragmented structure (the institutes organized in the form of autarchic entities) and not very uniform about distributed and provided benefits and services, as the institutes were individualized by professional categories.

For more than three decades, the history of the Retirement Institutes was characterized by attempts to unify the pension system, as well as by the strong corporatist and political resistance that such centralization caused. In 1945, the Organic Law of Social Services was enacted in Brazil, creating a single Institute (ISSB) and aiming to unify all social security services. This law, repealed in 1946, was followed by another attempt, through a bill that followed the legal channels in Congress, from 1947 to 1961, when the Organic Law of Social Security (LOPS) was enacted, which covered all employees under the CLT regime, equaling benefits to be earned. The LOPS, however, was not regulated, maintaining, in subsequent years, internal differentiation about social security benefits.

Until the early 1960s, the intended unification was simultaneously linked to several issues. On the one hand, a solution was sought that would standardize and expand social security benefits and services. On the other hand, the point was devising a solution that would enable a more effective financial use of the funds, which were fragmented among the various IAPs, either because of the "natural" worsening of their financial situation or because of the perceived alternative that they would finance large economic projects of the government. Furthermore, the unification could reinforce instruments for political mobilization and control of the working classes. Logically, by the nature of the issues involved, and by solutions, then, that strongly contradicted the existing political articulations, the unification encountered resistance and divergences within the bureaucracies of the trade unions and institutes but also from political parties, as well as from the bureaucracies of government, in particular within the Ministry of Labor. Because, it is important to remember, this social security "system," due to its relations with the unions, on the one hand, with the bureaucracies of the Ministry of Labor, on the other hand, and to the well-known direct relations of the union bureaucracy with the Ministry, operated through several clientelist, manipulative and controlling processes of the working classes, in addition, of course, to having seen – in the fragmented form in which they were composed – crystallize strong corporatist interests of professional categories that saw in the unification a threat to privileges and benefits already achieved.

For all these reasons, remodeling and unification would only occur in the post-1964 period, in a situation where the interests of workers and their representations in the management of the institutes were already removed and repressed. Of course, part of the institutes' bureaucracy remained in the new system which, in the authoritarian situation of the post-1964 period, would be reorganized, consolidating the social security system, having been able to greatly expand its technocratic and, apparently, apolitical features.

After the INPS was created in 1966, a new centralizing, unifying and rationalizing impulse would be felt in 1977, when, in fact, social security was fully restructured, now conceived as a single system, organized according to functional specializations, including welfare actions and welfare geared toward minors. The National Social Security and Welfare System – SINPAS is created and managed by a new and specific Ministry, the MPAS. SINPAS is composed of seven entities: INPS, INAMPS, IAPAS, LBA, FUNABEM and DATAPREV (respectively social benefits; health care; collection/payment; social welfare; care for abandoned minors and offenders; and computerization).

Since its origins in the 1930s, social security has been financed by a tripartite system of contributions by employees, employers, and the State, operating on a pay-as-you-go basis. Contributions and benefits are related to past income, which causes social security benefits to, at most, restore the previous condition of employment and wages, thus excluding both those unemployed and those outside the formal labor market, reproducing, among wage earners, the wage gap in the economy.

From the point of view of redistributive aspects, the Brazilian social security system only has income transfers between the insured persons themselves (and their dependents): from active to nonactive; from healthy to sick; and, in a tiny proportion, from insured contributors to noncontributing beneficiaries (rural workers and beneficiaries of the Monthly Lifelong Income). The contributions of companies, passed on to direct costs, end up being paid by consumers (independently, in fact, of their level of income). On the other hand, given the prevailing ceilings on income subject to contribution and the small difference between the rate bands that are levied on the lowest salary ranges, the financing system that prevailed until the mid-1980s, is characterized by regressivity. In short, the financing of the social security system, as it was structured in the 1960s and 1970s, was limited to promoting a horizontal redistribution of income.

Undoubtedly, a certain pattern of universalization occurred within the system, mainly from the 1970s onward. The gradual incorporation of professional and functional categories added, in the area of health care, the extension of emergency care to the entire population, regardless of whether they were insured.

Under this pattern, formed as a system in the 1960s and reorganized in the following decade, the Brazilian social security system expanded significantly. Its most significant figures can be indicated. In the mid-1980s, the population suitable to pensions, services and benefits reached 100 million people, which corresponded to approximately 75% of the population. The mass of contributors exceeded 25 million, equivalent to 90% of the economically active population (in 1963, this percentage was approximately 23%). Even so, this system remained quite exclusionary under Brazilian conditions. Requiring a contractual relationship in a significant portion of its programs and excluding the *flat benefit* or minimum income option the Brazilian social security system excludes, for example, in the urban sector, workers who are precariously employed, those who are unemployed for a long time or those who are unable to participate as self-employed, given the high contribution needed.

Health care policy

Until the 1930s, there was not, properly, a national health policy in Brazil. It is certain that, as demands and pressures on the State agenda, the health of the population, in general, and of the working population, in particular, had represented an issue since much earlier, mainly driven by the processes of urbanization, migration and immigration, etc., throughout the development of the coffee exporting economy. However, until the late 1920s, no major response, of a national and effective nature, had been provided, and this limitation is related – according to the various authors who analyze the problem – fundamentally to the nature and organization of the oligarchic State. During its term, the social security and public health care actions are carried out, on the one hand, by some states of the Federation; on the other hand, by benefits and services provided by companies or, in the 1920s, by some Retirement and Pension Funds – practically a private sphere of action, as already mentioned[6].

6 See. Braga, J. C. & de Paula, S. G. (1981). *Saúde e Previdência: estudos de política social* (pp. 41–50). HUCITEC.

The effective intervention of the federal state in health care began in the 1930s and would only consolidate a specific structure from the mid-1960s onward.

Between 1930 and 1966 – according to the periodization suggested by José Carlos Braga – driven by the centralizing impulses of the Brazilian State, there was the definition of a mode of intervention and the outlining of a health policy "[...] organized centrally in two subsectors: public and social security health care. The first would prevail until the mid-1960s, and as to many fundamental features, the structure then instituted remains in force to date. Alternatively, the social security health care subsector expanded significantly from the late 1950s and, in terms of state health policy, it assumes predominance from the second half of the 1960s"[7].

The public health care subsector shows a movement, between the 1930s and 1950s, of centralization and specification of the federal administrative machine and diversification of actions under a sanitarian model of intervention in health. The Ministry of Education and Health, created in 1939, already provided a National Department of Health and Medical Social Welfare, which, in 1937, takes over the coordination of the state health departments, standardizing their internal structures. Sanitary campaigns had been carried out by the Ministry since 1934 and would, in turn, constitute important elements of the centralization of the policy. They are supported by institutional and service diversification, such as the creation, in 1937, of the National Yellow Fever Service; in 1939, of the Northeast Malaria Service; and, in 1940, of the Baixada Fluminense Malaria Service. In 1941, a reorganization in the Ministry led to the incorporation of several other services that dealt with endemic diseases and to it assuming control of the training of public health technicians, in addition to institutionalizing the sanitary campaigns. The structure of the Ministry also indicates the areas of intervention. National Services for Tuberculosis, Plague, Malaria, Leprosy, Cancer and Mental Diseases, Yellow Fever, Sanitary Education, Medical Inspection, Biostatistics and Medical Biometrics, in addition to the National Department of Children.

Another important moment in the organizational formation process would be the separation, at the ministerial level, of the areas of health and education, with the creation, in 1953, of the Ministry of Health; the Special Public Health Service – SESP also expanded in these years, which, as a foundation, would become part of the Ministry in 1960. Finally, in 1956, the National Department of Rural Endemic Diseases was created, which began to centralize the services to combat endemic diseases. Driven by this centralizing movement and sanitary campaigns, this area of state intervention was organized,

7 See. Braga J. C. & de Paula, S. G., op. cit., p. 52.

theoretically representing a public universalist way of extending mass health care – the so-called public health measures.

However, regarding funding, expenditure, and the results of the public health policy, restrictions and limitations characterized the area. From the 1960s onward, there was a relative decline in public health expenditure and, as we said, the growth of social security health care. According to José Carlos Braga, two hypotheses can be postulated to explain this movement. In addition to the structural restrictions inherent in the industrialization period, the first hypothesis is of a political nature: given the low degree of organization, mobilization, and political strength of the mass of the population, especially its poorest segments, there were also low pressures on the government to expand its action and implement the (universal) basic, collective health policy. The government’s operation, in the period, was carried out primarily through sanitary campaigns, which were important but had little effect on instituting permanent health care services. Obviously, these campaigns resulted in substantial political dividends of a legitimizing character.

The other hypothesis refers to the limitation of the tax structure, which, at this stage of economic development, provided a relatively small amount of resources to the state. As the author states, “[...] with the lack of resources and the absence of political pressure, public health saw very little money allocated to it. At the same time, the social security system was substantially self-financeable, increasing its financial availability with the increase in employment [...]. As the objectives of social security health care mobilized – moreover – considerable political forces, it is not surprising that, regarding health care as a government social policy, social security was strengthened and privileged”[8].

For it is truly social security health care that, from the 1960s onward, would affect the health policy in Brazil and it has been, to date, within the scope of social security organization, that the universalization of health care policy and effective expansion of coverage has been observed, a situation that can be exemplified by a single indicator. In 1970, public spending on health care was distributed as follows: federal government - 15.13%; states and Federal District - 22.42%; municipalities (of the capitals) - 2.06%; and INAMPS - 60.01%. In 1980, the INAMPS accounted for 64.01% of public spending on health care under those organizational characteristics already mentioned in the previous topic, and under the aegis of authoritarian governments, a health care system featuring very peculiar characteristics was devised through the expansion of social security health care. Let us highlight the main characteristics.

8 See. Braga J. C. & de Paula, S. G., op. cit., p. 55.

From the point of view of health care system financing – jointly considering public and social security health care – the greatest weight falls, as we have seen, on the participation of the INAMPS, which was financed by contributions from social security insured subjects, in the form of self-financing. The insured participants then bear the largest share of financing a system that, in turn, has universalized part of the health care system, theoretically covering the entire population. It is true that this situation is not unique to Brazil. However, in addition to drawing attention to its proportions, it was organized in conditions in which the basic level of public health care is precarious, limited and insufficient (except for a few states of the Federation). On the other hand, financed in this way, this system is particularly affected by the financial behavior of the social security system, which is sensitive, as we know, both to crises and recessions and to the injunctions of its natural "maturation" process with the expected growth of spending on benefits, in particular retirements and pensions.

From the point of view of system management, regarding its segment of social security health care, the exclusion of the working classes from decisions in this area began to characterize, in the post-1964 period, the decision-making and power system. However, the predominant rationalizing and technocratic view did not mean, from the outset, greater immunity of the system to clientelistic and corporate pressures. Under the authoritarian regime, there was a strong clientelistic use of the system, especially in electoral cycles (although it is a little researched subject, empirical evidence has never failed to appear in the press and in testimonies). On the other hand, given the privileged relationship between the system and the private sector, provider of medical services, particularistic interests in this segment, coordinated with bureaucratic interests, were very present in the decision-making and resource allocation process. Finally, especially from the late 1970s, the expression of the corporate interests of professionals linked to the area (physicians and paramedics) was increasingly strong, particularly in issues related to salaries, alternatives and even resistance to reforms and reorganizations.

The proportionally greater expansion of social security health care in relation to public health introduced and intensified distortions in the system. The former meant the imbalance between hospital-curative medicine to the detriment of preventive and primary health care. The latter meant a particular form of coordination with the private sector, with the system oriented less toward the expansion of public services and more toward the purchase of services from the private sector (hospital care, group medicine, etc.). A situation that, according to one analyst, meant "the maximization of particularistic interests," in addition to bureaucratic and corporate interests, with a low degree of public control over the actions of the state and far from the interests of the population consuming health services[9].

Under these characteristics, the health care system developed in the country in the 1960s/1970s expanded remarkably. The coverage of services was extended, comprising an increasing number of people. The evolution in the number of medical appointments, hospitalizations, dental appointments and complementary exams shows the dynamism in the production of services. However, this growth, marked by the characteristics mentioned above, maintained, and deepened the differentiation between sectors of the workforce, between urban workers and between regions of the country (expenses with health care for rural workers constituted, in 1984, 1/7 of the expenditure on urban social security, despite the rural population amounting to more than 1/3 of the urban population). More than anything, the system quickly began to suffer from all the evils of its gigantism and lack of control, which led, from the mid-1970s, the discussion of its reform to be marked, above all, by the theses of integration (of the three levels of public action – federal, state, and municipal levels), on the one hand, and of (political and administrative) decentralization and deconcentration, on the other hand.

Thus, between 1975 and 1982/83, several measures were taken, accordingly, through the law that instituted the National Health Care System in 1975; the Program for the Internalization of Health and Sanitation Actions – PIASS, in 1975; the National Program for Basic Health Services – PREV-SAÚDE, in 1980; the Plan for Reorientation of Health Care in the scope of Social Security – CONASP, in 1982; and, finally, the Integrated Health Actions – AIS, in 1984. After the start of the democratization process, in 1985, a new integration/decentralization program was defined in 1987, the Unified and Decentralized Health Care system (SUDS), currently in progress.

Due to several and complex reasons, it is only with the Integrated Health Actions (AIS) that a strategy for reorganizing the health care system begins. In general, both this strategy and, subsequently, the one initiated by the SUDS had, as a more general objective, overcoming the most perverse, contradictory and irrational characteristics of the health policy in Brazil. This would be done by means of goals for integrating public actions at the three levels of the Federation, reorganizing the relation with the private sector, improving managerial capacity, optimizing the financial resources of the system, and decentralizing decisions and operations. All of which aimed at raising the level of effectiveness and problem-solving capability of the policy and bodies responsible for the execution of health care in the country[10].

9 See Silva, P. L. B. (1984). *Atenção à saúde como política governamental*. UNICAMP.

10 For a detailed examination of the plans and programs that preceded the AIS, see Brasil (1985). *Relatório sobre a situação social do país*. NEPP/UNICAMP.

The AIS aimed at structuring state health care systems with a high degree of problem-solving capability; developing the managerial capacity of services at the local and regional levels; integrating the allocation of resources from different sources (federal, state and municipal sources); valuing the human resources participating in the health team; planning intervention through the development of technically and financially viable parameters adapted to local conditions; and orienting the research and activities of educational institutions toward the health needs of each region. From the outset, the AIS faced several difficulties and resistances, either because of the dimensions of the problems to be solved, or because they affected countless interests, or, finally, because of the very conception and design, as a policy. Thus, in 1984, there were already signs of retraction of resources from the state and local spheres, changing, in practice, the principle of proportional burden sharing; excessive hegemony of INAMPS, which began to have strong interference in state and local health departments, since the transfer of resources was conditioned to preestablished productivity standards; low representativeness and lack of agility of the service planning and management committees, which had not been able, thus far, to effectively become the real locus of decisions (CLIS, CIMS, CRIS, CIS)[11].

The AIS were, in fact, supplanted, in 1987, by the SUDS, a more radical decentralization strategy that will be examined in a section below.

Housing Policy

As a centralized state system, referring to the entire national territory, supported by resources from specific institutions, housing policy is a late area of social intervention by the State, being implemented only in the post-1964 period, with the institution of the Housing Finance System (SFH) and the creation, to operate it, of the National Housing Bank (BNH).

However, the introduction of the policy in the field of affordable housing for the poor precedes it. In fact, many of the Retirement and Pension Institutes provided, among their activities, housing financing plans, in particular the IAPB, the IAPC, and the IAPI, as well as those linked to (federal and state) civil servants. Unfortunately, there are no empirical verification studies on the production of affordable housing through IAPs throughout the 1940s and, mainly, the 1950s. Additionally, in 1946, at the level of the Federal Government, there was the creation of the Fundação da Casa Popular [Affordable Housing Foundation], whose achievements are little known.

11 See. NEPP, op. it., p. 145–148.

Created in 1964, the SFH and the BNH had, as sources of financing, the Length-of-Service Guarantee Fund (FGTS) and deposits in savings accounts. The FGTS, as mentioned above, was instituted with the objective of replacing the employment stability statute, constituting the worker's assets for housing, unemployment, etc. Intended to finance the SFH, its application should produce financial returns to remunerate such assets, occurring the same with the resources originating from savings accounts. On the other hand, in conjunction, the applications of SFH resources should also generate surpluses to appreciate the (public and private) capital that participates in financial intermediation in the production process and in the management of housing policy. Thus, "it is easy to see that the cost of these resources, combined with the income structure of the Brazilian population, limits the effectiveness of this financing mechanism. Its inadequacy, evident in favorable economic situations, reaches the paroxysm in the recessionary conjuncture of the early 1980s, when the very high levels reached by inflation and interest rates joined the wage deindexation policy. If, in the late 1960s, the dream of home ownership for the low-income strata came undone, in the crisis of the 1980s, this dream also vanishes for the middle classes"[12].

If the form of financing and the rule of financial self-support already limited, at first, the social effectiveness of this policy, which ended up, in fact, benefiting middle sectors, other characteristics deepened its low social effects and the perversions that occurred in it, such as the excessive centralization of the political decision-making power and of the control over financial and institutional resources at the federal level; and the high degree of privatization introduced in the decision-making and resource allocation processes, given the possibility that private (construction sector) and bureaucracy segments would maximize their interests to the detriment of collective interests.

Conceived and implemented under the authoritarian aegis of the post-1964 regime, this area of State intervention was perhaps the one in which characteristics of inequities, irrationality and a very low degree of social effectiveness were most pronounced. The large, modern, expensive, and sophisticated Housing Financial System produced, over the 1965–1984 period, an approximate total of 4.5 million houses, of which, however, only 723,000 were assigned to the low-income strata of the population (up to three minimum wages, including urbanized lots). In the same period, only 7.7% of the total balance of financing under the SFH was allocated to borrowers with an income of less than 3.5 monthly minimum wages. The table below shows the production of SFH in the 1965–1968 period.

12 See. NEPP, op. cit., p. 4.

SFH PRODUCTION
1963/68

INCOME LEVEL	UNITS	%
From 1 to 3 minimum wages		
urbanized lots	41,901	0.01
João de Barro	9,760	0.00
PROMORAR	222,140	0.05
From 3 to 5 minimum wages		
COHABS	1,247,725	27.27
PICAM	96,305	6.02
From 5 to 10 minimum wages		
Cooperatives	810,358	18.72
More of 10 minimum wages		
SBPE	1,900,878	41.54
RECOM	247,424	5.40
TOTAL	**4,575,992**	**100.00**

The system practically collapsed in the 1980s, and between 1985 and 1987, the project of its complete reorganization underwent little to no progress, occurring only in early 1988.

The 1980s also saw the growth of state and municipal initiatives aiming to by means of various systems (joint effort, mutual aid, urbanized lots, etc.), advance in the production of housing for the underprivileged sectors of the population, in a very critical situation of lack of housing. It would be difficult, now, to estimate, at the national level, the results of such initiatives, although all studies that have attempted to examine these "alternative" ways of dealing with the housing problem point out the meagre results achieved.

The Welfare Policy

It has been difficult to establish precisely, in Brazil, the specific scope of a welfare policy. There are several welfare programs in the country that are conducted by different public bodies and distributed in the three levels of government. On the other hand, they are aimed at the most varied services and benefits, ranging from meeting the needs to health, nutrition, education, work, leisure, legal support, etc., seeking to tackle, in the form of temporary or emergency reliefs, some of the multiple aspects of the situation of needs that affect the vast majority of the Brazilian population.

With this fragmented, indefinite, relatively unstable character, public welfare programs have been developed in the country throughout its history. A given centralization, however, occurred at the level of the Federal Government and, later, at the level of the states of the Federation, with the creation of social promotion departments, since the mid-1970s.

At the federal level, this process tended to take place primarily around an agency created in 1942: the Brazilian Legion of Welfare (LBA), organized as part of the Emergency Civil Labor Mobilization Program during the war. In 1969, the LBA was transformed into a foundation and linked to the Ministry of Social Security and Welfare, integrating, from 1977 onward, the SINPAS. Within its scope, programs were developed to assist minors (nursery, food, etc.), maternal and child nutrition, legal identification actions for citizens, assistance to elderly individuals, the disabled and vocational education programs.

For the public it covers, the LBA, despite being part of the social security system, is not only aimed at policyholders; in general, the population covered by its programs consists of people who are unemployed, underemployed, who have insufficient purchasing power or who have reduced conditions to overcome, by their own means, their current situation of disadvantage. As for its financing, the resources earmarked for the LBA originate mainly from the Social Security and Welfare Fund and, recently, from resources originating from the FAS (Social Assistance Fund) and FINSOCIAL (Social Investment Fund). As for its organization and operation, the LBA operates through centers and agencies distributed throughout almost all Brazilian municipalities, indirectly through agreements with private entities and, occasionally, with municipal governments. Its main programs began in the 1970s, after the institutional reorganizations mentioned above.

Finally, for the public served, it is very difficult to estimate, throughout its existence, the most significant figures of its programs. Like most social areas, this is characterized by a recurring difficulty in clearly and accurately estimating its public in operations that are always marked by double counting. Around 1985, the LBA was claimed to be serving approximately four million beneficiaries, mainly among its priority programs, those aiming at children, pregnant women, and nursing mothers in the population with income of up to two minimum wages. In 1987, having shown a great expansion in its resources and actions, the agency claimed to have served almost 50 million Brazilians, an exaggerated number.

It should also be pointed out that it is impossible to determine the impact of this type of welfare program in the composition of the household income of the poorest strata of the population, for several reasons, even the most evident one, that the permanence of the same families and people in the same programs is very unstable. The sharp fluctuation of provision, enrollment, and registration, according to political and clientelistic injunctions, are characteristics that have always marked the welfare area.

The other agency that deserves mention is FUNABEM, dedicated to the care of abandoned minors and offenders. Established in 1964, the National Minors Welfare Foundation replaced the former Minors Welfare Service (established in 1941); in 1974, it is linked to the Ministry of Social Security and Welfare, and in 1979, it became part of SINPAS. Theoretically, this foundation is of a normative nature, and direct operation should be carried out, at the state level, by FEBEM.

The LBA and FUNABEM should, by definition, develop the national welfare policy and the national policy on care for minors, a task that both, in fact, never managed to accomplish.

Finally, it is important to point out another area of welfare policy that is implemented through the multiple food and nutrition programs carried out by the National Institute of Food and Nutrition (INAN), established in 1972.

Historically, the food policy in Brazil has its origins in 1940, with the creation of the first federal Program – the Workers' Food Program. During the 1950s, two more programs were developed, supported by international food donations, under the auspices of UNICEF: a program for feeding pregnant women, nursing mothers and children aged zero to five years and another for school feeding. It was only in 1972, however, that, with the creation of INAN, this area of State intervention was effectively instituted, in compliance with the National Food and Nutrition Program, designed to operate during 1973/74. From the beginning, the target public is defined as the mother and child group, and a guiding principle is set: nutritional education. This is followed by PRONAM II, scheduled for 1976/79, but in fact extended until 1980. INAN, through PRONAM, operates in three basic lines: food supplementation (Program for Nutrition in Health - PNS); National School Feeding Program (PNAE); Supplementary Food Program and the Workers' Food Program (PAT); rationalization of the production and marketing system for basic foods (Project for the Purchase of Food in Low-Income Rural Areas (PROCAB); Basic Food Supply Program for Low-Income Rural Areas (PROAB) and supplementary and support activities (combating specific nutritional deficiencies, training human resources and conducting studies and research).

The eligibility criteria for each program are varied: if they are mostly intended for the population with income of up to two minimum wages, being, therefore, selective and requiring means tests, the PNAE, for example, is different, by being, theoretically, intended for all children enrolled in preschool and elementary school (in 1985, it was also extended to the siblings of students who were not enrolled in school), having, in this sense, a universal character. There are also differences in relation to the financing of these programs: in general, they use resources from the Union Budget, the federal banking system (Banco do Brasil and Banco Nacional de Crédito Cooperativo), FAS, FINSOCIAL, etc. The PAT, however, is a program organized by companies through tax incentives, and the final cost of meals is shared between companies (38%), employees (20%) and the government (42%). For coverage, the most comprehensive program is the PNAE: currently, school meals cover practically the entire age group of students to which it is intended. Next, there is the PNS (in 1984, it reached 4.3 million beneficiaries); the other programs had reduced coverage. For the form of operation, the programs also vary greatly. In general, the operation is centralized, especially regarding the purchase of food; however, there has recently been an effort to decentralize school meals, which are currently strongly municipalized.

Two final considerations regarding welfare policy are necessary. First, it is worth pointing out that the welfare programs carried out by states and municipalities are also multiple, although there is no tendency in Brazil to favor local and municipal welfare actions present in other countries.

On the other hand, this area of government intervention has been repeatedly noted as the most permeated by clientelistic mechanisms, as well as by the absence of controls, which tends to make it an easy prey for manipulation and corruption. In the absence of clear policies for the sector, of public mechanisms for control and verification, there is open space for these characteristics to be reproduced; on the other hand, in the absence of a clear definition of citizens' rights in relation to that provision of goods and services in Brazil, throughout its history, the welfare policy has always been marked by a narrow concept of welfare, which tends to stigmatize its beneficiaries, making them solicitors and beggars before a supposedly benevolent state.

Periodization and Characterization of the Brazilian Welfare State

Although brief and insufficient, the history above can support the exercise we will conduct below, that of constructing a periodization of the institutional establishment of the Welfare State in Brazil and indicating, according to the commented typology, the more general characteristics of the Welfare State pattern in force among us.

It is useful, from the outset, to underline, once again, the conception of Welfare we are working with: that of a transformation in the relations between the State and the economy, which is manifested in changes in the very structure of the State and in the emergence of national, public or state-regulated education, health, income integration, social welfare and low-income housing systems. Concretely, these are processes that are expressed in the organization and production of public goods and services, in the setting up of social transfer schemes, in public intervention on the structure of opportunities to access public and private goods and services and, finally, in the regulation of (and incentive to) the production of private social goods and services.

Accordingly, the periodization that we intend to indicate can only have as a starting point, as we have already said, the period that commences in 1930, considering the set of transformations in the Brazilian State and the forms of social regulation that began then. On the other hand, this same conception forces us to carefully examine the nature of the legal production and innovation in policies that transpire in the period from 1930 to the present in an attempt to avoid a linear view of the movement of construction and consolidation of the Welfare State among us.

Many authors pointed out the fact that, throughout this period, two phases of accelerated legal production stand out: the 1930-1943 phase and the 1966-1971 phase, both, in fact, carried out under authoritarian regimes, a situation that seems to endorse the thesis of preventive actions by elites and the pursuit of forms of legitimation through social policy. However, this is not the discussion we are interested in having here. Rather, it seems important to us to examine to what extent these two periods are similar in nature or express distinct phases of that general movement that we want to periodize.

The legislative production to which the 1930–1943 period refers is fundamentally related to the creation of the Retirement and Pension Institutes, on the one hand, and, on the other, that relating to labor legislation, consolidated in 1943. If this is, in fact, the most important innovation, the period is, however, also fertile, as we have seen, in changes in the areas of health and education policy, with high degrees of centralization, in the Federal Executive, of institutional and administrative resources and instruments.

In addition, within the limited framework of the democratic regime that was in force between 1945 and 1964, the movement of legal-institutional innovation (in the fields of education, health, social welfare and, very slightly, in affordable housing for the poor) kept on going. The social protection system was expanded according to the models and parameters defined by the innovations of the 1930-43 period; that is, at the same time, there are advances in the processes of institutional centralization and of incorporation of new social groups into protection schemes, <u>adopting, however, a selective (in terms of beneficiaries), heterogeneous (in terms of benefits) and fragmented (in terms of institutional and financial aspects) pattern of social intervention by the State</u>.

The period from the mid-1960s to practically the mid-1970s is very different, due to its nature, content and social impact. The set of legislative measures constitutes, in relation to the previous period, a context of radical transformation of the institutional and financial framework of the social policy system. A radical transformation because this is the moment when, effectively, the public or state-regulated national systems are organized, in the area of basic social goods and services (education, health, welfare, social security and housing). This transformation overcome the previous fragmented and socially selective form, leading to certain universalizing trends, but mainly to the subsequent implementation of mass policies of relatively broad coverage. Moreover, this is also a period of innovation in the social policy, as State intervention is instituted in new sectors (housing), mechanisms are introduced in the field of formation of workers' assets and of the so-called corporate profit sharing (FGTS and PIS/PASEP) and, still maintaining strong exclusion characteristics, the social protection system advances in the inclusion of rural workers, and benefit plans for urban workers become differentiated.

Thus, with the authoritarian and technocratic characteristics of the regime that was installed in 1964, the Welfare system in Brazil is completed: the hard core of State social intervention is defined; the centralized apparatus that supports such intervention is established; the funds and resources that will financially support the system are determined; the operating principles are set; and, finally, the rules of social inclusion/exclusion that definitively mark the system are defined. The massive expansion, which occurs from the mid-1970s onward, will take place under the pattern that had been organized since 1964 and which, already in the late 1970s, shows signs of exhaustion and crisis.

The above considerations enable us to set forth, then, a proposal for periodization of the process of the Brazilian Welfare State's institution. According to our view and supported by the international literature on the same issue[13], it is possible to observe the following temporal cutoffs and characteristics:

1930–64 – Introduction and Fragmented Expansion

a) 1930–43 - introduction
b) 1943–64 - fragmented and selective expansion

1964–85 – Institutional Consolidation and Conservative Restructuring

a) 1964–77 - institutional consolidation

13 See, for example, the periodizations indicated, for European countries, by Alber, Flora, & Heidenheiher, op. cit. The Italian case was well periodized by Ferrera, M. (1984). *Il Welfare State in Italia*. Il Mulino.

b) 1977–81 - massive expansion

c) 1981–85 - conservative restructuring (attempts)

1985–...- Progressive restructuring (attempts)

Several observations should be made regarding the criteria used in this attempt at periodization. First, the three major cutoffs (1930, 1964 and 1985) fundamentally consider changes in the sphere of the political regime and, for 1930 and 1964, changes in the form of the State, much more than in specific occurrences at the level of the Welfare institutions themselves. This criterion seems indispensable to us, whether because of the more general definition of the Welfare State with which we work or because of the characteristics of social protection itself, especially in its more or less universalizing, "assistentialist" or redistributive aspects. In addition, of course, to the definition of the relation between economic policy and social policy (both at the more structural level of economic and social regulation and at the level of "models for development" and management of the economy).

Second, the criteria considered to specify the subperiods are quite heterogeneous, which can naturally introduce difficulties. However, at the current stage of this work, it was not possible to fully overcome this risk. For example, the 1930–43 subperiod (Introduction) refers fundamentally to social security and labor legislation, while other subperiods, mainly that of institutional consolidation (1964–77), refer to the more general framework of the State's social action (including therefore, education, health, and housing).

Obviously, major innovations or modifications in each area or subarea of the State's social action are not strictly contemporary. Therefore, the option selectively emphasizes the modifications that seem most important in the organization and supplementation of the basic core of the Welfare State.

The expressions "fragmented and selective expansion" and "massive expansion" used to describe the mode of growth, advancement and coverage of social protection are also insufficient to account for the specificity of the movement in each subphase. The first, obviously, is considered fragmented and selective, either because not all areas of state social intervention operated fully or because the policy was aimed at social groups that were gradually incorporated into the system (social security but also in relation to other collective social goods and services). The second – massive expansion – concerns a moment of growth with characteristics of mass politics.

The problem with descriptive expressions such as these is that they do not enable us to grasp differences, when it is known that fragmentation, selectivity, universalism, and massive care can permeate both subperiods in different ways. For example, massive expansion does not necessarily mean universalization and, therefore, a total rejection of selective modes of growth.

Finally, there is an additional difficulty in relation to the period that began in approximately 1981. Strictly, this period extends to date, since, in fact, there was not a full restructuring of the social policies system in the country. However, it is true that, in terms of governmental agendas, the issue of restructuring is proposed (in fact since the late 1970s) and, in the conditions of economic crisis, it is intensified. However, it is possible to distinguish differences in conception and orientation in the formulation of the agenda itself, as well as in the restructuring proposals that are submitted still under the military regime and those that are placed on the agenda, already under the civil government of the New Republic – which we designate as conservative and progressive.

Attempts that are still partial but much more decisive only took place in 1987 and 1988 – some in the field of health and social security and others in the context of the ongoing constituent work. Thus, albeit imprecisely, with the 1981–85 and 1985–... subsections, we sought to represent both the nature of the proposed developments (the restructuring) and the differences in the conception and definition of a new Welfare State profile in Brazil.

With all these considerations, the suggested periodization seems necessary. According to the objectives of this work, it will be able to guide and better support the analysis that will be made in the next chapter of the morphology and functioning of the Brazilian Welfare State, as it was built and consolidated in the post-1964 period. Before undertaking it, however, it is worth underlining the general characteristics of the pattern followed in Brazil throughout the introduction and consolidation phases.

As we saw in the first section[14], welfare typologies emphasize mainly the meritocracy-universalism binomial of the State's social actions, as well as the residual or selectivity aspect with which they reach and/or incorporate social groups into their benefits. Considering the above arguments, as well as the characteristics pointed out in the historiography, it is possible to observe that the principle of merit, basically understood as the occupation and income position acquired at the level of the productive structure, constitutes the basis of the Brazilian social policy system. In the case of social security, this has been the principle in force since the introduction phase; in the consolidation phase, when other benefits and the system of social funds are defined, the income-contribution-benefit ratio also remains dominant and, in this sense, the social policies, for the most part, reproduce the system of inequalities prevailing in society. Their redistributive and egalitarian aspects are scarce and are theoretically present only in the field of education (compulsory and free basic education) and health (emergency care). Thus, the inexistence of

14 Not included in this volume (editor´s note).

social minimums extended to all citizens, regardless of their position in the labor market, weakens – in the state/market relationship – the corrective mechanisms that, in principle, should operate through social policies.

It will not be strange, then, to claim that the Brazilian pattern of Welfare is of the meritocratic-particularistic type, as defined by Titmus. However, on this basis, the Brazilian system also acquired other important characteristics throughout the 1970s, especially in the subperiod that opened in 1981. Given the meritocratic model, on the one hand, and the current employment and wage structure, on the other hand, the Brazilian system has developed a dense welfare scheme, superimposed and/or parallel to the security core (LBA and food and nutrition programs), a scheme that simultaneously refers to specific groups – and, therefore, theoretically residual – but which, in principle, addresses the majority of the population, salaried or not. As the eligibility criterion is family income of up to two minimum wages, in fact those welfare programs (noncontributory) are, by definition, related to "risk groups" – children, pregnant women, nursing mothers, the elderly – that, however, constitute the vast majority of the population, given the current income and employment structure in the country. Thus, the theoretically supplementary aspect of the public welfare policy is less residual and, rather, operates as a precarious substitute of social minimums (not defined, nor institutionalized). Obviously, destitution, underemployment and unemployment are at the base of this further derivation of the Brazilian system, which escalated, in fact, in the post-1985 period. In any case, it is important to point out the fact that, more than becoming universalized, the Brazilian social protection system has advanced in the path of being supplemented by currently very important welfare mechanisms (remember, also, the diversified programs operated by FINSOCIAL, FAS, SEAC, etc.).

In its relations with interest groups and the political system, the Welfare State in Brazil has tended to acquire, since the introduction phase, a characteristic corporatist connotation, which, in fact, often marks meritocratic-particularistic systems. Nevertheless, it is perhaps the clientelist character that most strongly affects its dynamics. This is due to several and complex reasons. Since the introduction phase, the privileged relationships are known; in the case of social security, between bureaucracies of the institutes, bureaucracies of the Ministry of Labor and top party members (especially of PTB[15]). After this pattern was broken in the post-1964 period, other forms of clientelism entered the system, affecting the allocation of resources, the expansion movement and, finally, tending to feudalize (under the sway of groups, personalities and/or top party members) areas of the social security body and, mainly, the distribution of benefits in electoral periods.

15 Portuguese abbreviation for Partido Trabalhista Brasileiro, or Brazilian Labor Party (editor´s note).

From the late 1970s onward, the growth of the welfare space of social policies only reinforced the clientelist aspect; the opening of the political system, post-1985, made this characteristic of the system's functioning more clearly visible. It is important to remember, however, that clientelism does not only concern the core of social security: it has always affected education (in political relations between the spheres of the Federation and, in the post-1964 period, mainly in the mode of operation of the Federal Council of Education) and, with strong corporatist and privatist contents, it also characterized the functioning of the Housing Finance System.

It is true, as already pointed out, that universalizing trends – in terms of coverage and beneficiaries – were gradually introduced into the system. In the field of social security, the unification of the IAPs under the INPS already constituted a movement of homogenization of benefits and universalization of rights, at least for all urban wage earners formally included in the labor market. As for health, as mentioned, since the late 1970s, emergency care has been opened up to the entire population through social security health care. In the case of education, the compulsory and free basic level was already included in the first republican constitution, and the extension of the compulsoriness to eight years in the 1970s expands this "right" of citizenship (although it is known that the effective coverage in this cycle is low, especially after the first grade, which presents dropout rates in relation to the second in the order of 50%). However, these universalizing trends are still far from providing "institutional-redistributive" characteristics to the Brazilian Welfare system.

Having made these brief observations, it is possible to elaborate in the next topic the morphological representation of the Welfare State in Brazil, presented as it took place from the mid-1970s onward. A rigorous evaluation of this representation would involve an quantification effort (of resources, services provided, beneficiaries) that is extremely difficult to be carried out here. However, from the outset, it is possible to observe that, as this system was set up, greater equality, in the sense of a vertical redistribution of income (through social policies), is not a basic objective: the minimum level provided is quite meager and, as we will see, the redistributive mechanism internal to the social transfer scheme is fragile.

In principle, the first objective of the Brazilian system would tend to be, in the context of social security, the protection of the status already acquired by the worker against risks of social decline (present and future). Here, too, whether because of the inequities that it contains or, finally, because of the low values of benefits, the fragility is manifested in the protection.

These observations only point out very generic trends and characteristics of the Welfare State in Brazil. Next, we will study, in more detail, its morphology and operating principles.

C. Specificity of the Brazilian "Welfare State"

There is no doubt that the State's social intervention assumed quite clear characteristics after 1964, characteristics that are expressed in organizational principles that are perfectly coherent with the conservative and socially exclusionary economic model. Let us see what these principles are.

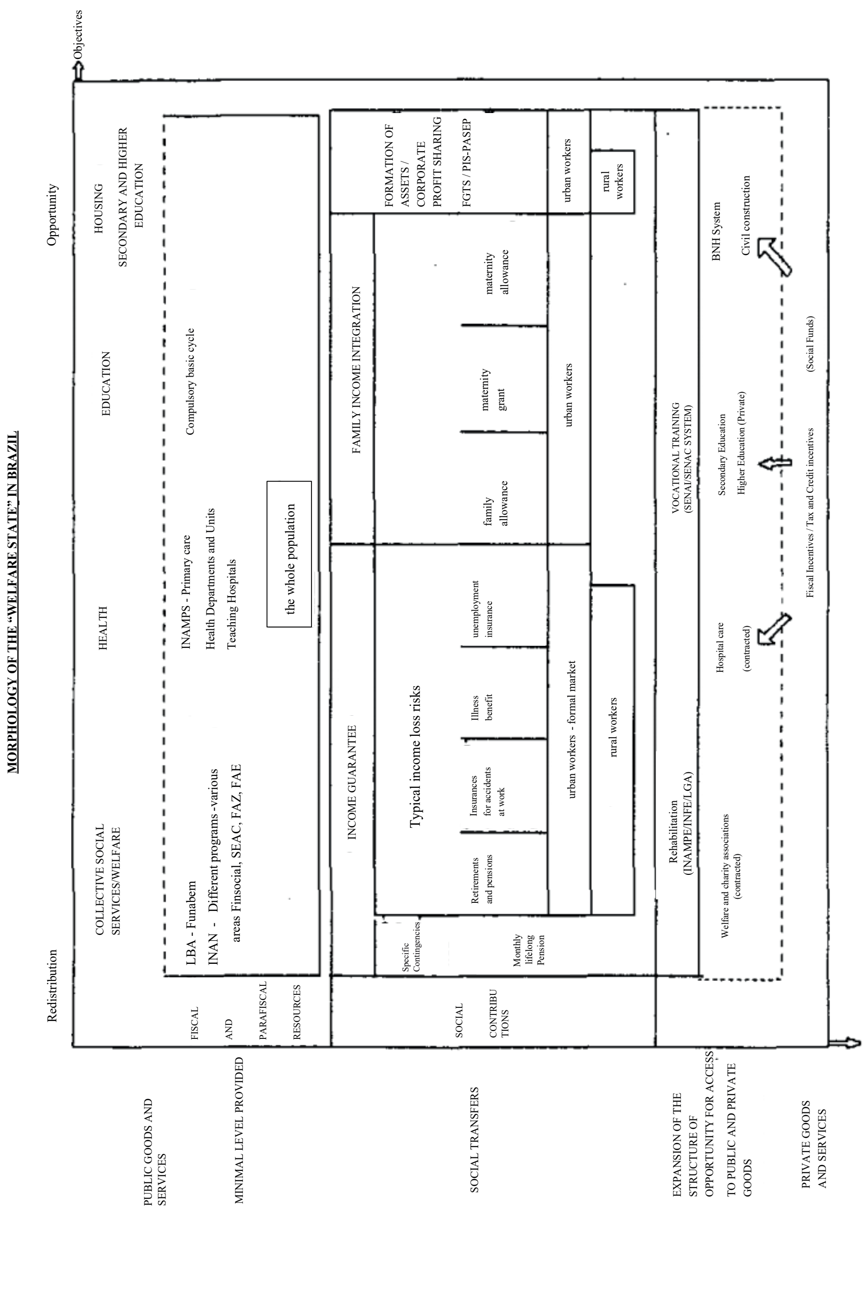
1. **The extreme political and financial centralization of the government's social actions at the federal level**

It is indisputable that the centralization of decision-making power and financial controls in the federal government assumed unprecedented proportions. On the one hand, centralization "expropriates" states and municipalities from the instruments of social intervention in three ways: by concentrating financial resources on the Federal Executive; by establishing general rules applicable to social policies; and by submitting the application of federal funds to the decisions of the federal government, thus avoiding, as much as possible, any type of "automatic transfer" of resources. <u>Within the Federal Executive</u>, on the other hand, there is a relative direct reduction of the administration's social action and its replacement, either by large organizational complexes (BNH, SINPAS, etc.) or by decentralized administration bodies (companies, foundations, and autarchic entities).

2. **A formidable institutional fragmentation**

There was a multiplication of different forms of public bodies, such as institutes, foundations and, mainly, public companies. It is possible to identify the most serious consequences of this "decentralized" way in which the state social apparatus has expanded:

a) excessive bureaucratization;
b) growing autonomy of these bodies in relation to the central government;
c) blocking the formulation and implementation of general plans for each sector and, evidently, of a national social policy;
d) absence of public control mechanisms, which enables the free movement of private interests in the State apparatus;
e) incredible overlapping of programs and publics, as an expression of institutional disintegration.


MORPHOLOGY OF THE “WELFARE STATE” IN BRAZIL
Objectives
Redistribution
Opportunity
State/ Market
PUBLIC GOODS AND SERVICES
MINIMAL LEVEL PROVIDED
SOCIAL TRANSFERS
EXPANSION OF THE STRUCTURE OF OPPORTUNITY FOR ACCESS TO PUBLIC AND PRIVATE GOODS
PRIVATE GOODS AND SERVICES
FISCAL AND PARAFISCAL RESOURCES
SOCIAL CONTRIBUTIONS
COLLECTIVE SOCIAL SERVICES/WELFARE
HEALTH
EDUCATION
HOUSING
SECONDARY AND HIGHER EDUCATION
LBA - Funabem
INAN - Different programs -various areas Finsocial, SEAC, FAZ, FAE
INAMPS - Primary care
Health Departments and Units
Teaching Hospitals
Compulsory basic cycle
the whole population
INCOME GUARANTEE
FAMILY INCOME INTEGRATION
FORMATION OF ASSETS / CORPORATE PROFIT SHARING
FGTS / PIS-PASEP
Typical income loss risks
Specific Contingencies
Monthly lifelong Pension
Retirements and pensions
Insurances for accidents at work
Illness benefit
unemployment insurance
family allowance
maternity grant
maternity allowance
urban workers - formal market
urban workers
rural workers
Rehabilitation (INAMPE/INFE/LGA)
VOCATIONAL TRAINING (SENAI/SENAC SYSTEM)
Welfare and charity associations (contracted)
Hospital care (contracted)
Secondary Education
Higher Education (Private)
BNH System
Civil construction
Fiscal Incentives / Tax and Credit incentives
(Social Funds)

3. Exclusion of the population's social and political participation in decision-making processes

The bureaucratic and authoritarian movement of centralization and fragmentation suppressed or prevented the participation of unions, parties, and social movements in all domains of social policies. This occurred, from the outset, in a domain where union participation had long been established: in social security. The new "sectors" were already conceived according to this orientation, such as housing. On the other hand, the fundamental guidelines of social policies were not discussed in Parliament. Therefore, all forms of public control were suppressed. It is no accident that, in the early 1980s, the social protection system exhibited all forms of institutional disorder, administrative disorganization, fraud, and corruption.

4. The principle of self-financing of social investment

This principle, in addition to having meant the creation of specific financial funds for each sector, also represented the submission of social spending to economic and financial criteria of private profitability for the allocation of resources. The best example, we believe, is that of the BNH, which favored housing over sanitation and housing for the middle class at the expense of affordable housing for the poor.

5. Privatization principle

The principle of self-financing translates into a kind of golden rule of social policies: users must pay for what they receive. Ultimately, this rule leads to the privatization of social services, which has different aspects:

a) the opening of space for the penetration of private interests in the State apparatus through pressure groups, lobbies, etc.
b) a very structured form of coordination between the state apparatus and the private sector that produces services (such as hospitals) or provides "social products" (such as construction companies). It can be said, therefore, that a division of labor is established between the state and the private sector: the state establishes rules and transfers resources; the private sector is in charge of producing goods or distributing services;
c) privatization finally resulted in a relative decrease in the State's participation in the education and health sectors.

These principles underlie the reorganization and reproduction of the Brazilian social protection system. It is not necessary that we address this further here, demonstrating how they manifest concretely in the effective functioning of the social apparatus of the State. Rather, it is worth mentioning a few words about two points that characterize well the distortions of our Welfare State.

First, the issue of the extremely regressive nature of the financing of state social spending. We can identify four types of resources that are used to finance social policies: fiscal resources, social contributions, equity-type funds, and funds constituted with contributions from companies specifically intended for social spending, such as FINSOCIAL and the education salary.

As for fiscal resources, it is not necessary to emphasize what is already known – the Brazilian tax system is quite regressive – nor to point out its main distortions – the ridiculous tax burden on agriculture, the high degree of tax evasion of small and medium-sized companies, injustices regarding income tax for individuals, etc. What we must reiterate is the residual character of social spending financed with fiscal resources in two senses: the State directly spends a relatively small proportion of what it collects as taxes, and this spending is a negligible fraction of the total social spending. Classic example: the state's noncontribution to social security.

The other three types of resources are generally defined as a relation between salary or payroll and contribution. Studies on this subject have shown that this form of financing falls mainly on wage earners, with a greater weight on the lower income strata. The most notable example is, arguably, social security: a ceiling of 20 minimum wages is fixed for the calculation of contributions, and the highest income strata are privileged; thus, for example, those earning between one and three minimum wages pay 8.5%, while those earning 100 minimum wages pay only 2%.

Regarding the funds formed by companies, it can be said that, in general, they are operated as if they were indirect taxes and are passed on to the prices of products, which means that they are paid by all consumers. Therefore, they do not have redistributive effects.

The second point that deserves comment is the excessive bureaucracy that characterizes the public social machine. Evidently, this is not an exclusive feature of the State's social apparatus, but it contaminates all public activity. However, the consequences here are perhaps more tragic. First, in a situation of chronic needs and lack of resources, it is unacceptable that the cost of operating social policies ends up consuming most tax resources, as the observation seems to indicate. Second, bureaucratism and inefficiency end up introducing or accentuating the practice of favors (example: difficulties for retirement). Third, the relative autonomy of the bureaucracy is effectively a very important factor of resistance to changes in social policy, which, as is well known, requires the suppression of certain bodies, the relocation of others, the extinction of programs, etc.

Having made these considerations, it becomes easier to understand why we consider our Welfare State to be meritocratic-particularistic. In fact, the state's social intervention is based on the contributory capacity of the worker, sanctioning what we can call the primary distribution of income. Thus, for example, the water and sewage network will only be extended if the states and municipalities are able to service the loans contracted with the former BNH, charging users with "realistic rates." Loans granted for the construction of low-income housing, made basically with resources from the Length-of-Service Guarantee Fund (FGTS), require an installment compatible with the costs of BNH and financial agents, which results in a real interest rate of approximately 10% per year. The tariffs for urban collective transport services must remunerate private investments; university students who cannot find places in the public education system must pay tuition fees compatible with the investment in education; private hospitals are an application of capital like any other, etc., etc. In this context, as we have already said, public spending, financed through a regressive tax system, assumes a frankly residual character, playing no redistributive role that could alter the primary distribution of income.

That said, it is necessary to take a step further and try to better understand the specificity of our Welfare State. The key aspect is understanding that our capitalism defined a conservative path of social "progress."

We mean by this that:

a) Rapid economic development leads to an accelerated and profound transformation of the social structure;
b) this transformation translates into a change in the employment structure; this job creation is socially expressed in a process of upward social mobility;
c) However, on the other hand, low wages prevail for large contingents of workers, while millions remain underemployed in the cities or entirely marginalized in the rural towns.

Therefore, social progress takes the form of social mobility combined with absolute poverty of a large portion of the population, in sum, upward mobility with extreme inequality. Social progress, among us, is achieved almost entirely by fulfilling capitalism's requirements of an "ideal form" of social development – unfettered competition between free men, which "selects" the "fittest."

Now, this situation is entirely different from the historical framework of the Welfare State in developed countries. Social welfare policies appear simultaneously with a situation of full employment, which, accompanied by a persistent rise in real wages, raises the living standards of the overwhelming majority of the population. Not here. For the vast majority, salaries are low, and for a significant portion there is no regular employment. Given this, there are several fundamental consequences:

a) The very contribution base (the salary) per capita is relatively narrow if we consider the area of social security. Consequently, the quality of services is affected, and the social benefits are necessarily insufficient for the purposes for which they are intended;
b) The welfare policy aimed at combating absolute poverty is "overloaded," as it has to address the needs of, say, a third of the population;
c) However, there are two thirds that <u>even employed and regularly receiving salaries</u> need State welfare aid to ensure a decent life. As a result, the very definition of welfare policy is impaired.

However, on the other hand, the fiscal resources available to support the expanded tasks of welfare policy and to complement welfare resources are scarce because the tax system expresses the "great pact," which encompasses all fractions of the owner class, either exempting them from fair tax contributions or favoring them with incentives and subsidies.

D. Interpretations of the origins of the Welfare State in Brazil

The analysis of the emergence and expansion of social policy has, often, suffered from the linearity of reasoning, typical of functionalist-type interpretive schemes, whether from the pluralist or Marxist perspective. In the first case, social policy is taken as a result of the demands of the modernization process in Brazil, with its contents of industrialization, urbanization, demographic transformation, etc. According to Marxists, the development of capitalism introduces a certain pattern of social division of labor and leads to mechanisms that guarantee the reproduction of the labor force, consistent with the demands of the accumulation process. Given the modernization or the need for (abstract) reproduction of the workforce, one could observe a *continuum* from the first social policy measures, taken in the first decade of the 20th century, to the most recent ones, in the 1970s, all of which presented in terms of a permanent process of expansion, either of beneficiaries or of the types of benefits, or, in short, of the financial and institutional resources mobilized by the State in the operation of public systems of social policy.

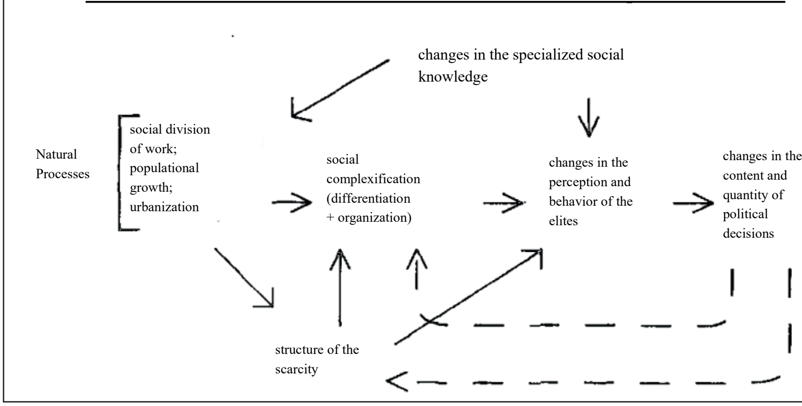
Accordingly, it is worth highlighting the difference that can be observed in Marxist or pluralist studies that emphasize the field of power relations and social and political conflicts as determinants of both the origin and the expansion of social policy systems. Either because they favor the movement and pressures of the working classes, or because they emphasize the behavior of the elites, or, finally, because they take seriously into account the structure of the State, the political regime and system. The authors working in this tradition treat the moment of introduction of social policies and the steps of their transformation according to fundamentally political and political-institutional criteria, which somehow breaks with the linear pattern we pointed out earlier, leading to a periodization, in our view, more consistent and underlining important qualitative differences in each stage. Let us consider two works to better exemplify what we said: "Cidadania e Justiça," by Wanderley Guilherme dos Santos[16] and "Saúde e Previdência," by José Carlos Braga[17].

The first work has the advantage of exposing, very clearly, the analytical framework that drives the interpretation. Moving in the field of elite theories, social system theory, modernization theory, it seeks to identify the variables, as well as the most typical relations that allow us to understand social policies. Briefly, it could be said, according to the author, that the availability of resources (apprehended through the concept of scarcity, more precisely the structure of scarcity) determines changes in the behavior of elites, which, in turn, causes changes in the content and the quality of their decisions. However, these relations are driven by "natural" processes (i.e., not controllable by government policies), such as the social division of labor, population growth and urbanization, which in turn produce impacts in terms of social differentiation, mediated by organizations that generate demands (the process of social differentiation plus organizational multiplication are here called social complexification). Together, they act as intervening variables between the structure of scarcity and the behavior of decision-making elites. The accumulated social knowledge also acts on the latter as an independent source of propulsion, with impacts even on the processes of transformation of the social structure. In general, these variables do not act independently but rather compose a dynamic framework of relations and interactions that can be visualized in the following scheme, proposed by the author.

16 See. dos Santos, W. G. (1979). Cidadania e Justiça: a política social na ordem brasileira. *Contribuições em Ciências Sociais*, *1*: 138.

17 See. Braga, J. C. & de Paula S. G., op. cit.

VARIABLES AND RELATIONS THAT ARE TYPICAL OF SOCIAL POLICIES



Source: dos Santos, W. G. *Cidadania e Justiça: a política social na ordem social brasileira*, op. cit., p. 67.

Finally, we note the fact that decision-making elites do not operate the state apparatus (bureaucracies, technical groups, advisory bodies) freely. In fact, greater or lesser probabilities of conducting decisions (changes or resistance to them) will depend on the various possible forms of interactions between political elites and the public bureaucracy.

Supported on this framework of causal relations and interactions, the work under examination claims that the change in the composition of elites – which took place in 1930 – is the closest explanatory factor that accounts for the origin of the social policy in Brazil as a regulation of the production process. This is because, in the narrow framework of *laissez-faire* principles, prevalent until the 1930s, the processes of population growth, migration, immigration and consequent social complexification, generating mobilization and demands through the trade union movement, were met by fundamentally repressive, coercive responses on the part of the elites. This reaction was only marginally altered by the unionization law of 1907 and by the Eloy Chaves Law of 1923 (Retirement and Pension Funds). The latter, according to the author, marks the beginning of the production of effective social laws in the country. Without completely rejecting the “Laissez-Faire” principles (since they also correspond to quasi-private agreements between employers and employees), they express, however, the recognition of the role of the labor force and of the need for norms for stabilizing the social order. In this way and for these reasons, the compensatory social policy in Brazil precedes the social policy by means of the regulation of accumulation, which will only begin after the Revolution of 1930, when it had already become clear that “[...] a change in the composition of the elite, or at least in a portion of it, was indispensable, which would allow the renewal of the ideological equipment with which the problem of the economic and social order was confronted, in the first place, and, as a corollary, that the norms that regulated the process of accumulation and the social relations were changed”[18].

In summary, in relation to issues regarding the origin and context of emergence of the social policy in Brazil, Wanderley Guilherme dos Santos ultimately emphasizes the behavior “from above” of new elites, after 1930, in the face of demands of organizations that express different levels of social complexity. He suggests two moments for the beginning of the social policy: the regulations of the 1920s, giving rise to compensatory social policy, and the economic and social policy initiated by the government, especially in the first four years after the 1930 Revolution.

Regarding the same issue, the work of José Carlos Braga, following the Marxist tradition, seeks to compose a framework of determinations, which ultimately considers the needs of training and reproduction of the workforce under the conditions of capitalism and, in the first instance, the type and degree of the Brazilian capitalist development, as well as the nature and function of the National State. In his words:

> “In this work, the notion of social issue is used, in a descriptive and provisional way, to apprehend complexly determined phenomena. On the one hand, the genesis and transformation of these phenomena constitute concrete manifestations of the ways in which the social relations of production are reproduced. On the other hand, they manifest themselves in political and ideological practices and tend to become the object of state policies. Capitalist development, in this sense, converts those processes related to the formation and reproduction of the labor force for capital, among others, into social issues. In the same movement, the State constitutes the body, par excellence, regulating and responding to such issues. In doing so, the capitalist and national State expands their significance, ‘attributing’ to them a general and universal character.
>
> In Brazil, the late character of capitalist development precociously poses such issues to the State. Both because the State assumes practices that ‘classically’ belonged to the initiative of the social classes and because, even in the first stages of its formation, it must, minimally, act as a National State. Considering the social issue this way, it seems possible to apprehend different processes and their respective regulatory policies, distributed over different planes: the regulation of the labor market and of the work process (immigration policy, labor legislation, wage policy, working hours regulation, etc.); the regulation of political activity (union organization and control, legislation on the right to strike, etc.), the composition of the collective consumption of employees (health, housing, education, etc.); the

18 See. dos Santos, W. G., op. cit., p. 74.

composition of 'labor income' (such as the Length-of-Service Guarantee Fund – FGTS, the Public Servant Fund – PASEP) "[19]

According to this analytical framework, Braga affirms the emergence of social issues (health among them – which is what concerns him) in the context of the coffee exporting capitalist economy, the first stage of the development of capitalism in Brazil, a process that operates on two levels: "[...] it reflects the advance in the division of wage labor; from a political point of view, it takes the form, albeit embryonic, of social policy"[20].

It is true, according to the author, that the State implemented gradually social policy measures since the first decades of the century, but mainly during the 1920s[21]. However, only after the 1930s, with the change in the character of the State and the necessary expansion of its social bases, would social issues gain political status, becoming part of the problematics of power. Furthermore, only in a second moment, when accumulation becomes dominated by industrial capital, does this process gain economic support. Fundamental, in his view, to mark this moment of inflection, in relation to the origin and moment of introduction of the social policy (as a national policy), are "[...] the changes of a political nature and the transformations in the nature of the State, which created the initial conditions so that the social issues in general [...], already posed in the previous period, could be addressed through an organic and systematic set of policies. The previous capitalist development posed a series of social problems that were impossible to solve in the economic and political framework of the First Republic. However, the political process of 1930 and, in particular, the fact that this new system of power should, in some way, include urban wage earners, made it necessary to define and attempt to implement social policies [...] a way to control, politically and economically, the working class, responding, at times, to its movements, maintaining the profitability of the industrial sector and its capacity for accumulation, maintaining minimum levels of reproduction of the workforce, keeping the political participation of workers under control"[22].

The origin and moment of introduction of the social policy in Brazil are related to a complex set of determinations, which is not reduced to the level of indeterminate structural requirements. Requirements of reproduction of the workforce, workers' mobilization and demands, and needs for social and political control of workers were posed since the birth of the capitalist export economy, but they would only see an organic and integrated response (albeit restricted) after the Revolution of 1930.

19 See. Braga, J. C. & de Paula, S. G., op. cit., p. 41.
20 Id ibid, op. cit.
21 Id ibid, op. cit., p. 41.
22 See. Braga, J. C. & de Paula S. G., op. cit.

It would not, in any way, be incorrect to say that the body of literature on social policies in Brazil assumes – as in the case of the two authors we have analyzed – the Revolution of 1930 as the landmark that initiates the social action of the State, although, evidently, there may be disagreement within this basic "conflictual" view. For example, Wanderley Guilherme dos Santos emphasizes, as we have seen, the preventive action of the elites. José Carlos Braga speaks of the need for legitimation, through the masses, of the power structure constituted by the "compromise" between agrarian and urban-industrial sectors in a situation of hegemony crisis.

We will find neither this clarity nor this basic agreement regarding the beginning of the social policy in Brazil when considering the formation of the Welfare State after the "Revolution of 1964."

For some years, it was very difficult for those who opposed the authoritarian State to abandon the stagnationist thesis and admit that the "Revolution of 1964" had carried out economic reforms based on which it was possible to overcome the crisis and trigger a vigorous process of production expansion. After ending up surrendering to the facts, the oppositions shift their criticism of the exclusionary character of the economic development to the issue of income distribution. Under these circumstances, admitting that the social policies gained new momentum and centering criticism on the conservative character of the State intervention was very difficult, not only because of possible ideological blocks but also because of the fear of not being understood and weakening the criticism of the regime. Thinking then about a Brazilian Welfare State, as we are doing now, was practically impossible because this category has, among us, a positive connotation that associates it with income redistribution, broad social rights, etc.

However, today, we believe it is correct to say that, in the late 1950s, there was a "social question" that admitted several paths and alternatives. Evidently, there is a structural background. It can be thought that there were new needs for social regulation, arising from the advance of industrialization that completed its last stage (heavy industrialization, bringing with it the emergence of the large modern oligopolistic company and the structuring of the industrial apparatus, the densification of the wage-earning of the workforce, the unification of the labor market and the development of urbanization and metropolization) and from the future deepening of this process, with the evolution of a new stage of capitalist development. Nevertheless, the choice of solutions, the type of Welfare State, we would say now, would depend above all on the political struggle. In addition, it was the conservative capitalist restructuring that conferred the meritocratic-particularistic character to our social protection system, which has an enormous dynamism arising from the economic expansion and, at the same time, is savagely regressive.

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CHAPTER 10

EMPLOYMENT AND WAGES IN THE MANUFACTURING INDUSTRY: the Brazilian case

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Paulo Renato Souza[2]

Latin American economic and social thought in the 1960s was characterized by deep pessimism regarding the manufacturing industry's capacity to generate employment. In the core of these discussions were controversies about marginality (Nun, 1969; Cardoso, 1971; Nun, 1971) and about the link between income distribution, employment and the technology used in the industrialization process (ECLAC, 1966; Pinto, A., 1965, 1970; Vuskovic, 1970; Tavares & Serra, 1971).

In general, emphasis was placed on the weakness of the pace of labor absorption in the modern activities of industry and services, resulting in the tendency to "spurious" growth of employment (Prebisch, 1970) both in the public sector and in marginal activities, especially in services.

This peculiar behavior of employment was explicitly blamed for the maintenance, and even growth, of pockets of poverty in the metropolises of the region. In other words, the people who managed to enter modern activities would have theprivilege of enjoying a more or less decent standard of living, which would hardly be attained by most of the employees in what later came to be called the "informal sector of the labor market".

Thirty years after the vigorous process of industrialization in Latin America, we are in a better position today than we were 10 or 15 years ago to evaluate more accurately its impact on employment generation and income distribution. First, we must recognize that it is untrue that the pace of job creation in modern activities has been sluggish, at least in Brazil. Table 1 shows the annual expansion rates of employment in the various non-agricultural activities, according to the "organized" and "unorganized" strata of the labor market[3]. These two strata maintained between 1950 and 1970 a steady participation around 63%

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3 See the definition in table 1. We are aware of the methodological limitations of this estimate. They have the sole purpose of illustrating orders of magnitude of the phenomena to be discussed. In addition, an analysis was carried out at the level of States and activities, in which a remarkable degree of coherence between information that, as mentioned in the table, comes from different sources and is not necessarily compatible with each other (See DEPE-UNICAMP, 1980).

and 27% respectively of total nonagricultural employment, the remaining 10% being in building construction. As can be seen in the table, "modern" activities showed a rather appreciable dynamism compared with the pace of expansion of total nonagricultural employment. Consequently, the relative participation of employment in modern activities in the non-agricultural total has remained more or less constant; this occurred during a period of exceptional dynamism in the growth of the economically active urban population, due to the previous demographic growth and the accelerated migratory process.

In recent years, despite not having census sources of information, we can estimate that employment growth in modern activities has even accelerated, particularly in the period of the great economic boom of the early 1970s. Industrial employment in establishments with 5 or more employees, between 1970 and 74 grew at an unusual rate of 8.4% per year in Brazil and 8.8% in the State of São Paulo[4]. For the latter state, household surveys show a growth in industrial employment of around 8.6% per year between 1970 and 1967[5]. Finally, the comparison of average monthly employment growth in the metropolitan area of São Paulo from 1971 to 1978 makes it possible to distinguish two well-marked periods: in the first, 1971-74, the expansion rate was 9.2% per year and in the second, 1974-78, it was reduced substantially to 2,6% per year (due to the economic slowdown), which resulted in an average growth of 5.4%.

Table 1 – Brazil: Annual growth rates of "organized" and "unorganized" nonagricultural employment 1950-1970
- percentages -

Industries	"Organized" employment	"Unorganized" employment	Total Employment
Secondary	3.6	3.3	3.6
Construction	-	-	4.8
Tertiary (total)	4.6	4.3	4.5
trade	4.7	3.5	4.7
Services	3.0	4.5	4.2
Transport, communications and storage	2.9	-	2.9
Private social activities	6.3	-	6.3
Public employment	5.6	-	5.6
university professionals	6.3	-	6.3
NON-AGRICULTURAL TOTAL	4.3	4.1	4.3

(a) "Organized" employment corresponds to that recorded by the census of firms, "non-organized" to the difference between employment according to the demographic census and employment according to the census of firms. In services. the latter total was increased by employment in domestic services.

Source: DEPE•UNICAMP, Research on the Labor Market, Campinas, 1980. Source of data: IBGE, Demographic and Economic Censuses of 1950, 1960 and 1970.

4 Sources: FIBGE, Industrial Census of 1970 and Industrial Survey of 1974.

5 Sources: IBGE, 1970 Demographic Census PNAD (Household Survey), 1976.

Contrary to what was implied in the analyzes of the 1960s, however, insertion in the "modern" sector was not, in itself, a guarantee of an "adequate" standard of living for employees. As we will see later, the increase in the wage gap was the implicit product of the reduction in the average level of real wages of a good part of the wage earners. On the other hand, although a great part of the "informal sector" employees is very poorly paid – below even the legal minimum wage levels – a part of the self-employed manages to obtain higher incomes than those of salaried workers in similar occupations (Souza and Tokman, 1978; Souza, 1980). In the more developed urban areas of Brazil, even the lower strata of self-employed workers manage to obtain higher incomes, on average, than those of salaried workers in manual occupations, as shown in Table 2.

Table 2 – Brazil: Relationship between the incomes of the lower strata of self-employed and salaried workers in non-agricultural activities, 1970 and 1974 Income from wages = 100

	Incomes from wages (Lower Strata) 1970 and 1974	Income from self-employment (lower strata) 1970	1974
State of São Paulo	100		150
Metropolitan São Paulo	100	108	
Rio de Janeiro State	100		119
Metropolitan Rio de Janeiro	100	93	
South Region	100		127
Metropolitan Porto Alegre	100	102	
Northeast Region	100		91
Salvador	100	70	
Metropolitan Recife	100	70	
States of Minas Gerais and Espírito Santo	100		109
Belo Horizonte	100	82	

Note: Definitions adopted:

Lower strata of wage earners:

1970 Manual and unskilled non-manual occupations

1974: Manual occupations

Lower strata of the self-employed:

1970: Self-employed in services, itinerant trade and construction

1974: Self-employed (non- established)

Source: 1970 -DEPE-UNICAMP (1980) based on the 1970 Demographic Census; 1974-FIBGE, National Household Expenditure Study, Rio de Janeiro, 1979.

In summary, the evidence available today leads us to the conclusion that the "exclusionary" characteristics of the Latin American capitalist development model have manifested themselves at two main levels: in the low wage levels that force a substantial portion of wage earners to live in conditions of extreme poverty (PREALC, 1979) and in the marginalization of a portion of the labor force that cannot even obtain incomes equal to those of the poorest wage earners, especially in the most backward metropolitan areas of the region.

In view of the above and given the limitations of a "paper" with the characteristics of the present one, we will leave aside the problem of employment growth in the modern sectors, and in manufacturing industry in particular, to concentrate on the currently most important theme of the evolution of wages. In this, we will analyze the evolution of industrial wages because we understand that their determination is endogenous to the industrial sector and because the wage patterns in manufacturing industry have a diffusing effect on the rest of the economy.

In determining the urban wage rate, the wage floor of manufacturing industry plays an essential role. In fact, this variable has a "spillover" effect on the wages of the other "modern" activities, even serving as a kind of "beacon" to the revenues of the so-called informal sector of the labor market (Souza, 1980).

In our view, however, the wage question suffers from the lack of an adequate theoretical body, which has led to serious confusions. On some occasions the series of average wages have been taken as an indicator of the evolution of workers' welfare (Simonsen, 1979; Von Doellinger, 1979) or of a supposed improvement in the general occupational situation, in an evidently tautological reasoning (Ramos, 1976).

These considerations led us to divide the present paper into two parts. In the first, we examine the theoretical issues related to wage determination in manufacturing industry. In the second, we analyze some available empirical evidence on the evolution of wages in the Brazilian manufacturing industry.

Wage determination in manufacturing industry: an outline of interpretation theoretical assumptions

The literature deals with the problems of wage determination from a dual perspective. In general, the analyses of the determination of the wage rate (from the classical school to the neoclassicals, including the "Cambridgesians") adopt the simplifying hypothesis of considering labor as a homogeneous "factor" or "commodity", disregarding wage differences. The analysis of the latter, in turn (for example, the theory of "human capital" or labor market segmentation), does not consider the level of wages. Obviously, what lies behind this methodological procedure is the assumption that the two variables

- wage rate and wage distribution - are independent. Our position is based on the principle that it is necessary to consider the level and structure of wages together, because there is a strict link between their basic determinants[6].

Although they are distinct concepts, the wage rate and the wage distribution are deeply linked to each other. Not to go too far, it is enough to consider that both must be compatible with the current consumption structure, which is an important adjustment element in any dynamic analysis that takes as its starting point the relationship between the wage rate and the rate of accumulation.

In order to consider the two variables together, it is necessary to make a small modification in the concept of the wage rate in relation to the current treatment in the economic literature. Thus, from now on, we will consider that the wage rate of an economy is the remuneration to unskilled direct labor in its truly capitalist core. This variable is, therefore, the wage floor upon which the distribution of wages is structured.

Despite the analytical distinction, in practice the link between the two concepts may reach a certain degree of interdependence. Thus, the value of the wage rate may condition, to a certain extent, the extent of wage differences: the lower it is, the greater the possibility of a more unequal distribution, and vice versa. In this sense, the wage rate is a theoretical unit of fundamental importance for the analysis of the problems of distribution and accumulation. The level of the wage rate and that of the wage distribution determine the wage pattern.

To understand the structure and dynamics of this wage pattern we must define the pattern of capital accumulation. To do this, we must first consider the pace of expansion of productive capacity and the sectoral growth structure of current production[7]. Secondly, we cannot fail to consider the input-output analyses that make productive differentiation explicit through the degree of intra and inter-sector integration[8]. Finally, we must also take into account the contribution of "industrial organization" analyses that point to the oligopolization of markets, emphasizing the growing importance of the power of large firms and unions in determining the structure of industrial prices and wages[9]. In summary, the pattern of capital accumulation must synthesize the key elements

6 The hypotheses used here are a derivation and deepening of previous work; see Tavares and Serra, 1971; Tavares, 1975, 1974, 1979; Baltar, 1977; Souza, 1978(a), 1978(b), 1980; Souza and Baltar, 1979; Possas & Baltar, 1979.

7 This is the approach adopted by the literature of the United Nations bodies, starting with the pioneering analyses of Svennilson (1954) and Prebisch (1949).

8 We refer especially to the pioneering work of Leontief (1952) and not to more recent developments in multisectoral general equilibrium analysis.

9 We understand that in this aspect the original contributions of Steindl (1946), Bain (1956) and the later one by Labini (1964) remain fully valid and up-to-date.

of the movement of the industrial structure, for which it is indispensable to take into account the forms of intercapitalist competition and the mechanisms of conflict and submission of the labor force in each industry.

The determination of wages and industrial organization

All firms, regardless of size, participate in the general labor market (“external” labor market in the conceptualization of Doeringer and Piore, 1971). Small companies tend to use it to meet all their labor needs; large companies recruit only unskilled workers or those needed to fill positions at the top of the hierarchical promotion ladder. This means that the conditions of this labor market are common to manufacturing industry as a whole. The prevailing wage rate is common to all industries and to all firms. In an economy where industrial capital is already dominant in the accumulation movement, we can therefore define the basic wage rate as the remuneration for direct unskilled labor in manufacturing industry[10].

On the other hand, large companies also operate with “internal” labor markets (Doeringer & Piore, 1971). The large-scale organization of the work process requires a functional division within the large company, which leads to the constitution of bureaucratized and hierarchical careers. For positions within the hierarchical ranks, recruitment takes place among the firm’s own workers. Working conditions – and wages – in these markets bear little relation to general labor market conditions. Trade union action, in turn, tends to reinforce and sanction the establishment of internal labor markets (Rubbery, 1978).

The domination that large companies exercise over a given industry, together with the similarity of their occupational structure, which largely depends on their technical conditions of production, can even lead to the creation of true internal labor markets for the industry. In this case, the similar conditions of the internal markets of each company are reinforced by the existence of unions by industry that tend to allow the mobility of workers between companies.

The joint operation of the “external” and “internal” markets allows the existence of a wage rate in force for the entire capitalist core of the economy, not being incompatible with growing sectoral disparities in remuneration. These disparities cannot be present at all levels of the workforce, which would

10 We understand that industrial capital is dominant when the manufacturing industry leads the growth of the economy, regardless of its absolute size or the weight (financial and political) of the other fractions of capital (agrarian, mercantile and banking). We therefore clearly detach ourselves from "Lewis"'s (1954) dualistic hypotheses, according to which income in the subsistence sector or, more recently, in the "informal sector" determines the wage rate of the economy (see, by the way, Souza, 1980).

lead to the establishment of different basic wages for each industry. On the contrary, the increasing salary differentials are verified especially along the hierarchical structures of the companies or industries, given that the internal labor markets – through which the differentiation is manifested – are valid only for the labor that enters to a functional career within the company [Souza, 1978(a)]. The unskilled work and part of what is necessary for the "entry" positions to each of these careers is recruited in the general labor market, in which all companies – large and small – in all sectors participate, also observing a high labor turnover. The wage rates of each sector or industry tend, therefore, to be equal without, however, there being a perfect identity between them. In other words, the basic wages are much less differentiated than the other remunerations and – what is important for our analysis – do not show a tendency to a growing distance between them.

We can therefore identify three wage variables at the level of each industry, which have some relationship with each other: the (basic) wage rate, the distribution of wages and the average wage in the industry. When we take the average wage of any industry, we are, in fact, considering a variable that implicitly contains a given wage rate and a given distribution of wages. This makes it possible to take average wage comparisons between industries in an economy as a kind of indicator of the degree of wage disparity, since the wage floor is common to the manufacturing industry.

In this sense, therefore, the average salary of each industry – given the level of the (basic) salary rate mentioned above – is the result of the action of several elements: trade union power vis-à-vis the market and political power of the leading companies; the differentiation of the occupational structure and the average level of productivity of the industry. This means that we can associate to each industry a certain degree of salary dispersion from a given basic salary rate for the entire economy, as we can also associate to each industry an average salary level. The fact that the average salary and the dispersion of salaries are determined by the same set of elements, does not mean that they are identical variables that can be taken "one for the other" in any circumstance. However, within an economy and given the common wage rate for the manufacturing industry, we can consider the average wage as an indicator of the degree of wage disparity in each industry. To simplify our analysis, we will refer to the problems of determining the average salary of each industry, without this meaning that we fail to consider the latter as a variable-result of wage differentiation, given the wage rate.

The negotiation between workers and entrepreneurs determines the nominal value of the salary rates. The way in which this negotiation takes place, admits two possible alternatives: is done at the level of each industry or at the global level of the industrial sector, when the existence of collective bargains and national confederation of trade unions allows it. Let us suppose initially that it takes place at the level of each industry.

Given the different market power in the different industries, the (basic) wage rate is the one that applies to unqualified direct labor in its "most vulnerable industry". The concept of "most vulnerable industry" should be understood as one where unions tend to exist with less strength, where the dominance of large firms is reduced , where "average productivity rates" are lower, since – among other things – the power of their leading firms to differentiate prices relative to primary costs is minor than in other cases. Therefore, their wage rate tends to be adopted as the wage floor in every industrial sector. If, for some reason, the wage rate were to be raised above this level (by legal imposition or by "strong" collective bargaining at the general level of the manufacturing industry), the industries that could not pay wages at this new level would have to undergo a process of drastic transformation, with the elimination of many firms, concentration of the production structure, renewal of their technical bases, etc.

Similarly, we can consider the second alternative, in which the negotiation between workers and employers takes place at the general level of the industrial sector, through the union confederation. In this case the (basic) wage rate is set almost directly and imposes a level to which industries must necessarily adjust. If it were relatively high, the difference with respect to the average wage rate of the manufacturing industry as a whole would be relatively small, and even more, both values would tend to move together (in the cycle); it would be impossible, in this case, the survival of industries with structures very different from the average conditions of concentration, productivity, etc., prevailing in the industrial sector as a whole. Thus, the technical progress introduced from the leading firms would more rapidly generalize throughout the industrial structure under the double impulse of intercapitalist competition and union pressure. If the level of basic wages were relatively low, the opposite would happen, and wage disparities would tend to be larger, as well as the conformation of a very heterogeneous industrial structure would be possible. As can easily be seen, state setting of minimum wages in this sense is only a special case of "collective bargaining" of a basic wage rate.

Industrial dynamics and wage movement

Based on a given nominal value of wages and raw material costs - which together form the direct or primary costs of production - companies set their prices through their market power, setting the respective "margins over primary costs" ("markups").

Real wages as a cost of each industry depend, in turn, on the value of nominal wages negotiated by the respective unions, modified by the relative price changes determined by the operation of the markups in each industry. An average level of the "degree of monopoly" for the entire manufacturing industry is derived from the structure of industrial markets.

This is the distributive parameter or "degree of monopoly" in Kalecki's definition that operates as a mechanism for adjusting the level of employment in the industrial economy to the aggregate movement of effective demand. This demand corresponds, in its turn, to the aggregate level of consumption and investment, considering that investment is the significant variable to the economy´s cyclical behaviour.

"Thus, capitalists' consumption and investment, together with the 'distribution parameters', determine the consumption of workers and, consequently, national production and employment. National production will rise to the extent that the profits they obtain, according to the 'distribution parameters', are equal to the sum of capitalists' consumption and investment" (Kalecki, 1954, 1977, pp. 96–7).

The distribution parameters mentioned by Kalecki that determine the wages share are the degree of monopoly and the relationship between the price of raw materials and wages. The degree of monopoly is measured by the ratio between the price of industrial products and direct costs (wages and raw materials) and is, no doubt, determined by several elements, both structural and circumstantial[11]. Among the first are the growth of firms and their power to induce market behavior, and among the second are the market power of firms in various industrial structures at each stage of the economic cycle, and the power of trade unions. For concentrated industries with large market power, the degree of monopoly will be higher in the depression and lower at the peak: in the depression, costs tend to fall (whenever the structure of the supply of raw materials is "competitive"), but indirect costs tend to increase and firms seek to defend their profit margins to compensate the fall in incomes, using their market power to mark up prices. Moreover, at this stage there is no possibility of new producers entering the market, so price competition is less important. At the peak, on the contrary, direct costs tend to grow, but indirect expenses fall, and the increase in turnover allows companies to reduce their profit margins without compromising their profitability (profit rate). This means that the increase in direct costs is not fully passed on to prices, which means that price competition is more acute at the peak.

11 Usually the measurement of the degree of monopoly is confounded with its determination, leading to the conclusion that Kalecki's formulation is tautological (see Kaldor, 1956; Ferguson, 1971).

In the case of less concentrated and/or more “competitive” industries, the movement of profit margins and final prices may be the inverse of the concentrated industry model. The sectoral composition of the manufacturing industry may thus cause the empirical analysis to show results of cyclical stability of markups at the overall manufacturing industry level[12].

On the other hand, the degree of monopoly also depends on the workers´ union power. Price markups can generate new wage demands, and so on. Certainly, union power has a long-term trajectory in each economy, but it also fluctuates with the economic situation, being higher at the peak and lower in a recession.

The relationship between the price of raw materials and wages influences the participation of each of these elements within direct costs[13]. Since the behavior of profits depends on the degree of monopoly and is influenced by the evolution of direct costs, one can conclude that the share of wages in the latter also influences their share in income.

In summary, therefore, effective demand and the distribution parameters jointly establish a given mass of wages. The mass of wages and the level of employment, corresponding to a given level of utilization of production capacity, determine the average value of wages in cost terms for the manufacturing industry as a whole. However, the real value of wages in terms of their purchasing power is different and depends, above all, on the price index of industries producing consumer goods for workers, an index strongly influenced by the prices of raw materials and the price index of food produced outside manufacturing industry.

Structural and cyclical changes in the process of capital accumulation interact with wage differentiation and sometimes affect the wage floor itself, by reducing or raising, not only for strictly political reasons but also because of modifications in the structure of production, relative prices and the composition of workers’ consumption that do not depend on their organizational power. The rise or fall of the wage floor may come from a change in the relative prices of primary products, which affects, in the opposite sense, the purchasing power of workers and the primary costs of manufacturing industry, producing an accentuation of wage demands with less or more dispersion of

12 This was the empirical test in the Kalecki model for the case of the American economy in the 1920s and 1930s, leading some authors of the English school to conflate the Kaleckian hypothesis with "normal prices".

13 Kalecki's essential assumption in this regard is that raw material prices are "demand-determined". In the cyclical downturn, the price of raw materials falls, as do wages, but the fall in wages has an additional effect on the fall in raw material prices, due to the decrease in demand for consumer goods. At the peak the opposite occurs, with the price of raw materials tending to grow more than wages. Again, it is worth mentioning that we are in the presence of compensatory trends and not in the "normal price model".

the wage gamut within the manufacturing industry as a whole, depending on whether there is an increase or decrease of the overall cost of the basic wage to the manufacturing industry.

Thus, the organization of the labor market (internal and external to the industry) and its dynamism, measured by the pace of capital accumulation, tend to determine (given a stable inter-industrial structure) the upward or downward movement of the basic wage rate. That is the reason why real wages and wage dispersion depend on more complex structural determinants than usually explained by traditional economic models.

Wage pattern and consumption structure

Returning to the starting point, to explain the movement of wages and productivity in manufacturing industry, we do not have a series of average wage levels differentiated by industry (as observed empirically), but a (basic) wage rate and a certain differentiated structure at all levels and along the manufacturing industry. This true range of differentiations will be more open the greater the "structural heterogeneity" of the manufacturing industry, the more highly concentrated its leading sectors are in relation to the others, and the lower the basic wage rate.

In its historical movement, this wage structure must be "adequate" to the broader functioning of the economy and correspond to a determined pattern of accumulation, which has implicit an inter- and intra-industry dynamics of production and a differentiation of consumption patterns that allows for the larger scale commercialization of current production.

In macroeconomic terms there must be *some correspondence* between the structure of wages, the structure of consumption and the productive structure of the industries producing these goods. This is not to say, however, that this correspondence is rigid, in the sense that the possible combinations are unique and mutually determined.

In reality, the "compatibility" between these structures is achieved by a series of intermediate instances, such as the production financing system, the consumer financing system, the tax system, foreign trade, etc., which allow a reasonable degree of flexibility in the adjustment between the three structures.

This degree of flexibility results in an important problem, of difficult approximation. If the relations between the three structures were rigid and univocal, it would not be necessary to ascertain which of them would have the predominant role over the others in their adjustment process, in which case any change in one of the three structures would mean the need for modifications in the others.

This is a particularly important aspect because the basic determinants of each of the structures are not necessarily the same. Thus, for example, we have seen that the wage structure has a set of main determinants linked to the same productive structure of the manufacturing industry in general and to the structure and power of the trade union organization. The structure of consumption in turn is related to the historical pattern of accumulation, that imposes an “urban lifestyle” on the working classes, It is also influenced by the productive structure of the departments producing consumer goods, that act through product differentiation, advertising, credit, etc., aiming at generalizing mass consumption to adjust it to the massive scale of production. The productive structure of the consumer goods producing departments, finally, is determined by the historical pattern of accumulation, being at the same time in permanent dynamic relation with the other economic sectors, especially those producing capital goods; one cannot even think that at the internal level of the consumer goods producing departments there exists a rigid correspondence between the productive structure itself and the type and quantity of goods produced. Not to go too far, a single plant in the automotive industry, for example, may, with certain adaptations, produce buses or “popular” or luxury automobiles.

The central point we wish to emphasize, therefore, is that each of these structures can be modified “independently” of the others. In any case the adjustment between them depends on the intermediate instances mentioned above. These instances are subject to a series of influences whose study belongs to the area of history and economic policy. However, we cannot fail to observe that in a capitalist economy in which industrial capital is dominant in the accumulation process, it will be difficult for any of these instances to bring up problems for a form of compatibility between the three structures that are “favorable” to industrial capital. In this sense, therefore (and only in this sense), one can say that industrial capital has a certain “primacy” in promoting the adjustment among the structures mentioned above.

In historical terms, however, it is possible that the changes in the various structures, pushed by different causes, be mutually beneficial or not (Tavares, 1975). The important thing is to point out that, in dynamic terms, it is impossible to conceive the idea of the realization of current production if the three structures are not in “conjunction”.

Summary and conclusions

In each historical pattern of industrialization, the structures of production and competition are determinants in first instance of market and consumption structures. The adjustment between these two structures involves the personal distribution of income, especially labor income, which differs more or less depending on the level of the basic salary.

The dispersion of productivities in the different industrial branches tend to be greater than that of wages since the former corresponds to a strong inter- and intra-industry technical heterogeneity. The basic salary, in turn, is valid for the entire manufacturing industry structure and the dispersion of salaries within each branch depends on the industrial organization and the internal labor markets of large companies.

In turn, the homogenization or differentiation of consumption patterns required to carry out the current production of leading companies profoundly affects the base levels of urban wages in the markets outside the manufacturing industry.

Two variables, size and industrial concentration, which correlate very well with productivity and intra-industry dispersion of wages, do not alone determine the market power of leading companies to control their profit margins. What is essential, directly for the "markup" and indirectly for (monetary) productivity, is the market power they can establish through barriers to entry, through diverse plants and product differentiation, among other mechanisms. This market power vis-à-vis the bargaining power of unions is what allows them to differentiate wages from a basic wage (common to all industries, thanks to the high turnover of labor that the existence of a market of work outside the manufacturing industry facilitates them). Whether differentiation at the level of an industry takes place or not depends much more on the strength of the trade union category, when it is organized by industrial branches, than on the heterogeneity of the set of industries that make up the category[14].

In summary, there is no univocal determination between salary structure, production structure and consumption structure, given that financing schemes, types of goods and relative prices can promote dynamic adjustment between

14 This conclusion is supported by the results of empirical investigations on the industrial structure, carried out recently in Brazil, at UNICAMP and FINEP, under the guidance of M. C. Tavares (see Gonçalves, 1976; Possas, 1977; Baltar, 1977; Tavares, Façanha and Possas, 1978). In Brazil, a growth of the medium wage closer to the productivity increase is observed in the group of the metal-mechanic and chemical industries at the expense of a greater dispersion of the remuneration of the workforce, not only by qualification, but above all by the conformation of the hierarchical structures that are related to the presence of large public and international companies in the leadership of the main sectors. In general consumer goods industries such as food, cigarettes, beverages and textiles, size is not associated with differences in productivity and much less in wages. Average productivity growth is accompanied by a similar increase in the average wage rate; the dispersion of wages is smaller, and the concentration of workers close to the basic salary is more accentuated.

the three structures within certain limits given by the general pattern of inter-capitalist competition. This is the one that historically allows the articulation of the productive structure of each industry, the expansion of the consumer market and the industrial capital power over the financial means of an "intermediation system" that is inherently "functional" during the expansion phase of each industrial cycle.

The Case of Brazil

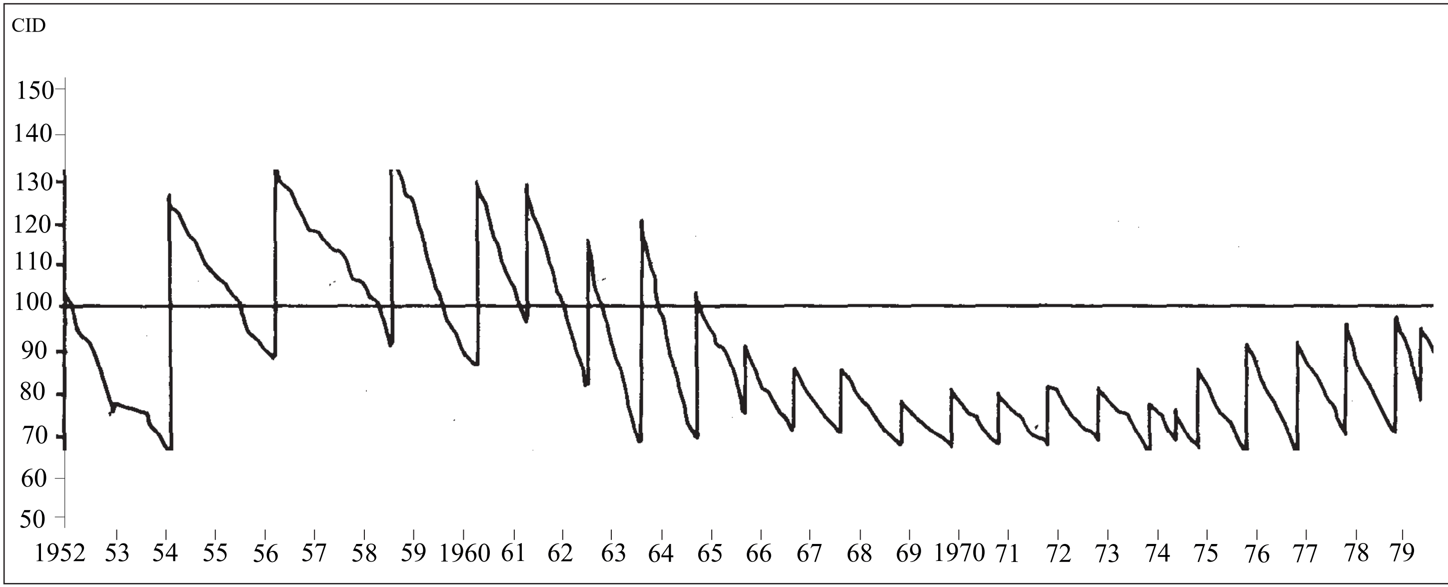
The wage rate of the Brazilian manufacturing industry

It is necessary to separate the determinants of the wage rate from the mechanisms that make them apparent. Thus, the entire set of factors mentioned in the first part of this paper are implicitly valid, even when the setting of a given wage level apparently results only from negotiations between businesspeople and unions. On the other hand, in the case of Brazil and many so-called underdeveloped countries, the State plays a very important role in setting the wage rate, through the minimum wage policy. Obviously the State does not have such a perfected "information system" that would allow it to establish precisely the wage level that is compatible with the set of determinants mentioned. The wage level set at a given moment will be compatible or not with them. If it is, it will be valid for a period; if not, it will be modified by price variations, by the effect of economic crises that interrupt the accumulation process, or even by the emergence of workers' protest movements[15].

The available evidence in the Brazilian case show that the legal minimum wage can be considered as the basic wage rate in Brazilian manufacturing industry during the last three decades. Graph 1 shows its real evolution in the 1952-79 period, when we observe its notorious variation in the period of economic crisis in the early 1960s and its reduction because of the policy imposed by the military governments since 1964. One can conclude, therefore, that the minimum wage level went from a relatively high level in the second half of the fifties to a level 40% lower than that, starting in 1967, to start a slow growth from 1974.

15 It is important to note that we are not claiming that crises or inflation are caused by an inadequate level of the wage rate. We simply say that these two factors can change wage rates, whether fixed by the government or by negotiation, if they are not adequate for the accumulation process.

Graph 1 – Evolution of the real minimum wage in São Paulo, 1952-1979 (January 1952 =100)



(Note) Monthly values deflated by the Fundação Getúlio Vargas Cost of Living index. As of 1962, the 13th salary was included by adding 1/12 of the real value of December of each year to the real salary of each month.

Source: DEPE/UNICAMP, research program on the labor market in Brazil.

On the other hand, the figures in Table 3 allow us to see how the lower levels of wages of such a specific union category as the metalworkers in the municipality of São Paulo followed the minimum wage level perfectly.. Likewise, some of the large industries in a sector as modern as the automobile sector currently have a salary structure in which 25% of their workers receive between 1 and 2.5 times the minimum wage. This evidence, together with the fall in the minimum wage during the 1960s, shows that it is important for determining the basic wage level even in larger industries[16]. In a recent work, an economist from IPEA showed that the wage levels of the lowest paid groups of workers in the manufacturing industry in Brazil were equal to those of the minimum wage in the peak period (1970-1974), which corresponds to the so-called "Brazilian miracle". In these years, the high rate of growth in the demand for labor should - according to the orthodox interpretation - have led to a detachment of the wage base from a minimum wage that remained constant in real terms.

The orthodox school of economic thought in Latin America in general and in Brazil in particular struggles between two extreme positions in relation to the importance of the minimum wage policy for the functioning of the labor market. It is sometimes argued that the minimum wage "artificially" raises the cost of labor relative to its "shadow price"; other times, the opposite argument is reached, postulating the inefficiency of the minimum wage to set wages, given that the market would take care of doing it. The first argument can be refuted with the simple observation that the minimum wage has been lowered over the recent period in Brazil, which suggests that the setting has an ordering effect on the wage rate: it can serve both to raise it and to lower it. The second has already been implicitly answered above. In fact, the empirical evidence on which the orthodox argument was based refers to the reduction in the proportion of people who receive wages close to the minimum, which has been observed throughout the current decade in the Brazilian case. However, this evidence doesn't contradict what we mentioned since, as the minimum wage followed the industrial wage base, wage differences grew notably, as we will see later[17].

16 Bacha and Taylor (1978) measured the elasticity coefficient between variations in the minimum wage and the median industrial wage in Rio de Janeiro, reaching a coefficient of 0.5 for the period 1952-1975. In a situation when the wage structure has become more unequal in Brazil, especially since the mid-1960s, as will be discussed later, this coefficient strengthens the argument that the minimum wage has indeed played the role of fixing the industrial basic wage rate in Brazil.

17 See in this regard Considera (1979).

Table 3 – Minimum wage and salary of unqualified workers in the category of metallurgists in São Paulo

	1956	1961	1966	1971	1976
Minimum wage in March (1961=100)	82.5	100.0	76.0	56.4	55.4
1st Decile in relation to the minimum (b)	1.00	0.99	1.00	1.00	1.18
2nd Decile in relation to the minimum (b)	1.13	0.99	1.00	1.00	1.31
3rd Decile in relation to the minimum (b)	1.20	0.99	1.00	1.07	1.35
4th Decile in relation to the minimum (b)	1.20	1.05	1.00	1.12	1.50
5th Decile in relation to the minimum (b)	1.29	1.08	1.05	1.21	1.58

(a) 1961=100.

(a) It is the relation between the salary that sets the upper limits of the decls in relation to the minimum salary in force.

Source: DIEESE, 1978, quoted by Souza and Baltar, 1979.

Average wage and the differentiation of the industrial structure

The average salary of the manufacturing industry had a different evolution from that experienced by the minimum wage. In general, over the period 1952-1974, a clear divergence between the two variables can be noted. Table 4 plainly illustrates the point, by noting the differences between the average wage and minimum wage indexes - both on the same basis.

We can, however, observe the existence of some periods of quite different behavior. During the decade of the 1950s, when we had both the minimum wage set at a relatively high level, and a reasonably active union power (at least in Brazilian terms), average industrial wages followed the evolution of the of the minimum wage[18]. In any case, this behavior is very variable at the level of the different branches of production.

18 It should be remembered that we are working with evolution indices that do not mean absolute differences between average and minimum wages.

Table 4 – Brazil, manufacturing industry: Indicator of the gap between the curves of the average real wage indices by industry and the real minimum wage in São Paulo (a)

Industries	Gap between the curves by period			
	1952-74 (b)	1952-59 (b)	1962-67 (c)	1968-74 (d)
Manufacturing industry (total average)	628.7	33.0	124.2	74.6
Metallurgy	465.4	8.4	149.7	52.2
Mechanic industry	484.7	-20.0	139.1	125.0
Transport material	363.4	-113.0	145.2	111.5
Electrical material and communications	368.9	-1.7	197.4	84.1
Pharmaceutical and chemical	1239.8	155.0	211.3	91.5
Paper and cardboard	637.4	50.0	98.7	98.5
Non-metallic minerals	402.6	10.8	108.9	82.0
Food products	582.7	95.7	89.5	59.4
Drink	497.6	2.0	84.8	88.2
Tobacco	966.9	112.3	174.3	96.8
Textile	436.2	37.5	69.1	86.7
Clothing and footwear	146.2	5.9	80.5	34.3
Leather, skins and similar	362.8	31.5	33.9	71.1
Wood	96.4	-44.3	75.2	101.7
Furniture	21.1	-56.0	106.6	72.2
Rubber	-77.9	127.9	201.6	92.8
Printing	433.3	55.3	116.5	115.4
Miscellaneous	450.0	87.4	122.1	136.5

(a) Corresponding to the area between the curves, calculated by the sum of the differences between the indexes.

(b) 1952=100

(c) 1962=100

(d) 1968=100

Sources of basic data: FIBGE, Census and Industrial Surveys.
Deflator: cost of living index in the city of São Paulo.

In several new metal-mechanical industries that were installed in the period, as is the case of transport material and electrical material, the evolution of the average salary is frankly unfavorable in relation to that of the minimum wage in the fifties, despite being "high wage" industries in absolute terms. The same is true for mechanical and metallurgical workers that, with the other two, make up a single union category in Brazil. This unfavorable evolution suggests that the metalworker's bargaining power was, contrary to what happens now, much weaker in comparison with the other worker categories. The largest expansion of the average wage in this period occurs in the chemical, tobacco, food, paper and cardboard, and printing industries. In the case of chemicals, tobacco and, to some extent, paper, there was a process of rapid growth and industrial concentration that clearly tended to diversify the employment structure, raising average wages, and introducing a broad differentiation in the structure of remuneration[19]. In the cases of the older industries - food and graphics - we have the presence of old trade unions that, at the time, were characterized by the political power of their actions.

In the period 1962-1967, characterized by the economic crisis, the reduction of the minimum wage and the fall in union power from 1964 onwards, there was a clear gap between the two curves of the average and minimum wages. In the years of the “economic miracle”, the gap between the average and the minimum wage gained new momentum, despite the wage base being “glued” to the minimum, as mentioned above. It is significant the average wage growth in industries such as metal-mechanical, chemical, and pharmaceutical, paper and cardboard and tobacco, sectors that have experienced a high growth rate and rapid processes of concentration of the industrial structure, with the penetration of new international groups (a typical case of the automotive and the tobacco industries).

In general, average wages have not kept pace with the productivity increase in the manufacturing industry. The regression lines of the product and the wage per worker index series, for the 1952-1974 period, have quite different angular coefficients: 9.1 and 3.9 respectively (see table 5). Furthermore, the industries that present the highest productivity growth rates are not necessarily those that had the largest increases in their average wages.

Nevertheless, in general, the industries that had slow productivity growth were the ones that increased their average salaries more slowly (the case of some “traditional” industries such as clothing, leather, wood, and furniture); there are three clear exceptions made up of the industries that were installed and developed in the period: transport material, rubber and electrical material, which started with high levels of productivity, registering a slow growth in this variable. This lower apparent productivity growth does not seem to be due to technological reasons since there was a substantial increase in production scales. It is due, rather, to the highly competitive nature of leading international companies (from different origins) in the search for expanding their participation in the market, which forced them to transfer the increase in productivity to prices[20].

The increase in scale in these industries produced an increasingly diversified occupational structure and the presence of large international assembly companies imposed greater internal wage diversification in the manufacturing

19 The Petrobrás, for example, was created in 1953 and is part of the chemical group, being one of the most active unions.

20 Indeed, there was a sharp drop in the relative prices of consumer durables, which was both a cause and a consequence of the strong expansion of the consumer market.

industry. For this reason, the differences between the coefficients of the productivity and wages lines of these three industries were the smallest of all industries.

The relationship between productivity growth and average wages can be more clearly observed by examining the angular coefficients of the regression lines for the periods 1952-1959, 1962-1967, and 1968-1974 (see table 5).

In the first period, corresponding to the 1950s, average productivity growth was not very high and showed a low degree of dispersion among the various industrial branches. The most notable exceptions appear in the tobacco, chemical and pharmaceutical, food products and miscellaneous sectors, branches in which there was a pronounced increase in the degree of concentration, which allowed for an increase in market power and markup. This contributes to raising the average productivity of these industries[21]. The angular coefficients of the average wage lines in this period confirm the observations made earlier with respect to the differences between average wages and the minimum wage[22].

Thus, in the branches where the degree of concentration grew, the average salary also increased at rates higher than the manufacturing industry average.

The second period, marked by the deceleration of industrial growth, presents a great dispersion of the angular coefficients of the productivity lines, with an average lower than the previous period. On the other hand, the average salary of the manufacturing industry maintained its growth rhythm, with substantial changes compared to the previous period in the relative positions of the industries as to the rate at which their wages increased. These grew more rapidly in the more “dynamic” industries, which experienced marked changes in their structure in the early 1960s. This is observable, for example, in the mechanical, transport material, electrical and communications material and rubber industries. We thus have the example of an increase in average wages concomitant with the fall in the minimum wage and the breakdown of union power. This increase seems to be due, therefore, only to the diversification of the occupational structure of the large international companies that lead these sectors, in a context of lower wage base.

21 This situation corresponds to the denationalization of important sectors of these industries by "takeover" of former international companies present in the fields for several decades.

22 The discrepancy between the regression analysis and the differences between the minimum and the average appears only in the graphics manufacturing industry.

Table 5 – Brazil: Manufacturing industry: Value of the angular coefficients of the regression lines (ACRL) of the indexes of the product per worker (PPW) and the real average wage (RAW): 1952-1974

	1952-74(a)			1952·59(d)			1962·67(b)			1968-74{c)		
Industries	(1) ACRL PPW	(2) ACRL RAW	(1) – (2)	(3) ACRL PPW	(4) ACRL RAW	(3) – (4)	(5) ACRL PPW	(6) ACRL RAW	(5) – (6)	(7) ACRL PPW	(8) ACRL RAW	(7) – (8)
manufacturing industry	9.1	3.9	5.2	6.4	3.1	3.3	5.5	3.1	2.4	9.9	5.9	4.0
Metallurgical	20.1	3	17.1	4.2	2.2	2.0	8.9	4.9	4.0	10.5	4.4	6.1
mechanics	8.8	4.4	4.4	5.0	1.3	3.7	16.9	5.2	11.7	4.5	8.3	3.8
transport material	2.8	4.1	-1.3	1.6	0.1	1.5	0.6	3.2	-2.6	6.4	3.9	2.5
Electrical material and communications	4.8	2	1.8	4.3	1.5	2.8	2.3	6.5	-4.2	5.8	4.0	1.8
pharmaceutical and chemical	11.5	6.3	5.1	9.9	10.0	0.1	8.9	4.6	4.3	10.6	5.3	5.3
Paper and cardboard	7.8	"3.5	4.3	3.8	3.5	0.3	5.4	0.4	5.0	18.1	6.2	11.9
Non-metallic minerals	7.1	0.6	6.5	2.8	1.7	1.1	8.7	1.1	7.6	9.9	6.5	3.4
Food Products	7.3	2.2	5.1	8.4	4.8	3.6	7.6	0.4	7.2	6.0	4.9	1.1
Drinks	8.3	3.3	5 7.5	5.3	4.1	1.2	1.7	1.2	0.5	14.3	5.1	9.2
Tobacco	12.5	4.9	7.6	11.4	6.0	5.4	4.8	3.9	-8.7	10.4	3.5	6.9
Textile	11.1	2.7 0.6	8.4	3.2	3.2	o.o	5.0	0.9	4.1	18.2	7.0	11.2
Clothing and footwear	4.6		4	3.9	1.4	2.5	1.1	0.3	0.8	7.4	4.3	3.1
Wood	6.8	1.2	5.6	4.0	1.6	2.4	2.3	1.2	1.1	14.2	6.7	7.5
Furniture	5.9	0.8	5.1	4.3	0.5	3.9	2.4	0.02	2.38	10.8	5.6	5.2
Rubber	1.8	1.6	0.2	2.0	-0.9	2.9	5.6	5.4	0.2	4.6	5.6	1.0
Publishing and graphical Editorial and Graphic	7.7	4.3	3.5	3.1	0.3	2.8	5.3	2.6	2.7	16.5	6.4	10.1
Miscellaneous	11.0	2.9	9.1	10.4	4.4	6.0	7.5	3.4	4.1	6.4	12.1	5.7
Leathers, hides and similar	4.9	2	2.9	3.0	3.5	-0.5	3.3	-0.4	3.7	11.2	5.4	5.8

(a) salary and product indexes 1952 =100; (b) salary and product indexes 1962 =100;

(c) salary and product indexes 1968=100.

Sources of original data: FIBGE, Census Industrial Surveys.

Finally, the period 1968-74 corresponds to the one with the highest growth in production, employment, and productivity in the entire post-war period. Average wages experienced a new boost, but were, however, well below the average increase in productivity. The only exceptions are observed in the mechanical, rubber and other industries. The first and the last are characterized by a disproportionate expansion of small and medium-sized companies in this period, which, nevertheless, must follow the wage standards of the respective industries, established by the evolution of the “internal labor markets” of large companies. In rubber, an extremely concentrated sector, the wage growth rate followed the average of the manufacturing industry and the wage standards of the large international companies that dominate the sector. Average productivity in this industry, however, grew well below the average for the manufacturing industry.

All this differentiated growth in wages and productivity in the last period (1968-1974) occurred under conditions of stability of the real minimum wage, as can be seen in graph 1.

Some conclusions

There is no reason to suppose, in principle, that productivity and wages must follow parallel paths. In fact, the “degree of monopoly” of the industry, explained both by the market power of large companies and by union power, does not tend to remain stable in fast-growing industries, with great structural diversification and sharp cyclical fluctuations. Precisely for this reason, in the case of the Brazilian economy, we cannot give a single explanation of the evolution, neither of productivity, nor of wages, covering the entire period analyzed.

As far as the evolution of wages is concerned, the fundamental changes seem to be due both to the collapse of union power after 1964, and to the change in the official policy of setting readjustments of the subsistence minimum wage and a posteriori indexation rates by the Ministry of Labor from 1964.

Until 1964, we had a more or less active union power and a high wage base until 1959. These two factors certainly contributed to shape a poorly diversified wage structure. This means that the average wage increases actually reflected the general increases at all salary levels. This manifested itself in a close link between the variations in the minimum wage and in the average industrial wage. On the other hand, the most active labor categories at this time belonged to the “old” unions of some “traditional” industries such as printing, food, textiles, etc. It is for no other reason that the upward trends in their wages were higher than those of other less organized groups such as metal-mechanics.

In the period of crisis, we had the reduction of the wage base and the breakdown of union power, resulting that the internal differentiations in the manufacturing industry could be expanded, sanctioning the hierarchical and bureaucratic gradations. The industries where there was a sharp growth in the average salary in this period were precisely those characterized by diversified occupational structures and by the "coexistence" between large, medium, and small companies (as in the metal-mechanic group).

In the period 1968-1974 production growth reached really high figures. There was also an increase in average wages in practically all industries, with higher rates in industries with a diversified occupational structure. It is recalled that the salary base remained at the level of the minimum wage as mentioned above. Salary disparities, on the other hand, reached very high levels, considering the short time they occurred. Table 6 gathers information on large industries in São Paulo, showing that between 1969 and 1975, low wages grew by 16%, while medium wages grew by 35%. High wages, on the other hand, grew by 63%. On the other hand, the work by Considera (1979) shows that high wages in the manufacturing industry between 1970 and 1974 grew 45% more than low wages.

The widening of wage differentials, together with the fall in the relative prices of consumer durables, allowed the adjustment between an unequal distribution of income and the new consumption patterns. These, in turn, progressively differentiated for the high-income strata and extended to the lower-middle strata by the considerable increase in their debt capacity stimulated by the new, and very dynamic, developments of the financial system. Thus, the logic of market expansion for the industries was made explicit, as we pointed out before, through the characteristics of personal income distribution, indebtedness schemes and consumption patterns, configuring at this more concrete level the general capita accumulation pattern of the Brazilian economy in the recent period.

Table 6 – São Paulo: Real wage rates for different categories of workers in the manufacturing Industry 1969-75

Categories of workers	1969	1970	1971	1972	1973	1974	1975
Low salaries (average of 27 positions)	100	106	110	107	107	110	116
Medium wages (average of 28 positions)	100	109	114	120	123	132	135
Medium-High wages (20 position average)	100	105	117	128	129	133	142
High wages (24 position average)	100	118	127	136	142	150	163

Source: Several salary investigations by specialized companies, cited by Suplicy (1977), p. 74.

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CHAPTER 11

FOREIGN DEBT AND TRANSFER OF REAL RESOURCES ABROAD: the public and private sectors in the crisis of the 1980s

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The fiscal and financial crisis of the Brazilian State – which marks the agony of the military regime in the first half of the 1980s and which continues to this day – is closely associated with the liabilities accumulated by the public sector, notably that resulting from the process of foreign indebtedness occurred after the 1964 military coup. More specifically, the form taken by the crisis in the 1980s is indissolubly linked to the cycle of foreign indebtedness/nationalization of debt/transfer of real resources abroad and to the relations between the public and private sectors established in the different phases of this cycle.

I

It is customary today to speak of the nationalization of the Brazilian external debt, a process through which the State has increasingly expanded its participation in the stock of debt contracted with financial organizations and private international banks. However, reasons for this increase in participation – which reached percentages above 80% in the mid-1980s – are still controversial, if not misunderstood.

From our point of view, the proper discussion of the nationalization movement must start from the preliminary distinction of two dimensions of the indebtedness process carried out in the national economic space. On the one hand, external indebtedness needs to be seen from a microeconomic perspective, that is, the determinants that induce agents – private and public companies, in general – to contract them. In this case, considering the conditions of the offer of international credit, what the analysis privileges is the sphere of competition, of individual capital accumulation, decisions regarding investment portfolio and their form of financing, etc. It should be noted, from this micro perspective, that the borrower of foreign loans is not always the

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user of the corresponding foreign currency. In the case of loans in currency, there may be a dissociation where foreign credit serves as an instrument for mobilizing resources in local currency for the contracting companies, while the foreign currency is sold to agents who demand it to make payments abroad.

On the other hand, foreign indebtedness must be analyzed as a component of the balance of payments capital account and, as such, as a way of financing current transactions carried out by the country with the rest of the world or as a generator of balances that will be accumulated in the form of foreign exchange reserves. Here, it is a matter of the macro perspective that comprises the aggregated results of all operations carried out in foreign currency by economic agents resident in the country. It is obvious that the results of the balance of payments, the product of an anarchic set of foreign and domestic decisions, constitute one of the main determinants of the decisions taken by companies which get foreign loans. But its influence on such decisions does not come directly through self-corrective or balancing mechanisms. It is mediated by state regulatory action which, in addition to imposing general rules for operations denominated in foreign currency, changes relative prices, and acts on individual decisions in order to ensure certain global results in the external accounts, compatible with other economic policy objectives.

As an example, it is worth remembering that after the military coup, and during the 1960s and 1970s, the actions of the Brazilian government were decidedly stimulating the inflow of foreign capital. As a matter of fact, the fight against the much-vaunted xenophobia of João Goulart's administration was one of the main banners of the military and its allies, who had the declared objective of restoring a scenario broadly favorable to foreign capital. Shortly after the coup, the legislation on foreign capital was modified – with the inclusion, for example, of reinvestments in the calculation basis of profit remittances – while expropriation/nationalization processes involving foreign subsidiaries were suspended, or satisfactorily resolved from the point of view of the interests of the foreign capital[2].

Simultaneously, measures were taken to facilitate the massive inflow of loan capitals that were beginning to become abundant in the Eurocurrency Market. Alongside specific provisions, the institution of inflation indexing for financial assets and the exchange rate policy of currency mini-devaluations that allowed the practice of real domestic interest rates higher than those observed in the international credit market were fundamental. From then onwards, except for some circumstances and disregarding any differences in emphasis, exchange rate, monetary and fiscal policies were conducted by the

2 For an account of the issue of foreign capital in the early 1960s, see Bandeira (1967).

military administrations to guarantee, in the microeconomic sphere, a high level of attractiveness for foreign loan operations.

The deliberate action of military administrations to stimulate, or even induce, business decisions in favor of foreign credit was based, at the macroeconomic level, on the thesis of the scarcity of real resources, that is, on the idea that foreign indebtedness would have the function of financing the balance of payments deficit in goods and productive services transactions that would necessarily accompany the accelerated growth trajectory of a backward economy[3].

II

Having made these preliminary considerations, let us focus our attention on examining the ways in which the foreign debt was progressively concentrated in the hands of the Brazilian State and on the consequences of this process in the crisis of the 1980s. Before that, and as a requirement for further analyses, let us make a brief review of the first phase of indebtedness carried out under the aegis of the military regime – from the late 1960s to the mid-1970s – when foreign loans were contracted primarily by the private sector.

It is easy to see, from the outset, that foreign credit represented, from a microeconomic point of view, an extremely attractive financing alternative for large companies, especially for foreign subsidiaries, in the expansionary phase. First, these operations meant an expansion of long-term credit – a modality for which the domestic private financial system has historically been unable to meet -, in a context of strong acceleration of investments in the manufacturing industry. Second, they constituted a form of credit with relatively low costs given the conditions of the international supply and government incentives and subsidies. Foreign subsidiaries also obtained additional advantages, as they had preferential interest rates contracted directly by their headquarters with international banks. Furthermore, foreign subsidiaries replaced substantial volumes of foreign direct investments with loans, given the greater permissiveness of the legislation regarding remittances abroad in this second modality of capital inflow.

Apart from operations contracted directly by a company with an international bank, operations intermediated by local financial institutions also proliferated. Through this mechanism, commercial banks and investment banks internalized large amounts of resources from the financial system of Core countries. Foreign commercial banks with subsidiaries located in the country were particularly agile in this type of operation, transferring funds

3 For a discussion of the indebted growth model and for a description of the main government measures, see Pereira (1974), Cruz (1984).

from their respective headquarters to private companies with less direct access to the international credit market.

The high attractiveness of this form of resource mobilization in the expansionary phase is attested by the generalization with which foreign credit was contracted by private companies in the most diverse sectors of activity, notably in the manufacturing industry. Foreign borrowing was more intense in the second phase of the expansion cycle, starting in 1970, when, after exhausting idle capacity, the Brazilian industrial sector experienced a strong acceleration in its investment rate. From the aggregate point of view, from the balance of payments point of view, the absence of any more significant scarcity of real resources implied that the intense foreign indebtedness resulted in a large accumulation of international reserves[4].

III

The "nationalization of the foreign debt" – a process of progressive concentration of the debt stock in the hands of the Brazilian State – began in the mid-1970s and presented two major stages. In the first, which roughly intertwines the two oil shocks, the increase in state participation resulted from the greater participation of public entities in the annual flows of new loans. At this stage, state-owned companies were the vehicle, par excellence, of this nationalization.

In the second stage, which began at the time of the interest rate shock and the 2nd oil shock, state companies, now accompanied by direct administration bodies, further increased their weight in the flow of new loans. But what gives specificity to this second stage is the transformation of the Central Bank into a growing depository of foreign liabilities, either through the massive transfer of old debts, originally contracted by the private sector, or through the deposits of projects arising from the system of negotiation established in 1982, after the interruption of voluntary lines of credit. Let us take a closer look at each of these steps.

The first phase of the nationalization of the Brazilian foreign debt, as already pointed out, had as a key characteristic the growing weight of the public sector, especially state-owned companies, in the annual contraction of new foreign loans. Regarding bank loans traded directly under Law No. 4131, for example, the share of the public sector rose from 35% in 1974 to 60% in 1978 (Table 1). What were the determinants of this first advance in nationalization?

4 For an analysis of the different types of foreign credit and the behavior of the public and private sectors, see Cruz (1984).

Table 1 – Bank loans (law no. 4131) Structure of the annual gross income according to the ownership of the borrower's capital (1972-1985)

Discrimination	1972		1973		1974		1975		1976	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Public	623.1	24.9	1,130.9	39.7	1,098	35.3	1,900.9	50.4	1,953.3	51.1
Private	1,874.4	75.1	1,718.3	60.3	2,011.5	64.7	1,872.1	49.6	1,872.7	48.9
Total	2,497.5		2,849.2		3,109.5		3,773.0		3,826	
Discrimination	1977		1978		1979		1980		1981	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Public	2,500.5	51.5	5,317.4	60.2	6,642.9	76.8	3,687	76.6	5,285.5	69.6
Private	2,356.9	48.5	3,511.5	39.8	2,007.4	23.2	1,124.1	23.4	2,311.1	30.4
Total	4,857.4		8,828.9		8,650.3		4,811.1		7,596.6	
Discrimination	1982		1983		1984		1985			
	Amount	%	Amount	%	Amount	%	Amount	%		
Public	6,196.3	73.8	2,297.6	74.9	5,589.6	88.0	7,636.1	88.7		
Private	2,202.8	26.2	768.7	25.1	759	12	972.1	11.3		
Total	8,399.1		3,066.3		6,348.6		8,608.2			

Sources: For the period 1972/1981, see Cruz (1984); for 1982/85, see Biasoto Jr. (1988).

To answer this question, it is worth remembering, above all, that the Brazilian economy in the mid-1970s, under the international crisis impact, showed clear symptoms of exhaustion of the previous expansion ***boom***, such as: deceleration in output growth; loss of dynamism of private investments; strong imbalances in the balance of payments; rising inflation rates etc. At the same time, the military government launched the Second NDP (National Development Plan), an ambitious import-substituting program that aimed to give the definitive impetus to Brazilian industrialization. This program attributed a prominent role to state companies, which would be responsible for carrying out crucial projects in the areas of infrastructure and basic inputs (Lessa, 1978; Castro, 1985).

The feasibility of the task imposed on state-owned companies would take place through a financing scheme whose outlines were defined according to macroeconomic criteria and not according to a microeconomic logic. In fact, the financing scheme designed by the military government served global economic policy objectives and favored a source of resources, namely, foreign credit. The macroeconomic justification for this option rested, as always, on the thesis of the scarcity of real resources. State companies, by massively resorting to foreign indebtedness to provide funds, in local currency, for their projects, would be providing the country with the inflow of much-needed foreign currency to face the deficit in the goods and productive services account. It was also argued, of course, that the conditions regarding volumes, terms and costs of foreign credits were perfectly adequate to the needs of the projects to be financed and compatible with the financial flows of state companies.

It is true that the achievement of the stated objectives regarding the balance of payments supposed the participation of private capital. It should be remembered that large private capital, notably subsidiaries of foreign corporations, had already played a leading role in the foreign indebtedness carried out in the immediately previous period. However, despite the new measures to stimulate the deepening of private indebtedness – ***hedge mechanisms*** (regulation 230 and instruction 432), interest rate differential, etc. -, the behavior of private companies was cautious in view of both the new international scenario and the deceleration of private investment growth[5].

Given these elements, which set the framework in which the first advance of the nationalization of the debt took place, it is now necessary to direct our attention to the crucial role that the foreign indebtedness of state-owned companies played in the forms of management and solidarity of different private interests promoted by the military government of that time. In fact, the option for this alternative of financial mobilization conferred various degrees of freedom to state action in a context of intensifying competition for public resources.

The most conspicuous example is given by the price and tariff policy of state-owned companies, which, freed from ensuring funds for investments, was primarily operated as an instrument to fight inflation and as a mechanism for granting subsidies to the private sector via a change in relative prices. It is notorious, in the period, the containment of prices and tariffs of infrastructure sectors and of those producers of general-purpose inputs that, curiously, were at the very core of the Second NDP and demanded huge resources for their investments[6].

Another eloquent example is provided by the allocation of funds mobilized by the BNDE (Brazilian Development Bank) in the period. The massive use of foreign credit by state companies allowed the financial reinforcement attributed to the BNDE (PIS/PASEP) to be directed, in the form of subsidized credit, almost exclusively to private capital. A final example shows that while state-owned companies increased their indebtedness with international private banks, the central government was expanding the range of subsidized credits for agriculture, for the export industry, for small and medium-sized companies, etc. As a whole, subsidies and incentives granted in the federal area rose from 3.0% as a proportion of GDP in 1973 to 7.6% in 1980 (Table 2)[7].

In conclusion, foreign indebtedness played a fundamental role in the state's financial leverage, allowing the attempt to reorganize the productive structure to be conducted while preserving solidarity of a wide range of private

5 For an analysis of the behavior of the private sector regarding foreign loans in the period, see Cruz (1984). It should be noted that the inflection in the behavior of private capital took place precisely at the time when expressive deficits in the balance of goods and productive services appeared (1974/76).

6 On prices and tariffs of state-owned companies in the period, see Trebat (1983).

7 For a discussion of the evolution of subsidies in the second half of the 1970s, see Braga (1982, v. 2.).

interests receiving subsidized public funds. It is obvious that one of the main costs of this option was the accumulation of high liabilities denominated in foreign currency by state-owned companies, whose unbalancing potential was fully manifested in the balance of payments crisis of the turn of the decade.

Table 2 – Main subsidies (a) and tax incentives in federal area 1973/80 (% of GDP and Tax Revenue of Nat. Treasure)

Subsidies Incentives	Years							
	1973	1974	1975	1976	1977	1978	1979	1980
Incentives/GDP	2.7	3.5	3.5	3	3.4	3.5	3	1.7
Incentives/Tax Revenue	28.1	35.8	39.7	31.2	37.5	39.8	39.5	21.5
Subsidies/GDP	0.4	1.3	1.7	2.4	2.5	1.9	3.2	6
Subsidies/Tax Revenue	3.8	13.1	19.8	24.8	27.4	21.9	40.9	77.8
Subsidies + Inc./GDP	3	4.7	5.2	5.4	5.9	5.5	6.2	7.6
Subsidies + Inc./Tax Revenue	32	48.9	59.5	56	65	61.7	80.3	99.3

Source: Langoni (1981). Bases Institucionais da Economia Brasileira.

a) Implied to credit (agriculture, export); direct (wheat, oil, soy, sugar).

b) Explicit to credit (PROAGRO, FUNDAG); purchase and sale of agricultural products (minimum prices and regulatory stocks).

IV

The second phase of the process of nationalization of the Brazilian foreign debt began in 1979 and lasted until the mid-1980s. At this stage, the public sector further expanded its participation in the annual flows of new loans, reaching a percentage close to 90% of direct borrowings carried out under Law No. 4131 (Table 1). But the uniqueness of this period is the intensive use of foreign exchange hedging placed by the Central Bank at the disposal of the private sector – in the form of Deposits Registered in Foreign Currency (DRFC, or DRME, in the Portuguese acronym) – and in the transformation, in fact, of the Central Bank in borrower from international banks (project deposits). As a result of these new nationalization movements, the stock of deposits denominated in foreign currency in the Central Bank's liabilities reached the figure of US$ 27 billion at the end of 1985[8].

To begin the specific discussion of this second phase of debt nationalization, it is necessary to remember that, from an international point of view, the period we are dealing with was marked by an extremely adverse scenario for peripheral countries, as evidenced by the oil and interest rate shocks, the

8 This amount includes deposits derived from Paris Club refinancing. It also includes deposits made by state companies (Biasoto, 1988).

recession in the core capitalist economies, the rupture of the international credit market for non-core countries, the IMF re-entry on the scene, etc.

The international crisis imposed a progressive balance of payments constraint on the Brazilian economy, initially manifested in sharp current account imbalances – given the weight of oil on the import list and the volume of debt contracted at floating rates – partially financed by medium and short-term credits and partially through declining international reserves. At that time, large creditor banks, with portfolios full of increasingly doubtful assets and with funding problems, were already beginning to reduce volumes, shorten terms and increase loan spreads for countries considered to be of high risk (Batista, 1983).

The currency crisis culminated, at the end of 1982, with the interruption of the flow of international bank credit to backward countries and had as its most important consequences the global debt negotiations and the adjustment policies of the external sector imposed by the creditor bank cartel and by the IMF. Over the period in question, the Brazilian economy moved from a position of absorber of foreign resources to a position of net exporter of capital, through the generation of mega trade surpluses.

The advance of nationalization of the foreign debt that took place in the period, a topic that interests us more closely, resulted, to a large extent, from the currency crisis, the adjustment policies and the negotiations with the banks' cartel and the IMF. Otherwise, let us analyze. The military government's initial response to the aggravation of current account imbalances was the attempt to induce a greater volume of foreign credit contracting[9]. However, a complicating factor on the domestic demand side was added to the adverse conditions of credit supply, namely: private capital, which had already been in an attitude of relative caution, started to show a clear behavior of flight of liabilities denominated in foreign currency. The explosion of international interest rates, the country's exchange rate instability, the erratic movement of economic policy and the recession that began in the late 1980s explain the lack of interest of private companies in contracting foreign credit.

The military government's option, once again, was to use to exhaustion state companies and some public bodies of direct administration – including states and municipalities – as vehicles for contracting new foreign loans. These new loans – with increasingly unfavorable terms and costs – had little or nothing to do with the investment projects of the state-owned companies, which became scarce during the crisis, basically aimed at providing foreign currency at the macro level, to address imbalances of balance of payments.

9 On the measures adopted, see Cruz (1984).

In addition to the indebtedness of state-owned companies, a new channel for the nationalization of the Brazilian foreign debt was added, namely: the massive transfer of still maturing debts to the Central Bank, originally contracted by the private sector (DRFC). In fact, private companies fled not only from new contracts but also from old ones, that is, those assumed during the 1970s and with installments still to mature. During this period, and notably in the moments that preceded the cruzeiro maxi-devaluations, the hedge mechanisms (Instruction No. 432 and regulation No. 230) were widely used and constituted an important part in the financial adjustment carried out by private capital[10]. On the other side, by financing the monetary authorities in local currency, the DRFC meant the transfer of contractual obligations to the State, denominated in foreign currency in a context of sudden increase in international interest rates and the exchange costs of operations[11].

The last conduit for nationalization of the Brazilian foreign debt was instituted at the end of 1982, during negotiations with the creditor bank cartel and with the IMF. In addition to intensifying the aforementioned trends, global renegotiation gave rise to a new mechanism – project deposits – through which the Central Bank ended up acting as the final borrower of foreign loans (Biasoto Jr., 1988).

As it is well known, the renegotiation determined an important change in the micro/macro relations of the foreign indebtedness process of the country. From then on, creditor banks, acting in an explicitly cartelized manner, began to define a specific global credit availability to Brazil and to impose internal policies that ensured the trade surpluses that enabled those restricted financing quotas. In this process, the volume, and conditions of credit to be contracted by the country in each period – to finance part of the interest and refinance amortizations (Projects 1 and 2) – came to be agreed directly between the banks' cartel and the Brazilian government, without the intervention of individual agents taking foreign credit.

Because of this change in micro/macro relations, project deposits and relending emerged. Under the terms of the agreement, foreign funds contracted without prior definition of a final borrower would be deposited with the Central Bank, in the name of the respective creditors. During the deposit period, all debt services would be the Central Bank's responsibility. At the same time, the banks holding the accounts were allowed the free movement of funds for application in credit operations to internal final borrowers (relending).

10 The equity and financial adjustment carried out by large private capital is examined in FUNDAP (1989).

11 It should not be forgotten that, in the same process, the Brazilian government issued large volumes of bonds with an option clause for exchange rate correction (ORTN-exchange).

Given the flight of private capital from liabilities denominated in foreign currency, the resources of Projects 1 and 2 had two main destinations: either they were lent to state companies – subjected to strong financial strangulation, as will be discussed below – or they remained deposited for a long time with the Central Bank itself, which acted as the final borrower. Here is the culmination of the process of nationalization of the Brazilian foreign debt.

Before moving on to the discussion of the consequences of this process, let us briefly review the main points raised. As seen, the first stage of the nationalization process, which took place in the second half of the 1970s, resulted from the financing pattern imposed by the military government on state companies responsible for the 2nd NDP projects. This option, by widening the bases of state financial mobilization, allowed the directing of subsidized resources to a wide range of fractions of private capital and, in this way, contributed to the legitimacy of the military regime itself. However, oil and interest rate shocks charged a high price for this option. State-owned companies, already heavily indebted in foreign currency, were impacted by rising interest rates and exchange rate devaluations as part of the export effort.

Unlike private companies, which quickly and with government support developed equity and financial adjustment mechanisms, state-owned companies were forced into a snowball indebtedness. Once again subjected to restrictions imposed by the central government, such companies became prisoners of an increasingly deteriorated equity and liquidity situation. While private firms, notably subsidiaries of large foreign groups and export-oriented groups, became net investors in financial assets, state-owned companies, as will be discussed, were pushed towards widespread default.

But not only the sate-owned companies acted as absorbers of the costs of the crisis. The central government, through the DRFC with the Central Bank, assumed a significant portion of the liabilities associated with foreign credit. Private capital, in anticipating the liquidation of its debts, escaped exchange rate and interest rate shocks, transferring their effects to the non-monetary liabilities of the monetary authorities. Furthermore, given the terms of the renegotiation with the creditor banks' cartel, the Central Bank was responsible for directly covering the cost of turning over a growing stock of foreign debts. It can be seen, therefore, that the nationalization of foreign debt was a powerful instrument for socializing the burden of the crisis, for committing public funds in favor of the preservation of international banking capital and privileged fractions of private capital operating in the country.

V

Let us now examine some of the implications of this process. Let us remember, to start the discussion, that as of 1983 the Brazilian economy entered a new phase in its external economic relations, becoming a net exporter of real resources to the advanced capitalist economies. Indeed, the generation of mega trade surpluses was our economy's main response to the stranglehold imposed by the international crisis and the cessation of bank capital flows from core countries[12].

The transfer of real resources abroad had, in turn, several consequences for the Brazilian economy, among which we are interested in highlighting those associated with the nationalization of the foreign debt. First, we must bear in mind, at the micro level, that the remittance of resources abroad is made by public entities (state companies, direct administration bodies and the Central Bank) that have become responsible for almost all of the foreign debt and, therefore, for its contractual obligations. At the same time, public entities contribute little to the direct generation of the currency to be remitted. The export balance is produced by private capital and acquired by the public sector with an equivalent amount in local currency.

Such internal transfer of resources would not raise major problems since the nationalization of the foreign debt had been accompanied by a redistributive process in favor of the public sector as a way of providing local monetary balances for the acquisition of dollars to be remitted abroad. However, as paradoxical as it may seem, the public sector, instead of expanding, lost its relative position in the country's internal income in the period considered[13].

According to national accounting data, which exclude state-owned companies, the loss of relative position is evidenced, above all, by the behavior of the gross tax burden in relation to GDP, which fell from 25% in 1980 to 22% in 1985 (Table 3). Despite the reduction in subsidies observed in the period, the pressure of interest on foreign and domestic public debt caused the net tax burden to fall from 12.1% of GDP in 1980 to 9.7% in 1985. Given the relative rigidity of current expenditures, public sector savings, which were already at relatively low levels in 1980, disappeared in 1985. Thus, the transfer of real resources abroad had, as a counterpart, a drastic reduction in the investment capacity of the Brazilian public sector in the period.

A long digression is not necessary to show that the fiscal-financial stranglehold on the public sector was aggravated by the very format of the adjustment policies aimed at generating trade balances. Citing only three examples,

12 For an appreciation of the nature of the trade surplus in the 1980s, see Carneiro (1991). For alternative view, see Silva (1984), Castro, Souza (1985).

13 On the impact of resource transfers on government savings, see Werneck (1987).

the impact of active currency and interest rate policies on inflation levels and output levels and, in this way, on the gross tax burden; the effects of real interest on the cost of the internal debt, whose stock grew significantly because of the adjustment policy itself; and, finally, the tax exemption resulting from the export promotion policy, with its consequences on the tax burden.

Table 3 – Brazil Government Savings in Current Account 1980/85 (% of GDP)

Items	1980	1981	1982	1983	1984	1985
Gross Tax Burden	24.7	24.5	25	24.7	21.4	22
Direct Taxes	11.2	11.7	12.6	12.1	11.2	11.7
Indirect Taxes	13.5	12.9	12.5	12.6	10.2	10.3
Transfers	12.6	12.2	13.2	13.9	12.9	12.4
Interest on Internal Debt (1)	0.8	1.1	1.2	1.5	2	2.3
Interest on Foreign Debt (1)	0.4	0.3	1.1	1.6	1.7	1.5
Social Security	7.8	8.2	8.5	8.3	7.6	7.1
Subsidies	3.7	2.7	2.5	2.6	1.6	1.5
Net Tax Burden (2)	12.1	12.3	11.8	10.8	8.5	9.7
Government Consumption	9.2	9.3	9.9	9.5	8.1	9.7
Personnel	6.3	6.4	7	6.5	5.5	6.8
Goods and Services	2.9	2.8	2.9	3	2.6	2.9
Savings	2.9	3.1	1.9	1.3	0.3	0

Source: Central Bank of Brazil/DEPEC – Public Sector Macroeconomic Indicators.

1. Until 1982, the interest on the internal debt corresponded to the concept used by the FIBGE, discounting the monetary correction of the treasury bonds and the discount of the treasury bonds. From 1983 onwards, both the interest on the domestic debt and on the foreign debt was estimated based on the average balance of public sector debt.
2. Excludes other current net income.

This inability to generate resources to deal with remittances abroad was determined, in turn, by the ways in which the central government managed both the prices and tariffs of state-owned companies and the transfer of resources from the Treasury to these companies. The tariffs and prices of public services and goods, which had already been managed as part of the anti-inflationary policy, suffered a new real fall from 1983 onwards, now with a view to providing an exchange rate/local costs ratio favorable to the export *drive*. In this respect, the behavior of prices in the electricity and steel sectors, which fell sharply in the period, is emblematic. As a result of the price and tariff policy, the real operating revenues of the state productive sector were situated, on the average of the 1983/85 triennium, about 10% below the values observed in 1980 (Table 4)[14].

14 For an analysis of the economic-financial performance of state-owned companies, see Werneck (1987), Pagano (1991).

Let us now see, in a little more detail, the effects of the internal transfer of resources on state-owned companies. As it is well known, these companies have little direct participation in generating the export balance given their historical role as a supplier of infrastructure and basic inputs to capital operating in the country. In the historical model of Brazilian development, since the creation of the so-called "tripod" (foreign capital, domestic private capital, and state firms) in the fifties, state-owned companies were molded to a type of action aimed almost exclusively at the domestic market.

The intense indebtedness experienced by government companies from the mid-1970s did not substantially change their form of insertion in the country's productive structure in such a way that the growth of foreign currency obligations – resulting from the stock of foreign debt, from rising international interest rates and currency devaluations – was not accompanied by greater export potential[15]. Soon, state-owned companies experience net operating losses in their foreign currency transactions. Simultaneously, they proved incapable of generating balances in local currency for the acquisition of the missing currencies.

Table 4 – Selected data for the state productive sector, except for PETROBRAS 1980/85 (billions of Cr$ 1980)

	Operating revenues		Treasury Resources		Investments		Personnel and expenses		Interest		Short Term Credit (1)	Credit Total (1)	
	value	index	value	Index	value	Index	value	Index	value	Index	value index	value	Index
1980	757.1	100.0	190.3	100	457.8	100	248.6	100	104.3	100	0	377.4	100
1981	664.6	87.8	155.9	81.9	450.4	98.4	200	80.4	158.4	151.9	31.2	397.2	105.2
1982	655.3	86.6	125.9	66.2	414.1	90.5	213.3	85.8	212.5	203.7	21.5	422.2	111.9
1983	591.6	78.1	92.7	48.7	282.1	61.6	172.2	69.3	221.4	213.3	100.3-	329	87.2
1984	668.1	88.2	98.7	51.9	273.1	59.7	152.5	61.3	273.1	261.8	25.9	448.9	118.9
1985	769.7	101.7	115.6	60.7	278.1	60.7	178.6	71.8	300.8	288.4	232.8	507.7	134.5

Source of raw data: SEST. Extracted from Pagano (1991).

(1) Variation in annual balances.

The insufficiency in the generation of own resources was not compensated by a greater transfer of resources from the Treasury. This would have been an intra-public sector arrangement capable of compensating state-owned companies for their mandatory contribution to the objectives of macroeconomic policies, the solidarity of private interests and the socialization of the burden of the crisis through the nationalization of the debt. Regardless of other

15 Of course, state-owned companies contributed to the trade balance through import-substituting projects. However, from the micro point of view, which is what interests us, the foreign currency savings are accounted for by the user and not by the supplier of the substitute good.

considerations, allocation for example, the financial disruption of state-owned companies could have been avoided by a greater contribution of resources from the Treasury, which should have the responsibility for supporting the benefits and favors granted through state-owned companies.

However, this financing alternative did not occur. On the contrary, the Brazilian State, faced with the progressive narrowing of its fiscal-financial range of action, deepened the policy of fiscal cuts by reducing the resources transferred to the state-owned companies. In the 1983/85 triennium, the real resources transferred by the Treasury to state-owned companies suffered an average reduction of 46% in relation to the amounts transferred in 1980 (Table 4).

Submitted to such restrictions, state-owned companies were obliged, in order to generate balances in local currency, to reduce non-financial expenses and to increase fundraising from third parties. On the expense side, two items stand out. In the first place, the behavior of the mass of salaries and social security contributions should be highlighted, which presented a real drop of around 30% in relation to the values observed in 1980. Second, the financial bottleneck implied the deterioration of the investment capacity of state-owned companies. In the 1983/85 triennium, investments suffered expressive cuts, standing, on average, 40% below the levels verified in 1980. This means that the remittance of real resources abroad had as one of its main counterparts the relative paralysis of investments in infrastructure and basic inputs, par excellence an area of activity for state-owned companies.

As for third-party resources, state-owned companies, prevented from disputing domestic credit, became captive customers of relending operations offered by international creditors. But given the global credit limits imposed in the adjustment program, such operations were insufficient. To avoid generalized defaults, part of the responsibilities ended up being transferred to the monetary authorities (bridge loans granted by Banco do Brasil) while the state-owned companies increased their short-term indebtedness in their accounts. In the 1983/85 triennium, the short-term credits of state-owned companies reached on average around 28% of total credits against around 4.0% in the 1980/82[16] triennium.

VI

The analysis developed so far has sought to show, on the one hand, how the process of nationalization of the external debt represented a powerful mechanism for the valorization/preservation of different fractions of private capital and, on the other, how the transfer of real resources abroad had a

16 The role of GB-588 and MF-30 in the financial administration of state-owned companies is discussed in Biasoto Jr. (1988).

devastating effect on the finances of government and state-owned companies in the first half of the 1980s. It was highlighted, throughout the exposition, that the internal face of the transfer problem was determined by the following dichotomy: external debt onus of eminently public responsibility (debt nationalization) and export balances generated essentially by the private sector.

It is now necessary to explore, from another angle, the second term of the dichotomy mentioned above. It is true that the examination of the ownership of capital of Brazilian exporting companies shows an almost absolute predominance of private, national, and foreign capital companies. However, and here is the point to emphasize, the export activity led by private capital has behind it a whole range of subsidies and incentives that mean, ultimately, a massive transfer of public resources to the capitals that operate in the sector.

It is well known that the military governments took different actions to foster and diversify the country's exports, notably in the first half of the 1980s, when the search for expressive trade surpluses overcame all other economic policy objectives[17]. It is also known that trade balances emerged, and grew, with the effective contribution of the export of industrialized goods, whose share in the foreign sales grew from around 57% in 1980 to around 66% in 1985 (Table 5).

Table 5 – Brazilian Exports (FOB) 1980/85

(US$ million)

Itens	1980	1981	1982	1983	1984	1985
Total	20132	23293	20175	21899	27005	25639
Primary Products	8470	8920	8238	8535	8755	8538
Coffee	2486	1517	1858	2096	2564	2369
Iron Ore	1564	1748	1847	1465	1605	1658
Soy bran	1449	2136	1611	1793	1460	1174
Sugar	624	579	259	333	326	167
Other	2347	2940	2655	2848	2800	3169
Manufactured goods	11376	14000	11686	13057	17955	16821
Transport Material	1512	2076	1718	991	1354	1694
Boilers and Mech. Eq.	1382	1546	1191	828	1396	1590
Steel products	625	801	795	1151	1548	1357
Orange juice	339	659	575	608	1415	749
Other	7518	8918	7407	9479	12242	11431

Source: FGV/Conjuntura Econômica/jan.1990.

It should not be forgotten, however, that exports of manufactured goods had a wide range of incentives, including drawback operations, premium credit,

17 On the way in which the goals of the external sector determined the shape of economic policy in the period, see Bacha (1983).

income tax reduction, tax exemptions, pre and post boarding financial incentives and the Befiex program. Such incentives, if fully used, would reach an amount equivalent to about 60% of the FOB value of manufactured exports in the period 1980-85[18]. On the other hand, approximate estimates indicate that the incentive policies would have caused an annual transfer of public resources to the export sector of the order of 3% of GDP in the period (Bomtempo, n.d.).

Transfers of public funds to private capital in the export sector were not limited to incentives and subsidies provided directly by the central government. Other mechanisms were activated, among which the price and tariff policy of state-owned companies should be highlighted. As seen, these prices and tariffs suffered a strong real reduction in the first half of the 1980s, as part of the adjustment policies implemented at that time. In addition to operating as an anti-inflationary instrument, this reduction aimed to indirectly subsidize exports by changing the relative prices of some crucial inputs for the export activity. Conspicuous examples are given by cheap flat steel favoring auto industry exports, subsidized electricity benefiting aluminum exports, cheap naphtha stimulating exports of chemical products, etc[19].

However, it is possible to go further in examining the relationship between the public sector and private capital in the export sector. It has already been seen that the acquisition of foreign currency takes place in a context of total fiscal and financial constraints on public entities – a fall in the tax burden, a real reduction in prices and tariffs, disappearance of government savings, cutbacks in investments, etc. – implying an increase in the domestic debt at rising real interest[20]. Now, who were the beneficiaries of the expansion of the public domestic securities debt? It was exactly those segments and fractions of capital that managed, in the context of the crisis, to maintain or increase their profitability, as the case of export manufactures. Instead of allocating their earnings to a substantial expansion of their productive capacity, these segments started to increase their resources through highly profitable financial investments, becoming creditors of an increasingly indebted public sector. Through the domestic debt, a new public funds transfer channel for the accumulation of private capital in the export sector was established.

In conclusion, the dichotomy – public foreign debt services versus private trade balances – is misleading, as it hides the massive public funds transferred to private capital for the production of the export balance. In fact, the public sector subsidizes the production of foreign currency and reappears, in a second moment, as the buyer par excellence of the foreign currency produced.

18 For an assessment of the role of subsidies in Brazilian exports, see Baumann (1989).

19 On the relationship between the real fall in public prices and manufactured exports, see Simonsem (1989).

20 The replacement of external debt by domestic debt, within the framework of a contractionary monetary policy, is analyzed in Cavalcanti (1988).

Interestingly, to say the least, the acquisition of foreign currency is done at the market price – permanently updated/valued by the exchange rate policy required by the "adjustment" – completely ignoring the subsidies previously granted. As if this were not enough, the public sector still ensures the financial appreciation of profits appropriated by the export sector through the continued expansion of its domestic securities debt. Here again, we have a clear demonstration of the asymmetry that governs the relations between the public and private sectors in the external adjustment of the 1980s.

VII

The fiscal-financial crisis in the public sector remains at the center of the debate on the direction of capitalism in Brazil at the end of the century. Evidently, the discussion of the theme is impregnated with a strong ideological content, fueled by the winds of Reaganomics, Thatcherism and the recent transformations of the so-called socialist countries. As a result, the focus of the analyzes is often directed at the opposition between the public and private sectors, based on a supposed antagonism where the voluntarist and populist actions of the former would result in atrophy of the latter and, therefore, in damages for the whole society. Such an approach exalts the allocative/distributive virtues of markets and advocates the minimal State of the liberal ideals of centuries ago.

However, an examination of the Brazilian case shows that the relevant issues are of a different nature. It is not a question, as seen, of opposing the public to the private, but rather of apprehending the forms of public-private articulation. And the cycle of external indebtedness/nationalization of debt/transfer of real resources abroad is emblematic.

It shows, in an absolutely clear way, how the different segments of private capital appropriated public funds, whether in their defensive actions in the crisis, or in their active actions, redefining the spaces of capital accumulation in a context of rupture and external rearrangement.

In this sense, the fiscal and financial disruption of the State is an integral part of the profound changes that Brazilian capitalism has undergone since the crisis of the late 1970s. In fact, such transformations, based on the permanent search for a surplus commercial position and massive transfers of real resources abroad, impose an almost absolute restriction on the continuity of state action in the historical molds of the postwar period, while reducing dramatically the possibilities of exercising, in the near future, active economic and social policies aimed at promoting a growth model that contemplates a new form of international insertion and a new wealth distribution pattern.

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CHAPTER 12

THE DEBT CRISIS AND ITS REPERCUSSIONS ON THE BRAZILIAN ECONOMY

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1. The creation of the Financing Pattern of the Brazilian economy

The rupture of Brazil's financial articulation with the outside world, caused by the "foreign debt crisis," is at the center of the most serious economic crisis that the Brazilian economy had ever gone through and that would extend throughout the 1980s. Brazil's close financial relationship with the outside world developed during a boom in international financial markets in the 1970s that changed the face of foreign financing in several "developing" countries. Before that change, foreign financing was restricted to some international or foreign trade financing agencies of the most advanced countries, in addition to direct investment. In the 70s, private banks began to predominate, which introduced floating interest rates to protect them, a kind of indexation of their international operations. This guaranteed banks their own refinancing, constituting the basis for the granting of voluminous, agile, cheap credits and with highly favorable term conditions, around which a complex of macro and microeconomic relations was established in Brazil and other countries.

At the macro level, the resources from the new source started to finance the balance of current transactions with enormous automaticity and independence in relation to agreements and adjustments required by multilateral financial institutions. When the external accounts did not require financing, Brazil still tended to continue taking foreign resources. The need for financing was transferred to the microeconomic plans of internal agents for spending in national currency.

In this sphere, foreign financing filled a virtually insoluble gap, given the organization of the domestic financial system.

Monetary, financial, and fiscal reforms, carried out between 1965 and 1966, were intended to establish a new and modern financing pattern for the Brazilian economy, which would meet both the requirements of the private and public sectors. The tax reform raised and rationalized the tax burden, not only by creating new indirect taxes on value added to replace the old taxes that levied on the total amount of operations, but mainly by expanding the taxable base and imposing greater progressivity of the income tax. In addition, the government's indebtedness capacity was recovered, through the launch of Adjustable Treasury Bonds, subject to inflation indexing, a measure considered essential for the financing of any government deficits, in a context of falling, but still high, inflation. Public utility tariffs were released to eliminate a focus of pressure on the Treasury, represented by the current deficits of public companies.

In the area of currency and credit, the economic policy of the military regime put important measures of innovation and control into practice. To guarantee good monetary administration, the Central Bank and the National Monetary Council were created. The Monetary Council was conceived as an inter-ministerial regulatory body, under the presidency of the Minister of Finance, in charge of defining the direction of the country's financial policy.

The main concern of the reforms was to ensure adequate financing of the public sector, to avoid the use of inflationary expedients to cover eventual deficits and, simultaneously, to stimulate private savings, whose insufficient volume was identified as the crucial problem of economic growth. The formation and mobilization of these savings would require a reorganization of the financial intermediation system, until then practically restricted to the operation of commercial and public development banks. Finally, the financial reorganization should contemplate mechanisms for attracting foreign investments and ways of attracting foreign loans that would complement the internal "savings."

The reorganization of the financial system followed the principle of specialization, both regarding the instruments for mobilizing resources, and institutions dedicated to supplying the various types of credit. The function of supporting the consumption of durable goods would be up to the financial societies; the financing of the working capital of the companies would be up to the commercial banks; and operating in the long-term credit bracket would be for investment banks. The formation of investment funds fueled with income tax deductions was imagined to boosting the stock market. An official real estate credit institution was created, the National Housing Bank, which, supported by resources from the Employment Compensation Fund (a kind of unemployment insurance), was intended to stimulate the civil construction sector, ultimately guaranteeing the private real estate credit agencies. Simultaneously with the restructuring of the economy's financing apparatus, measures were adopted that sought to encourage foreign investment and make borrowing attractive in the international credit market, which was already booming. To this end, Law No. 4,131 of 1962 was regulated, which allowed the indebtedness of companies abroad, with the prior consent of the Central Bank, and Resolution No. 63 was enacted, which allowed domestic financial institutions to raise and transfer foreign funds.

The great innovation introduced by the reforms to make the domestic financial system more dynamic was inflation indexing (theoretically based on the variation of a price index) of the values of securities issued by the financial system (funding) and financing contracts (application). Under inflationary conditions, this would be a way to regularize debt and credit contracts and enable the development of financial intermediation, including the public debt, virtually non-existent until that moment.

In fact, inflation indexing helped to regularize contracts, but not to the degree of generality and breadth desired. This is because if indexing actually allowed to neutralize a certain type of risk in forward contracts, it also introduced other types of risk that explain its limitation. What was avoided was the classic "creditor risk" in the face of currency devaluation. The risks introduced were:

1. for the creditor (banks or investors in bonds issued by the capital market or banks), the risk that the indexes fixed by the government for correction do not follow the inflation index. This risk occurred several times in the 70s and 80s. The agents' reaction to it was not to refuse term contracts, but to only accept relatively short-term contracts;
2. for the debtor, the risk that their particular price/income did not follow the arbitrated index. This risk is as high as the inflation rate, when the possibility of price and income dispersion increases. Here too, indexed contracts did not cease to be implemented due to this type of risk, both because for some lines of financing (such as for households to acquire their own homes or for companies to take long-term resources from the official development promotion agency – BNDES) there was no alternative. For the most fragile and risk-vulnerable sectors, however, certain particular protections had to be introduced along with indexation, proliferating systems that meant in practice non-full indexation, or, in other words, some type of credit subsidy.

The relevance of both sides (creditor and debtor) had as consequences, firstly, the non-deployment of long-term operations within the private financial sector. The only agents willing to take on the creditor's new risk were the public financing agencies. Secondly, the debtor's new risk had to be taken on by the public sector as well. This absorbed the most fragile private segments (such as agriculture and small and medium-sized companies) granting them subsidized credit. In addition, it organized indexing systems for long-term BNDES loans and real estate financing with formulas for discounting the inflation indexing, to minimize risk, bearing the subsidy costs.

In short, the reforms were only successful in their general purpose of regularizing fixed-term contracts in the economy through inflation indexing, because the public sector supported the excluded segments of the private financial system with its own credit, and because, as the sole domestic supplier of long-term investment funds, adopted special indexing conditions, reducing the risk for the debtor.

Even so, financing for investment, especially for long-term maturation, such as in infrastructure, was internally scarce (restricted to BNDES). The gap was covered by foreign financing.

For state-owned companies, the external source was a particularly favorable alternative because the terms and interest rates that were in force were compatible with the large projects they were carrying out. The state-owned companies found at the external source investment financing that they could not obtain through their own generation of funds, given the declining levels of public tariffs that the economic policy elicited to combat the inflationary pressures that had been present since the second half of the 70s. This could compromise its debt capacity, but the external source seemed, at that moment, plentiful and cheap.

On-lending operations in foreign currency through the domestic financial system were a secondary form of expansion of the Brazilian foreign indebtedness. There is no doubt that direct loans by foreign companies until 1978, and public companies' debt, especially after 1976, were the main vehicles of the Brazilian foreign indebtedness process.

Within the domestic private sector, Brazilian banks also made extensive use of foreign financing. They raised funds abroad in the long term to be transferred to domestic borrowers in the medium term. In this way, Brazilian companies were able to count on an additional source of investment financing, in addition to a medium-term source of financing for working capital, both existing only in the domestic financial system public segment. The private system did not significantly develop, as we have seen, neither in investment lines nor in medium-term working capital, even after the inflation indexing of term contracts introduced with the 1960s reform.

This intense use of foreign credit, by the public and private sectors, mainly through currency loans (they grew at the very high rate of 50% per year between 1968-73), revealed that the insufficient development of the domestic financial system, in terms of volume, terms and conditions of medium and long-term credit, was both a condition and an intentional result of the linking of domestic financing to the internationalized financial system, in a phase of rapid expansion. This meant the internationalization of a significant portion of the volume of credit used by private companies and later by the public sector itself.

An exchange rate rule (which we could also consider as an index, in this case, of foreign exchange) regularized and served as an incentive to contract foreign currency debt. For most of the 1970s, exchange rate devaluations, determined periodically by the Central Bank, were indexed to internal inflation minus foreign inflation. As the latter reached double digits in the decade, the mini-devaluation rule resulted in an expressive benefit for borrowers in foreign currency. The cost of these was then determined by the international interest rate (LIBOR or *prime* plus *spreads*), which was at relatively low levels, plus the devaluation of the cruzeiro, which was substantially below domestic inflation. As a result, the cost of resources in foreign currency was reduced vis-à-vis loans with inflation indexing internally.

This multiple insertion of foreign financing into the Brazilian economy was decisive to maintain high investment rates and the economy's growth rate in the 1970s. Foreign debt quickly financed any imbalances in the current account balance; it constituted a fundamental source of financing for internal public and private agents for investments and working capital; it took part in a general indexation system that made contracts feasible in an inflationary economy, by applying a rule according to which the periodic devaluation of the exchange rate (the "mini-devaluations") provided an incentive to obtain foreign loans.

2. Attempt to adjust the balance of payments and restructure the domestic financing pattern: the origins of the public finance crisis

The reaction of Brazilian economic policy to the first oil shock was quite unique. The authorities sought to reconcile a balance of payments adjustment with the maintenance of high GDP growth rates, based on import substitution projects in capital goods and basic inputs. We will not analyze the correctness of such an option. We only intend to try to explain the effects of the chosen strategy on the financing mechanisms of the Brazilian economy and, particularly, on the evolution of fiscal, exchange and monetary accounts.

The Geisel government (1974-79), by redefining the priorities of the economy and industrial growth, shifts the dynamic axis of expansion. Private consumption and investment give way to public sector investment, notably by state-owned companies. Public sector investments will even fulfill the role of articulating the new wave of private investments. This movement should had been associated with a change in the way the Brazilian economy is financed, if it were the intention of the economic authorities to avoid greater "exposure" to foreign indebtedness. In fact, the compatibility of the two objectives - adjustment of the balance of payments and maintenance of growth – was achieved fundamentally by accelerating foreign indebtedness and specifically by a faster expansion of public indebtedness in foreign currency.

It is very important, however, to underline the changes that have taken place in the role of foreign financing since the mid-1970s. The public sector becomes the largest final borrower of loans contracted under Law No. 4,131, which, in the period under review, is the main form of foreign indebtedness. This movement of expansion of the public sector's foreign currency debt not only fulfills the function of meeting its own financing requirements, but also of supplying the private sector with the foreign currency needed to service the past debt and for the growth of imports. That is, the private sector's difficulty in balancing the financial flows of its operations abroad leads the government to increasingly use public foreign indebtedness to settle the balance of payments, without sudden reductions in the import capacity.

The adjustment process of the Brazilian economy was made possible by the abundant liquidity of the international credit markets. The exchange rate, credit, interest rate and public price policies tried to create the conditions so that the public and private domestic agents were induced to prefer foreign financing sources. Discounting the fluctuations, the more general direction of the economic policy of the period was characterized by an increase in the real domestic interest rate, restrictions on the expansion of domestic credit, growth in the public debt, and lags in exchange rate devaluation.

In the case of state-owned companies, the government delayed the readjustment of tariffs and prices, except for oil derivatives – with the dual objective of fighting inflation and forcing the raising of foreign debt. In an environment of strong investment acceleration, these measures caused a profound change in the financing pattern, reducing the contribution of internal sources to companies.

The general conditions of credit, interest and exchange rates, favorable to raising funds in foreign currency, were not, however, compatible with the rebalancing of the trade balance and with the financing of private investment provided for in the current development plan (the 2nd NDP). Thus, special policies were created for agriculture, exports and import substitution.

In the agricultural sector, export crops were encouraged, especially soy, to the detriment of crops aimed at the domestic market. The instruments used were tax incentives for large projects, subsidized credits (funds and programs of the Central Bank, Banco do Brasil and requirements of other commercial banks), minimum prices and direct subsidies (wheat). In agribusiness, a gigantic financial scheme is set up – through the Central Bank – to make possible the program for the use of alcohol as fuel, Proálcool, within the scope of the policy of substitution of energy sources.

The priorities of the industrial sector were supported by credit and fiscal mechanisms. In the case of the import substitution program for capital goods and basic inputs, BNDES financed the new investments at negative real interest rates. The fiscal budget covered the credit subsidy implicit in these operations.

Exports of manufactured products received the benefit of tax benefits, with emphasis on tax credit premiums and other export incentive programs such as BEFIEX, while Banco do Brasil granted large resources at incentive rates.

The monetary budget, which was already used to record the floating costs of the public debt, now includes not only credit advances but also subsidies related to operations with the export and agricultural sector. The growing distortion of the objectives of the monetary budget will lead to the appearance of financial rescue operations for companies or industries, such as, for example, sugar mills, slaughterhouses, etc. The financial agent of the Treasury in these loans was Banco do Brasil, which, for this purpose, drew funds from the Central Bank through the so-called “movement account”. In reality, the movement account provided Banco do Brasil with automatic financing of any cash imbalances, regardless of its origin, and not just those arising from its role as the Treasury agent. This privilege gave Banco do Brasil the status of monetary authority, but the absence of funding restrictions created the need to establish quantitative limits to the expansion of lending operations, and prevented the bank from operating in non-monetary markets. Thus, with the development of new forms of financial intermediation and the demonetization of the economy, associated with the acceleration of inflation, the Banco do Brasil gradually reduced its credit market share.

In 1973, total subsidies (credit, direct and fiscal) represented 3% of GDP and 31.9% of tax revenue. In 1980, these ratios rose to 7.6% and 99.2%, respectively. The real growth of subsidies was astonishing: 139.4% in the 1973-76 period and 84% in the 1976-80 period. In this last period, there was a strong deceleration in tax revenue, reflecting the drop in the economy’s growth rate, the very effect of the government's tax waiver materialized in the expansion of incentives, and the rise in inflation rates.

Interest rate differentials, exchange differentials (oil account), management of development funds by monetary authorities, cash compensations from decentralized administration (financial relations within the public sector) and domestic public debt service are the most important factors, alongside the growth of foreign reserves, in the accelerated expansion of domestic indebtedness at this stage.

The discussion about budgetary unification is born in this environment of serious lack of control of public finances. As early as 1979, the finance minister saw the need to regulate the inflow of foreign resources and took steps to curb credit expansion. More important, however, is the stated intention to generate a fiscal surplus that could cover imbalances in the monetary budget.

It is curious to note that the economic policy of Minister Delfim Netto, between September 1979 and November 1980, although in a contradictory way, basically tried to face the problem of public finances. It announces a fiscal reform and increases in public sector tariffs and carries out a maxi-devaluation (breaking the rule of "mini-devaluations"), also with the purpose of eliminating fiscal subsidies for exports. The prefixing that it then adopted for exchange rate and inflation indexing were important at a time when inflation was approaching 100%.

3. The rupture of the voluntary credit market and the "fiscal crisis"

The second oil shock, the jump in international interest rates - provoked by the sudden change in American policy - increased the need for raising funds at a time when state-owned companies were over-indebted, and the private sector showed little intention to expand its foreign indebtedness. These facts occurred concomitantly with the maxi-devaluation of the Cruzeiro (around 30% against the dollar in December 1979) followed by the prefixing of the inflation indexing and exchange rate correction at 45% and 40%, respectively, when inflation was already advancing to 100% per year. This combination of events destabilized the expectations of economic agents, and this destabilization was immediately reflected in an aversion to foreign borrowing, proportional to the risk of a new maxi-devaluation. In that case, the safeguards granted by Resolutions no. 432 and 230 of the Central Bank underperformed. These resolutions allowed direct borrowers and bank borrowers of foreign funds to deposit the equivalent amount in Cruzeiros in an account within the Central Bank, which was responsible for the financial charges (international interest rate plus spreads and commissions) and for the exchange rate risk.

It is necessary to emphasize the "composition fallacy" implicit in the issue dealt with above. From a macroeconomic point of view, what was needed at that time of "external shock" was to further increase foreign indebtedness to finance the current imbalance in the balance of payments.

Let us see how domestic agents reacted in the face of this macroeconomic context, in face of the rupture of the aforementioned exchange rate rule. The reactions of private agents was decisive for understanding the fiscal crisis the State would go through, as well as the limits that came to be imposed on stabilization policies. Let us take the reactions of two fundamental agents: the big company and the banks. First, it is necessary to stress the significance of the break in the exchange rate indexing rule in 1979. It determined the breakdown of agents' confidence in the stability of foreign contracts, greatly aggravating the risk components implicit in exchange rate indexing. Two main consequences followed:

1. given the growing risk of an economy with a deep external imbalance, in addition to the now much greater risk of financing in foreign currency, companies halted new investments, which would bring a recessionary trend for the economy;
2. given that the risk of foreign financing presented not only for new loans, but for the entire stock of accumulated foreign currency debt (given the effect of adjustable interest rates and the possibility, now real, of maxi-devaluations), the private reaction did not stop at interrupting of new loans (with the stoppage in investments and the retraction in the level of activities). It also sought to cancel the stock of debt contracted in the past.

In short, while from a macroeconomic point of view the country was led to take out new loans to settle its external accounts, the decisions of private agents were heading in the opposite direction. The public sector - then considered the traditional public sector at the federal and state levels, plus public companies and banks - was then the agent that got into debt due to an economic policy decision (not an economic rationality) in the face of the contrary private reaction. The new loan flows and the old stock quickly passed into their hands, in a process known as "statization of the foreign debt."

It should be noted that while the authorities were forced to intensify the stimulus for raising foreign resources, frightened by the rapid loss of currency reserves, the conditions of international liquidity changed significantly, particularly for a large debtor like Brazil. Average spreads rose to more than 2% above LIBOR, and by the end of 1979 the country had already degraded its position in the international financial market, with the raising of a jumbo-loan of US$ 1.2 billion, directly by the US American Treasury.

The Brazilian government is forced to adopt heroic measures, the most heroic of which is the imposition of quantitative limits on the expansion of domestic credit, set at levels much lower than those of inflation. At the end of 1980, these measures were reinforced by a new increase in domestic interest rates and by the end of the prefixing of interest and exchange rate adjustments, which once again followed the inflation rate evolution (the General Price Index).

The result of this sudden reversal was a recession that lasted from 1981 until the beginning of 1984, accompanied by a rise in the inflationary level, a severe balance of payments constraint and very high real interest rates. These phenomena have led the more agile private sector - both large national and foreign companies - to a recompositing of passive structures, cuts in fixed investments, reduction in the level of activity, brutal reduction of raw material and finished product inventories, increases in prices above average inflation. All of this has allowed large companies to drastically reduce their past indebtedness and curb credit demand. In fact, the adjustment policy of the recessive triennium (1981-83), by directing the composition of business assets towards financial investments with greater liquidity and guaranteed real remuneration, transformed large companies into the financial system net creditors.

As for the banks, for the same reasons of increasing risk and instability, they also quickly contracted loans to the private sector and processed a profound change in asset structure, concentrating their assets in debts of public companies or public debt bonds[1].

After 1982, with the collapse of foreign financing flows, the government had to turn to the domestic credit market and to the expansion of the securities debt, given the imperative of meeting the growth of its financing needs. At this point, it is the debt service that has contributed sharply to the expansion of the government's financial requirements, since public investment, especially that of government companies, begins to suffer significant cuts between 1982 and 1983.

In view of this, the domestic banking system, including foreign banks - is even more encouraged to provide credit primarily to the public sector, once the prohibition on the taking of foreign debt by states, municipalities and autarchies was revoked in 1980, via Resolution No. 63. State-owned companies, in turn, were encouraged to resort to foreign loans, intermediated by the financial system. Despite the significant demand from the public sector

1 Between 1978 and 1985, bank assets with the public sector (loans to governments and state-owned companies, deposits at the Central Bank and in public securities) rose from 0.1% to 25% of total bank assets.

— almost exclusively motivated by the need to refinance the accumulated debt — a significant fraction of the foreign resources raised by the banks ends up being deposited with the Central Bank, in accordance with Resolution No. 230. In December 1984, about a third of the funds raised by private banks were under the custody of monetary authorities, who bear the financial and exchange rate charges on debts. The total balance of deposits in foreign currency, under the responsibility of the Central Bank (Resolutions no. 432 and 230) reached, in 1981, around US$ 12 billion. It is ironic (or natural?) that a system of foreign fundraising, driven by private incentives, has resulted in a brutal "nationalization" of debt. This nationalization concerns not only the concentration of the stock of debt in the public sector (which at this stage has already reached 80%), but also the "socialization" of private debt, through deposits in foreign currency within the Central Bank.

4. The debt crisis and the state's financial crisis

The Brazilian economy and, in particular, the public sector are facing the most serious financing crisis since the post-war period. This crisis has its immediate causes not only in the sudden interruption, in 1982, of the voluntary supply of foreign resources, but also in the adjustment policies adopted to remedy the deficit in the balance of payments, through the generation of huge trade surpluses.

The financing pattern of the economy and the public sector, heavily supported during the 1970s by foreign indebtedness, collapsed. This fact would be enough to result in a severe "fiscal crisis." This is not only because the main source of liquid resources for the State and its companies was interrupted, but also because - during the period of rapid indebtedness - the contribution of tax revenues and, above all, the self-financing capacity of public companies dwindled.

The connections between the foreign indebtedness process and the "fiscal crisis" began to be established even in the period of positive net financing flows. In the second half of the 70s, the effects of the overborrowing strategy on public finances and the expansion of domestic indebtedness are already transparent, in addition to perfectly predictable consequences of a sudden interruption in the supply of resources or of a change in interest conditions and terms under which the resources were offered.

In fact, changes in foreign financing conditions, caused by the interest rate shock in 1979, and, later, the disappearance of the voluntary loan market in 1982 forced the acceleration of the process of nationalization of the foreign debt and the adoption of adjustment policies that aggravated the financial problems of the public sector.

The real exchange rate devaluations, particularly that of 1983, caused an appreciation of the stock of the public sector foreign debt. Simultaneously, it reduced the capacity to pay it due to the economic and political impossibility of readjusting public tariffs and tax revenues in the magnitude and speed required by the adjustment. The expansion of the trade surplus was an important factor in the growth of the domestic public debt, as the government had to finance itself in cruzados with the private sector (which held positive balances in foreign currency) to settle its foreign debt commitments with the Central Bank. In its turn, the private sector was carrying out a huge adjustment, at least in the segment of large companies.

Thus, since the beginning of the 1980s, or even earlier, as in the late 1970s, given the first signs of the international crisis and the change in exchange rate indexation, large companies were able to generate the internal liquidity necessary to initially reduce their debt levels, including canceling past debts, and then accumulating large financial surpluses. From the point of view of their balance sheet, they move from the recessive adjustment years of a pattern that prevailed in the 1970s, in which they were positioned as net debtors of the domestic and foreign financial system, to another, which will characterize them in the 80s in which, at the limit, they become net creditors. They used the internal generation of funds not to fund fixed investments, but rather sought short-term financial investments with inflation or exchange rate hedge, especially in public bonds. The big private companies were also able to take advantage of two alternatives for microeconomic adjustment, compatible with the orientation of macroeconomic policy adjustment:

1. the orientation of production for exports, following the orientation of the “adjustment policy” and benefiting from incentives and subsidies granted by the government, in addition to a favorable exchange rate policy;
2. the adjustment of profit margins, which the economic policy passively allowed, based on its priority to promote changes in relative prices that redirected production to the foreign market rather than price stabilization. Soon, the reduction of the debt level and the formation of liquid positions in the financial market and with the public sector would no longer be the strategy only of large companies and banks, ending up involving all private agents that could generate the required liquidity, including higher-income households who also contracted their spending. From a microeconomic point of

> view, these were "rational" reactions necessary to adjust and protect each one from an unbalanced, inflationary, and unstable environment. But from a macroeconomic point of view, it reinforced the crisis and the financial disorganization of the public sector. This is transformed, as quickly as the private sector balance sheet adjustment takes place, in the net debtor agent of the economy, combining the two sides of indebtedness: the domestic indebtedness of state-owned companies with banks, in addition to Treasury bonds, and the foreign indebtedness.

The extreme liquidity of the private sector, on the one hand, and the high indebtedness of the public sector, on the other, are at the root of the difficulties faced by the anti-inflationary policies adopted after the "recessive adjustment."

The high indebtedness of the public sector soon became a drain of state resources. It was the consequence of the rise in international interest rates on the nationalized foreign debt, the exchange rate policy, and the increase in domestic interest rates that the adjustment policy provoked. The interest burden on the public sector is still a central problem in public finance. In 1988-89, for example, the interest burden on the public sector's domestic debt (except state-owned companies) corresponded to 1.5% of GDP and the external burden rose to 2%. Including about 2% of GDP as the interest paid by state companies on their domestic and foreign debt, the public sector financial expense then rises to 5.5% of GDP. This represents about 25% of tax revenue. Only a monetary reform, which canceled rights and temporarily blocked financial investments, was able to reduce these results in 1990. Interest charges in 1990 may have declined to around 4% of GDP.

Such interest burden has not been effectively paid by the public sector; it is continually "rolled over," increasing the indebtedness. What the disruption of foreign financing represented for the public sector was precisely the end of one of the sources of this indebtedness, which then had to move to the domestic plane in the absence of a reform in public financing that would grant it an alternative, as in a fiscal reform. The solution, evidently provisional, but which has been dragging on for more than a five-year period, is short-term indebtedness through the issuance of government bonds whose almost entire volume roll over overnight, and which in fact represent quasi-money.

It should be noted that the generation of mega surpluses in the trade balance after 1984 allowed the country to honor the interest rate commitments it had undertaken in negotiations with foreign creditors, but it did not alleviate the financial imbalance in the public sector. The trade surplus is fundamentally private; the financial burden is fundamentally public. The acquisition of private rights then requires financing (in national currency) from the public sector, which has found it in indebtedness with the characteristics described above. Under these conditions, the mega surpluses, associated with the cessation of refinancing of interest on the foreign debt by Brazil's creditors, are a source of domestic indebtedness in the public sector. The other side of this process is the incentive to private wealth rentism since the beginning of the economic adjustment in the early 1980s, concentrated on the short-term turnover of public debt, with high liquidity, and profitability standards only comparable to export sectors.

These can count on the most perfect indexation (the daily update of the official exchange rate), and the country's interest rate commitments give their business the highest degree of certainty among all other alternatives for domestic productive activity.

Rentiers and exporters enjoy, for the reasons above, an asymmetric and almost monopoly power in the economy, which is exercised against the State and the attempts of economic policies to restore stability. The rentiers, as financiers of the domestic public debt; exporters, as holders of the prerogative of generating a strong (foreign) currency, and who ultimately finance the foreign financial commitments of a State subjected to growing financial imbalances.

The progressive deterioration of the financial situation of the government and its companies led the debate on the state of public accounts to many impasses and attempts at a solution totally disconnected from the real nature of the problem. Reductionism in diagnoses and proposals prevailed both on the part of public opinion and on the side of economists and government officials. There is an idea that an effort to reduce State intervention in the economy is enough, cutting spending and transferring companies to the private sector. No one can deny that the nationalization process has advanced unchecked over the last twenty years and that the expansion of the monetary budget, in the second half of the 70s, corresponded exactly to the pattern of creating expenses and favored lines of credit without corresponding tax revenues and in absence of an adequate programming of credit offered by public financial agencies.

The illusion of a balanced fiscal budget, during this period, is the symmetric of the deception that recommends budget unification as a major instrument of rationality in the process of annual setting of government revenues and expenditures. It is true that unification is a democratic and transparent imperative in public accounts, in addition to allowing the identification of factors that mostly contribute to the growth of public sector financing needs. Identifying the nature of the problem does not necessarily imply the ability to solve it, and this is a very bitter realization for those who have or have ever had the task of administering economic policy or managing public finances.

However, adopting solutions unaware of the nature of the problem can certainly aggravate things and make them almost unmanageable after a certain point. Again, a fiscal shock therapy is mentioned, combining spending cuts with tax increases. Carried out within the current tax standards and norms, this promised tax escalation can aggravate the inequity in the distribution of the tax burden, which basically falls on salaried and self-employed work. The increase in taxes, without expanding the concept of taxable income and without the adoption of effective tax progressivity criteria, becomes increasingly difficult from a political point of view.

In any case, even if the reformulation of the fiscal and tax instruments arising from the 1966 reform and an upturn of the net tax burden are unavoidable, we must not imagine that measures of this nature can solve the question of financing. It is not possible to separate the problem of creating additional tax resources for the government from the general conditions for financing the economy. Now, these general conditions are profoundly influenced by the double determination of the foreign debt service, its exchange rate dimension (generation of foreign exchange) and its fiscal aspect (growth of the domestic debt, shortening of its terms and pressure on the interest rate). Criticisms of traditional adjustment schemes, such as those sponsored by the International Monetary Fund, are based on the perception that there is incompatibility between the goals and the recommended instruments to achieve balance in the current account and the purposes of achieving a public deficit level that is likely to be financed.

We are not going to repeat here all the arguments that raise objections to the possibility of a fiscal shock therapy in the proportion required to rebalance public sector finances. Some estimates even fix the increase in revenues (tariff and tax) from 6% to 8% of GDP. The distributive conflicts implicit in a shock of this magnitude need not be exaggerated. In addition, the effects of a fiscal and tax escalation on government revenues can be negative, as they lead to an acceleration of inflation and a consequent reduction in the real value of revenue. Fiscal shocks, in an economy with high and chronic inflation, therefore marked by the spread of formal and informal inflation indexing mechanisms, have the same fate as any attempt to change relative prices: the acceleration of the inflation rate. For this reason, particularly in the case of tariffs and prices of public companies, there is an alternation between moments of rapid readjustments and periods of slower readjustment considering the evolution of inflation rates.

In a world of debts contracted at real interest rates, the effects of an acceleration of inflation are unfavorable to the public sector, which is unable to properly index its revenue to inflation. The inflationary tax on the net balance of private agents decreases as the demand for money reduces. Econometric studies reveal a high elasticity of money demand in relation to inflation. This means that the government cannot freely determine the funding mix between currency and bonds. It also means a complete endogenization of monetary policy, in the sense that the government's discretion is reduced to a minimum, given the agility of the financial markets in anticipating the maneuvers of the authorities. This is facilitated by the shortening of the term structures of public sector liabilities, not only for the securities debt but also for the banking one.

This situation tended to frequently bring the government closer to the zone of critical decisions (confiscations or compulsory devaluations), which provoked in the financing agents the perception that the public debt is not the private sector's net wealth. This circumstance aggravated the debt turnover conditions and, therefore, the ability to obtain new resources through indebtedness.

Another scenario could be envisioned if a fiscal reform were accompanied by an in-depth review of the foreign debt terms. This would make it possible to attack the problem in all its facets: in the disarming the asymmetric positions of rentiers and exporters regarding profitability and risk, which would make an anti-inflationary policy viable; in the financial recovery of the public sector, which would open the way for the resumption of basic investments; in the greater abundance of foreign reserves that, in addition to the repercussions at the level of exporters, would contribute to a likely increase in imports (which naturally accompanies the first phases of a expansion cycle) not running into a very restricted import capacity. In short, in these ways, it would be possible to combine anti-inflationary policies and growth resumption policies. It should be noted that, at the end of 1990, the Brazilian economy will have accumulated growth close to zero in its per capita product, if we take the period since the beginning of the crisis (1981).

5. External restrictions and limits to domestic policies

The external restrictions determined by the debt crisis have made the execution of economic policies in developing countries extremely difficult. In Brazil, we will illustrate the issue at two crucial moments in the country's recent economic history: the 1986 Cruzado Plan and the 1990 Collor Plan. Both constitute the largest initiatives in terms of trying to break up the inflationary process and stop the acute instability that the country is going through. It is worth pointing out the mechanisms that most reflect external restrictions. First: the absence of foreign funding flows to the country. This represented the loss of the external source for public financing and the long-term financing of investment, in addition to the loss of the country's possibility of resorting to short-term credits to regularize any short-term imbalances in the balance of payments. This contributed to an increase in the public sector's domestic indebtedness, to depress the economy's investment rate (with consequences for the average growth in the 1980s) and, in the short term, to create extreme inflexibility in the country's external accounts. As a result of this last outcome, the management of the domestic interest rate loses effectiveness as an instrument to induce short-term capital flows. Second: the generation of mega trade surpluses has become imperative as a counterpart to the "debt crisis" and the agreements with foreign creditors. This resulted in the commitment that the country would honor the expected disbursements of interests on the foreign debt. Combined with the dearth of short-term capital inflows to regularize the balance of payments, this determined an also extreme exchange rate inflexibility for the country, in the sense that a reduction, albeit modest, of the trade surplus (which, in another situation, would be perfectly "normal" according to the conjunctural oscillations of international trade and financeable through short-term capital movements) has domestic repercussions in the form of a balance of payments crisis with potentially explosive effects on the exchange rate. The privileged situation of exporters and rentiers at the domestic level, to which reference has already been made, correspond to these factors.

The Cruzado Plan was an example of the limits of a stabilization policy undertaken under these restrictions. The plan decreed the freezing of prices and the de-indexation of the economy, including the exchange rate, but it was fulminated by the action of liquid agents, banks and exporters. The first (companies and households with surpluses) shifted resources from less attractive financial investments to the purchase of real goods or assets, such as real estate, shares, dollars in the parallel market. This led to an explosion in demand and aggravated the speculation in the asset market.

The Cruzado plan and the ensuing change in public debt practically paralyzed the main sources of the bank´s profits (because they were nourished by the inflationary arbitrage of money and the profitability that public bonds offered). The banks reacted by violently expanding credit. The credit of financial institutions increased in 1986 by 32.8% in real terms, whereas for commercial banks the increase was 69%. The new loans represented additional purchasing power, which was made available above all to the private sectors, in the order of 12% of GDP. This was the most prominent component among those that individually contributed to the growth in demand in 1986. The public deficit, for example, reached 3.7% of GDP.

The freezing of the exchange rate, and the domestic overdemand that even made it possible to charge premiums over the legally fixed prices (obviously impossible in exports), brought about a sudden stoppage of the relative advantage of the export activity. The reaction of exporters was the main cause of the fastest reversal of the trade balance that Brazil has ever experienced. Until the month of August 1986, the country was able to accumulate monthly trade balances in the order of US$ 1 billion. Two months later, in October, it had already registered a deficit (of US$ 83 million), which would be repeated in the following months until January 1987. As a result, the annual trade balance was reduced by US$ 4.2 billion in relation to 1985, from US$ 12.5 to US$ 8.3 billion. The balance of payments crisis made the stability of the currency's value unsustainable, due to the speculation that it induced in the parallel foreign exchange market and the expectation of an imminent unfreezing it generated.

The moratorium declared in February 1987 did not influence this situation. It related to the attempted new national posture or policy in relation to the foreign debt and interest payments. But by then, the success of the plan was already compromised. As soon as the prices were liberated (starting in November 1986), high rates of inflation returned, as did financial and exchange rate indexation.

The Collor Plan of March 1990 impacted the economy at a time when it was going through a phase of instability even more acute than at the time of the Cruzado Plan. The economy was on the verge of hyperinflation. The Plan consisted of several measures that changed the wage policy, promoted a strong fiscal adjustment, froze prices (for a month) and blocked financial liquidity through a monetary reform that made a portion of the balances of financial investments (including demand deposits) unavailable for a year and a half. The exchange rate was subjected to a "dirty" fluctuation regime. The moratorium in which the country has been in since mid-1989 and the sudden shortage and appreciation of the Cruzeiro determined by the monetary reform allowed, at first, the maintenance of relative stability of the exchange rate in the official and parallel markets, in addition to a significant recovery of the Brazilian trade balance. This reinforced the country's foreign reserve position at a time when negotiations were resumed with the IMF and foreign creditor banks. Also, it contributed to the Plan's relative success in bringing down a monthly inflation rate from 90% to levels as 10 to 12% registered until September 1990.

Then, a reversal in the trade balance as sudden as that which had occurred during the Cruzado Plan was precipitated. The decrease was from a monthly average of around US$ 1.2 billion obtained between April and July to US$ 215 million in October. The increase in oil prices on the international market, after the new Persian Gulf crisis that began in August, partially accounts for this result, but the decisive factor was the drop in exports (from values close to US$ 3 billion to US$2.3 billion in October). The postponement of exports was motivated, according to exporters, by a large exchange rate lag.

The recovery of previous levels of trade balance was faster that year than during the Cruzado Plan (in December 1990 and January 1991 the values had already returned to the average of US$ 1.2 billion), due to the prompt reaction of the exchange rate (during the Cruzado Plan, the exchange rate remained frozen). In just three months, the national currency devalued 102% (between September and November; 71.5% in October and November), enabling the resumption of exports, but at the price of contributing to the acceleration of inflation. The inflation rate quickly jumps to the 20% mark, ruining yet another stabilization plan. The impasses faced by Plano Collor were not limited to the exchange rate problem (the monetary reform was not successful in reducing liquidity as intended, a reduction in the agricultural harvest pressured food prices, fuel prices rose sharply, etc.), but, without a doubt, such a significant and rapid devaluation of the currency, as caused by exporters in the last quarter of 1990, makes the intention of internally stabilizing its value inviable.

CHAPTER 13

FOREIGN-EXCHANGE CONSTRAINT AND ECONOMIC GROWTH IN THE 1980´S[1]

Ricardo Carneiro

During the 1980s, the Brazilian economy presented significant contrasts with previous decades, especially with the 1970s. The sharp drop in the growth rate observed in this decade indicates the exhaustion of a development pattern whose mark was the exceptional dynamism during the years of modern industrialization after 1930 and, particularly, from the mid-1950s.

The confrontation between the 1970s and 1980s also indicates a clear difference in the shape of economic cycles. While in the 70s there was, after the intense growth of the "economic miracle" (1970/73), a long period of deceleration (between 1974 and 1980), still marked by high growth rates, the 80s were characterized by the alternation of brief cycles of recession and expansion, and by a growth rate close to the population increase (Graph 1).

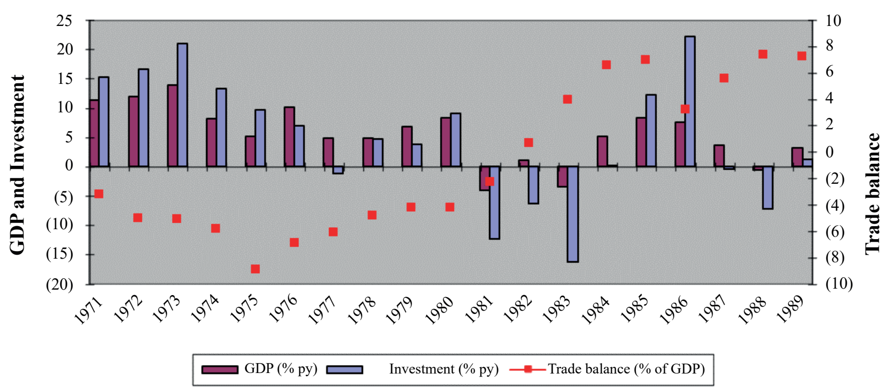
Even more important than the fall in GDP growth was the trajectory of investment. Its deceleration from the mid-1970s was replaced by an absolute reduction and intense fluctuations throughout the 1980s, indicating an environment of deep uncertainty and the absence of a sustained growth pattern. Another striking aspect of the 1980s is related to foreign relations. While in the 1970s there was a systematic absorption of real resources from abroad, by permanent trade deficits, the 1980s, on the contrary, were characterized by the continuous transfer of real resources abroad through the attainment of recurrent foreign trade surpluses.

The drastic reduction in growth, the stagnation of per capita product, the regression of investment, and the transfer of real resources abroad are, therefore, the highlights in a characterization of the 1980s. These characteristics, in turn, cannot be taken as independent of each other. There is a hierarchy among them or, more precisely, a greater relevance of the transfer of real resources as a defining factor in the trajectory of other economic

1 This chapter corresponds to chapter 4 of the book: Carneiro, R. (2002). Desenvolvimento em crise: a economia brasileira no último quarto do século XX. Unesp.

variables. From our point of view, the commitment to transfer real resources abroad to pay the external debt created a constraint on the development of the national economy.

Graph 1 – Compared Performance (1970 vs 1980s)



Source: FIBGE. *Contas Nacionais.*

Interpretations about the lost decade

A decade marked by such unfavorable economic performance has given rise to divergent interpretations about the factors that would explain this trajectory. From the set of these views, we can extract three distinct interpretations. The first one diagnosed that the root of the small dynamism was the incompatibility between domestic growth and the transfer of real resources abroad. In an intermediate position, we have the thesis of the possibility of resuming growth conditioned to its reorientation, to make it compatible with the external restriction. Finally, the other extreme consists of the perspective that emphasized the absence of external obstacles to growth.

The first strand of interpretations includes the works of economists who are critical of the external adjustment of the Brazilian economy. A summary of their positions can be found in Brasil - Ministério da Fazenda (1987a), which concludes that the attempts to resume economic growth and improve income distribution, carried out in the mid-1980s, ran into foreign-exchange restrictions, that is, into the imperative to generate high trade surpluses to pay the external debt.

According to the document, the compatibility between growth and transfer of resources abroad would only be viable in the recovery stage of the cycle, in which growth would occur based on the occupation of idle productive capacity. Once the existing capacity is fully utilized, growth would depend on an increase in the investment rate, requiring a rapid expansion of imports and a reduction in trade surplus.

Looking at the issue from a long-term perspective, Cardoso de Mello (1984) points out the temporal inconsistency between the growth of exports – the main factor for generating and sustaining surpluses –, and the transfer of resources abroad. This is because the good performance of the former would depend on the technological renovation of the national productive activities, in an international context of acceleration of technical progress. Such performance could only be achieved by preserving the investment rate at high levels, with the necessary and corresponding increase in imports.

Still on the critical side, from a macroeconomic perspective, Moura da Silva (1984) warns that the adjustment policy imposed by foreign creditors and the IMF on Brazil would have created obstacles to the country's sustained growth. The period of recessionary adjustment created conditions for short-term growth but compromised long-term growth. This is because the rate of capital accumulation would have to be below the rate of internal savings to make the transfer of real resources abroad feasible.

Summing up, the general direction of the adjustment was to reduce the excess of expenditure – or the deficit in current transactions –, adapting it to the new financing availability, which was much smaller. There were two basic requirements for making such an adjustment viable: reducing the public deficit – increasing domestic savings, in particular that of the public sector, the main debtor – and, at the same time, changing the relative price structure to increase the exported coefficient and decrease the imported coefficient, enabling the generation of foreign exchange. In the next chapter we will discuss the budget question and for now, the transfer one.

Between 1979 and 1984, the change in relative prices was centered on exchange rate policy. There was also an aggressive policy to recover administered prices and strategic inputs – basically produced by state-owned companies – and to gradually reduce subsidies and fiscal incentives for exports. The main goal of this policy was to use the active exchange rate policy as an instrument of export competitiveness, replacing the implicit and explicit tax breaks policy that had characterized the second half of the 1970s.

A different opinion regarding the possibility of a successful external adjustment of the economy was defended by the then minister Delfim Netto (1984). For him, since mid-1979, important structural changes have taken place in the Brazilian economy. The main axis of change, according to his analysis, was the transformation of the energy matrix, which was mainly responsible for the external imbalance. The other changes were subordinated to this strategic axis, highlighting the containment of the public deficit and the redirection of the productive sector to the international market, aiming to make exports the new source of growth dynamism.

The external imbalance was addressed mainly through an active exchange rate policy, comprising the maxi-devaluations of 1979 and 1983 and the mini-devaluations without discounting foreign inflation, that is, the full indexation of the exchange rate. The policy aimed to increase the exported coefficient and reduce the imported coefficient, producing a substantial trade surplus. This would be achieved fundamentally by changing relative prices, that is, by raising the prices, in domestic currency, of tradable goods, reducing their internal absorption, and by converting non-tradables into tradables, through lowering their prices in foreign currency and, finally, by increasing the price of imported goods. It should be noted that this would not only be a short-term policy but aimed at connecting as many productive sectors as possible to the international market, making exports a key variable in the new economic growth model.

At no time does this interpretation refer to the transfer of real resources abroad as an absolute limiting factor for the country's growth. According to his interpretation, a structural adjustment of the economy that would not collide with the foreign restriction had taken place. The recessive adjustment would have been necessary to reorient the economy, whose growth in a second stage would depend on the performance of exports or the export-led growth. The multiplier effects of the latter, in turn, would dynamize the internal market.

According to the then minister, there would be no incompatibility between the preservation of the trade balance and the growth of domestic demand, especially investment. The presumption of this view was that the country would be able to finance deficits in current transactions, as long as they were reduced, and grow based on the export drive, even with the transfer of real resources to the foreign market. In more precise terms, it was necessary to fulfill two conditions: greater growth in exports compared to imports to guarantee the trade balance surplus; and an export growth rate higher than the interest rate on the foreign debt. Thus, a declining deficit in current transactions and the payment of an increasing share of it was guaranteed. Under these conditions, in the foreseeable future, it would be feasible to return to the international credit market and obtain financing for the uncovered portion of this deficit.

In radical contrast to the previous theses, the work developed by Castro & Souza (1985) stands out, denying the relevance of the recessive and relative prices adjustment in the transformation and reorientation of the Brazilian economy, as well as the limitation to growth arising from the transfer of real resources abroad. Their main argument is that the rapid overcoming of the foreign-exchange crisis in the early 1980s was not due to the adjustment policy – expenditure control and changes in relative prices – but to the structural changes resulting from the implementation of the Second PND (National Development Plan), in the mid-70s a good part of them producing results from the early 1980s onwards.

According to these authors, the transformations carried out during the Second PND had allowed the country not only to generate a structural trade surplus, but also to overcome underdevelopment. Therefore, the central idea of this thesis was that the import substitution process carried out during the Second PND had enabled the economy to operate at increasing levels of activity, without significant changes in the import capacity. Furthermore, the possibility of generating surpluses after the elimination of idle installed capacity was admitted, that is, in the cycle acceleration phase, when investment was growing above the product. One of the main characteristics of this conception about the implications of the adjustment carried out in the 1974/79 period is to deny the relevance of the foreign-exchange constraint on growth.

Growth, cycle, and generation of surpluses

Empirical evidence (Table 1) allows us to characterize the 1980s as a period of stagnation. After the exhaustion of a long expansion cycle, the economy was left adrift without finding a new pattern of development. The GDP growth, with a significant reduction compared to the historical trend, reflects more immediately the contour line of this stagnation. However, in negative investment growth, it takes on its deeper meaning. There are other important aspects, such as the reduction in the average propensity to consume and trade surpluses, the latter being systematically obtained, despite the persistent deterioration of the terms of trade with the world.

Table 1 – Growth Rate of Main Economic Variables (% p.y.)

			1981/89			
Periods	GDP	Consumption	Investment	Export	Import	Trade Balance
						% Of the GDP
1981/89	2.2%	1.8%	−1.4%	8.5%	−1.3%	4.8
1981/83	−2.1%	−2.2%	−11.7%	8.0%	−12.0%	2.6
1984/86	7.0%	6.4%	11.2%	5.3%	7.7%	4.9
1987/89	2.1%	1.3%	−2.2%	12.3%	1.5%	6.7
Variation Interval (% p.y.)	(−4.0) to 8.3	(−5.7) to 9.7	(−16.3) to 22.2	(−10.6) to 21.3	(−17.4) to 28.6	–

Source: FIBGE. Contas Nacionais.

The common feature of all economic variables during the decade is their great variability or, more precisely, their high degree of instability, whose greatest expression is the short duration of economic cycles, characterized by brief periods of expansion and retraction. From this point of view, the most illustrative example is that of investment, as it showed an intense retraction in 1981/83, an equivalent expansion in 1984/86, and a new retraction in 1987/89. On a smaller scale, this volatility is also observed for consumption and for the variables that specify trade balance.

Empirical evidence allows us to associate the instability with the incompatibility between generation of trade surpluses and growth. In this regard, the relationships between investment performance and the variables defining trade balance should be stressed. In the recessive period, when investment shrinks, there is a proportional reduction in imports and an acceleration in export growth. In the resumption of domestic growth, when investment starts to grow again, imports increase and the export growth rate decreases. The same behavior is observable, on an attenuated scale, in the relationship between consumption and the variables defining trade balance.

Therefore, macroeconomic data suggest an incompatibility between the preservation of the trade surplus and the increase in investment, whose origin comes from both the expansion of imports and the unsustainability of the ascending pace of exports in the face of sustained growth in domestic absorption.. On a smaller scale, this contradiction is also observed regarding the increase in consumption and leads us to conclude that there is a strong opposition between the generation of trade surpluses and the growth of domestic absorption, at least when the increase in the latter occurs at historical rates.

Instability and investment decline

The impossibility of reconciling the transfer of real resources abroad and sustained growth has its greatest expression in the inferior performance of investment. One of the essential reasons for this behavior is found in the dissociation between private and public investments, whose rupture is a clear indication of the disintegration of the previous development pattern. Central aspects of this rupture are the systematic decrease in investments in state-owned enterprises, the unsustainability of public administration investment, and the low level of private investments (Table 2).

Table 2 – Evolution of Investment by Agent (1)

	1981/89								
	Total	State-Owned Enterprises		Public Adm.		Private Sector		Others (2)	
	(% p.y.)	(% p.y.)	(% of total)	(% p.y.)	(% of total)	(% p.y.)	(% of total)	(% p.y.)	(% of total)
1981/89	−1.4%	−7.4%	17.8%	0.1%	12.5%	0.0%	66.9%	−5.6%	2.8%
1981/83	−11.7%	−10.8%	22.2%	−12.6%	10.8%	−11.5%	64.0%	−17.8%	3.0%
1984/86	10.5%	−1.0%	17.5%	29.4%	14.0%	10.2%	66.1%	13.0%	2.4%
1987/89	−1.6%	−10.1%	13.5%	−16.5%	13.4%	2.6%	70.6%	−9.6%	2.6%

Source: FIBGE and Sest.

(1) Data deflated by the Capital Account deflator.

(2) Includes planted forests, new permanent crops, and imported breeding animals.

Public administration investment, strictly speaking, concentrated in infrastructure works, shows a negligible growth in the 1980s. It is marked by strong cyclical fluctuations and by the inability to sustain high levels over longer periods compared to private investment. The adjustment pattern adopted throughout the decade, which always favored cutting investments as a fiscal adjustment mechanism, and, later, the financial crisis in the public sector, both resulting from the transfer of resources abroad, constitute the origin of this behavior.

The oscillations of investments in the state-owned enterprises are less intense, since the downward movement in the level is continuous, not recovering from the peak of investments that occurred in 1981. In one chapter of the previous book Carneiro (2002), we analyzed the dependence of state-owned companies on external financing to carry out their investment programs. The exhaustion of this source of funds and the obligation to pay at least the interest on the debt were the main reasons for the permanent decrease in investments in this sector.

Given this behavior of the set of public investments, which have a strategic character because they are located in the areas of infrastructure and basic inputs as energy, for example, one could not expect a different performance from private investment, marked by decline and strong cyclical oscillations, ultimately reflecting a lack of a sustainable growth horizon.[2]

Information on investment allocation also support the stagnation thesis. Its composition shows the decreasing weight of machinery and equipment. The participation of construction - residential and commercial - in capital formation increased, translating only a less mediocre performance, with a zero growth rate. Thus, the higher absolute decrease and the more intense cyclical variations in expenditures on machinery and equipment testify to the unsustainability of the growth pattern (Table 3).

2 The absence of decline in private investment in the 1987/89 triennium, in disagreement with the trajectory of public investment, is strongly conditioned by the year 1989, in which the growing explicitness of the hyperinflationary process motivates the shift from financial wealth to real assets, increasing activity in real estate and even the imports of capital goods without a national similar.

Table 3 – Variation and Composition of Gross Investment by Sector (1)

	1981/89						
Periods	Total Gross Investment	Construction		Machinery and Equipment		Others (2)	
	(% p.y.)	(% p.y.)	(% of total)	(% p.y.)	(% of total)	(% p.y.)	(% of total)
1981/89	−1.4%	0.2%	67.8	−4.0%	29.6	−5.6%	2.7
1981/83	−11.7%	−7.3%	67.7	−19.7%	29.3	−17.8%	3.0
1984/86	10.5%	8.0%	67.5	16.4%	30.2	13.0%	2.3
1987/89	−1.6%	0.4%	68.1	−5.4%	29.3	−9.6%	2.6

Source: FIBGE. Contas Nacionais Consolidadas.

(1) Data deflated by the Capital Account deflators.

(2) Includes planted forests, new permanent crops, and imported breeding animals.

An additional qualification on the nature of the investment during the decade reinforces the previous point. According to Suzigan (1988), the growth of the capital goods industry occurs fundamentally in the serial goods subsector, while the custom-made goods subsector shows low dynamism. This characterizes the so-called modernization investment, whose main feature is the introduction of new machines designed to increase productivity, without substantial changes in production capacity.

The information analyzed so far demonstrates the disarticulation of the pattern of development in force for decades in the Brazilian economy, in which public investment and that of the state-owned enterprises played the role of inducing private investment. Certainly, the little dynamism that still exists in investment is due to private investment in sectors linked to exports and to the production of some subsectors of consumer goods, as we will see below.

The most important issue regarding investment performance refers to the inability of the export orientation to constitute itself in the element of its dynamism. In other words, the additional markets arising from the new export insertion were insufficient to ensure the increase and sustainability of the investment rate. The quantitative aspect, that is, the small degree of openness of the Brazilian economy, surely plays its role here. However, the qualitative aspect is even more relevant, that is, the notion that in a continental economy the growth of the internal market continued to be the dynamic element *par excellence* in determining investment. Foreign markets were and continued to be complementary.

Looking at the same issue from a microeconomic point of view, that is, from the determinants of investment, one can say that, in a few sectors, in which Brazil has absolute comparative advantages, foreign markets constituted the main incentive for investment. In the vast majority of productive segments, it was the prospect of expansion of the domestic market that determined the decision to invest, with the possibility of accessing foreign markets playing a secondary role.

The consumption cycles

When examining the trajectory of consumption throughout the 1980s, one can see its contribution to the process of adjustment, enabling the transfer of real resources abroad. The aggregated data show their growth below that of the GDP, when considering the whole of the 1980s, indicating a reduction in the average propensity to consume. However, its great variability is also noticeable, that is, its intense acceleration and deceleration during the economic cycle, higher than the variability of GDP (Table 2).

Data on consumption in the metropolitan region of São Paulo (Table 4), due to their level of disaggregation, can better illustrate what happened in that decade. Growth for total consumption is null and slightly negative for most categories of goods, except for non-durable goods and auto parts. Furthermore, the intense variability of consumption associated with the economic cycle is also confirmed. As a rule, it is observed that the greater the durability of the good, the greater the variation in its consumption regarding the economic cycle. This is due to the degree of essentiality of the good, the characteristics of demand – replacement concentrated in time for durable goods –, and the substitutability regarding financial assets.

Table 4 – Metropolitan Region of São Paulo – Actual Retail Sales

	Variation (%)						
Years	Vehicles	Auto parts and Accessories	Construction Material	Durable Goods	Semi-durable Goods	Non-durable Goods	General Trade
1981	(36.1)	(29.8)	(18.5)	(21.5)	(3.9)	0.7	(15.6)
1982	(3.2)	4.7	(4.0)	7.0	9.9	15.5	6.9
1983	0.1	4.7	(6.0)	(13.1)	2.5	(8.9)	(5.2)
1984	(11.3)	23.9	(16.2)	(6.9)	(10.3)	9.7	(4.0)
1985	36.3	28.5	4.3	4.7	16.1	21.8	17.7
1986	11.2	31.0	25.7	26.7	9.0	15.7	16.8
1987	(33.4)	(14.2)	(32.5)	(28.1)	(23.1)	(18.7)	(24.5)
1988	29.9	1.8	(13.6)	(11.8)	8.4	(17.0)	(3.4)
1989	5.7	2.7	12.1	(5.1)	(7.4)	16.8	4.5
1980/89	(0.1)	5.9	(5.4)	(5.3)	0.1	4.0	(0.8)

Source: FCESP.

For the 1981/86 period, the data show a high correlation between the consumption of durable goods and the economic cycle, as well as the lower importance of the latter in the consumption of current and semi-durable goods. Comparing the recessive period (1981/83) with the recovery period (1984/86) confirms that the consumption of non-durable goods, unlike durable ones, is not so influenced by the reduction in the activity level. In the recovery, consumption of all categories is pro-cyclical, although with different intensities.

In summary, the acceleration of consumption growth after the recession period was mostly due to the growth of durable goods. It is worth noting the weight of the high degree of liquidity of the financial wealth of high-income families and the episodes of its conversion into consumption defines this behavior. This pattern was certainly conditioned by the anticipation of consumption during the price freeze phases of heterodox stabilization plans.

An example of the previous trend is the low correlation between the consumption of more durable goods and the economic cycle, from mid-1987. The continuity of its growth (despite the decline in income) is initially associated with the Bresser Plan's price freeze and, later, with the beginning of a hyperinflationary process, in which one of the main characteristics is the conversion of financial assets into real assets. For higher-income households, this means converting financial savings into high-value durable consumer goods. The expressive growth in sales of automobiles, in 1988, and of construction materials, in 1989, is quite illustrative of this phenomenon (Table 3).

The intense variations in consumption can be attributed to the adjustment process for the generation of trade surpluses. The latter, having as one of its central elements a restrictive monetary policy, accumulated in the hands of the high-income strata a considerable mass of financial wealth, with a high degree of liquidity. During the recovery, income growth, associated with the high availability of financial wealth on the part of families, induced a greater propensity to consume, whose translation is the conversion of financial savings into consumption of durable goods. Periods of price freezes and the acceleration of inflation at the end of the decade only magnified this movement.

Productive dynamics, foreign trade, and trade balance

Another prominent issue refers to the effects of the new orientation of the economy and the transfer of real resources on the trajectory of production, and trade balance. There are two distinct issues to investigate here: on the one hand, to what extent the export orientation resulting from the new configuration of relative prices was sufficient to ensure the dynamism of the economy. In turn, one must also examine the origin and sustainability of trade balances.

Productive dynamics and foreign insertion

The middling investment performance was negatively reflected in the behavior of productive activities since they presented a substantial decline in the growth rates of the main segments during the decade (Table 5). These data are also an additional indication of the insufficiency of inducements from the export sector to sustain the growth of the Brazilian economy. Moreover, some central features of the decade are surprising: the stagnation of production in the manufacturing industry contrasts with the preservation of growth in agriculture. Furthermore, there is a clear dissociation between the cyclical behavior of these two sectors, which is quite visible when their growth rates are compared.

Table 5 – Sectorial GDP – Growth Rates (% p.y.)

		1981/89							
		agricultural production			Industry				
Periods	GDP	Total	agriculture	livestock	Total	Extractive industry	manufacturing	Construction	Public Utility
1981/89	2.5%	3.1%	3.4%	2.4%	1.1%	7.2%	0.8%	0.1%	6.7%
1981/83	−1.6%	2.4%	1.4%	3.9%	−5.4%	6.4%	−5.7%	−7.8%	5.8%
1984/86	7.4%	1.5%	3.3%	−1.7%	9.0%	14.5%	8.5%	10.3%	10.2%
1987/89	2.0%	5.5%	5.4%	5.3%	0.2%	1.2%	0.1%	−1.2%	4.1%

Source: FIBGE. Contas Nacionais Consolidadas.

In the agricultural sector, crops register growth above that of livestock and maintain a tenuous link with the industrial cycle. Livestock, on the contrary, shows a countercyclical nature, resulting, according to Rezende (1989), from the nature of this activity. In the recessive period (1981/83), the fall in demand to depress prices and the rise in the interest rate to increase the cost of carrying the herd are combined, both promoting an increase in slaughtering. In the recovery period (1984/86) the opposite occurs: despite the growth in demand and prices, the reduction in interest increases the retention of stock and makes production fall. In the 1987/89 period, the stagnation of production, despite the increase in the interest rate, is explained by the preference for real assets triggered by the threat of hyperinflation.

As already noted, the crop sector shows significant autonomy regarding the industrial cycle. Its performance from the second half of the seventies is preserved throughout the 80s, a period in which its growth rate is about four times higher than that of the manufacturing industry. As Rezende (1989) shows, this performance does not find a main explanation in the dynamics of tradable products, as these, unlike the 1970s, grow at a rate lower than that of non-tradable products. In fact, according to Fonseca (1990), the export performance of agriculture in the 1980s is lower than in the 1970s, despite the growth in exported value being primarily due to increases in quantities.[3] In any case, the foreign market represented a source of stable growth for agricultural production, especially for certain segments.

The data in Table 6 support the above statements. Although all segments of the primary sector continue to generate significant surpluses, the dynamism of exports is only present in two of them, in livestock and in the processing of vegetable products. In both, the trade surplus increased significantly. In the other two sectors, including the one with the greatest importance in generating the balance – vegetable oils –, neither exports nor the balances changed significantly.[4]

Table 6 – Primary Sector Foreign Trade (Triennial Moving Average, in US$ million)

	1981/88														
	Livestock			Processing of vegetable products			Vegetable oils			Other food			Mineral extraction		
	(X)	(M)	(X/M)	(X)	(M)	(X/M)	(X)	(M)	(X/M)	(X)	(M)	(X/M)	(X)	(M)	(X/M)
1981	986.1	623.9	1.6	1,131.5	936.3	1.2	2,520.1	38.0	80.8	379.1	157.7	2.4	1981.4	216.7	9.7
1982	965.6	486.4	2.4	1,234.1	881.5	1.4	2,611.3	30.7	90.4	360.7	136.5	2.6	1,967.8	185.4	10.7
1983	983.5	361.9	3.3	1,530.9	830.7	1.9	2,388.8	55.3	54.7	301.7	112.3	2.8	1,907.3	187.2	10.3
1984	1,229.9	252.6	4.9	1,649.0	780.7	2.1	2,328.2	71.5	38.9	316.5	98.2	3.2	1,847.0	224.1	8.4
1985	1,178.5	384.5	3.9	1,684.2	674.7	2.5	2,019.7	88.0	23.0	328.5	133.8	2.8	1,872.3	273.1	7.1
1986	1,217.9	420.2	3.7	1,460.4	530.1	3.0	1,863.8	67.6	32.8	346.4	169.6	2.3	1,861.0	325.0	5.8
1987	1,149.8	435.6	3.1	1,622.3	372.0	5.3	2,022.3	57.4	41.5	366.7	193.4	1.9	1,976.4	384.2	5.2
1988	1,398.4	363.7	3.9	1,772.5	320.2	6.0	2,402.8	53.7	47.3	381.5	235.6	1.8	2,241.4	460.3	4.9

Source: Ipeadata apud MDIC.

Aside from the importance of foreign markets as a factor in the autonomy of agriculture from the domestic cycle, Rezende (1989) points out two other relevant aspects: the pro-cyclical nature of the prices of important inputs (land and labor); and the exogeneity of relevant production costs, determined by the oil price. This allowed agriculture, unlike the industrial sector, to adjust to the crisis via prices rather than quantities. Even with the drop in prices, the

3 The stability both in prices and in the volume of foreign trade, although with depressed prices and moderate growth, faced with the expansion of the quantities exported by the country, is an important indicator of the competitiveness of these exports.

4 Another aspect to highlight is the presence of cyclical factors in determining the balance, such as the recovery of domestic absorption, observable in most sectors, except for the processing of vegetable products.

cheapening of labor and land, due to the stagnation of the economy, and of inputs, due to the drop in oil prices, allowed expanding production without compressing profitability.

The other relevant factor was the stability of markets for non-tradable products, resulting from the replacement of the subsidized credit policy by the support price policy. The latter constituted an important instrument for sustaining and stabilizing agricultural income. According to Buainain (1988), under the influence of the aforementioned factors, agriculture not only maintained its growth trend of the previous decade, but also presented expressive gains in productivity in the most important crops.

In contrast to agriculture, the industry showed mediocre growth during the decade. Only the mineral extraction industry – due to oil production and mineral exports – maintained the same growth trend of the previous decade. Public utilities are also noteworthy, whose growth was determined by the occupation of the production capacity arising from the large public investments conducted until the beginning of the decade, especially in electricity. The most important segments, however, remained virtually stagnant (Table 4). In construction, this performance was associated with reduced government spending on infrastructure and the SFH (housing finance system) crisis. The transformation industry certainly did not find an element of dynamism in the export drive capable of replacing the domestic market, reaching 1989 with a production only 8.5% higher than in 1980.

According to Ipea/Iplan (1989), the greater insertion of the Brazilian industry in the international market throughout the 1980s was the result of a double determination: the real competitiveness of some productive segments, but also the strategy adopted by other segments to escape the high degree of idleness resulting from the oversizing of Second PND projects and the recession at the beginning of the decade. Therefore, this insertion was not always conducted on a competitive basis, being supported by incentives and subsidies, deterioration of the exchange rate/wage ratio, price and public tariff lags, and the possibility of under invoicing exports.

The expansion of the foreign insertion was carried out, moreover, in a very uneven way. The data on the annual exported coefficient, measured by the export/domestic sales ratio (Table 7), show a very differentiated opening according to industrial sectors. One can also see that the greater the total exported coefficient, the greater the dispersion in the exported coefficients of the productive branches. This means that the degree of integration with foreign markets is extremely unequal and that its impact on the various industrial sectors is significantly different.

Table 7 – Exported Coefficient at manufacturing (Triennial Moving Average)

	1981/88							
	1981	1982	1983	1984	1985	1986	1987	1988
General Industry	9.2	10.5	12.3	14.1	13.8	12.6	12.5	13.6
Sectors								
Non-metallic Minerals	2.7	2.4	2.7	3.3	4.0	4.1	4.9	5.5
Metallurgy	8.5	12.7	17.4	21.4	21.3	20.1	20.9	23.4
Mechanics	10.6	10.8	10.6	11.4	10.7	10.2	11.4	13.8
Electrical and Communication Material	5.6	5.6	6.2	6.7	6.3	5.4	5.1	5.4
Transport Material	19.1	21.0	21.5	23.2	22.1	22.2	22.2	22.8
Wood	18.9	21.5	25.1	27.3	23.7	19.6	20.4	23.1
Furnishing	2.0	1.9	2.7	3.5	4.5	4.1	4.0	3.6
Cellulose, Paper, and Cardboard	17.6	19.6	23.5	25.5	24.9	23.1	23.7	24.6
Rubber	5.1	5.5	8.3	11.6	12.5	10.9	11.2	13.5
Leathers and Skins	23.7	23.0	21.6	20.8	16.4	16.7	20.2	26.2
Chemistry	5.4	7.1	9.2	11.0	10.9	8.3	6.7	6.9
Pharmaceutical and Veterinary Products	2.8	2.4	1.9	2.4	2.9	3.1	4.4	6.0
Perfume, Soap, Detergent, Glycerin, Candles	1.8	1.4	0.6	0.4	0.5	0.4	0.4	0.4
Plastic Material	1.7	1.7	1.7	1.7	1.8	1.7	2.2	2.8
Textile Industry	9.9	10.6	12.4	13.4	12.2	10.6	10.7	12.0
Clothing, Footwear, and Fabric	14.1	15.2	17.8	21.1	21.4	20.5	18.9	19.2
Food Products	14.1	13.1	13.9	16.0	15.9	15.8	15.6	17.1
Beverages	0.8	0.8	1.1	1.3	1.1	0.8	0.7	0.8
Tobacco	10.6	14.3	17.5	16.6	16.7	11.8	9.8	4.8
Editorial and Graphics	1.3	1.1	0.8	0.6	0.5	0.5	0.4	0.4
Diverse	9.3	7.9	6.2	5.3	5.1	5.9	9.0	10.4

Source: Fundação Getúlio Vargas. Sondagem Conjuntural.

Of the sectors with a significant export coefficient during the period – above 10% – only an extremely limited portion achieved this mark throughout the decade. The first case includes metallurgy and, to a lesser extent, cellulose, paper, and cardboard goods, both producers of intermediate goods and significant representatives of the sectors in which high investments were made during the Second PND. Most of the other goods with a high degree of openness were already traditional exporters, such as textiles, shoes, food products, wood, and leather and skins. In these segments, the variation in the exported coefficient was less significant and resulted from a lower domestic growth and a better foreign price.

It is also worth noting the consolidation of foreign insertion in transport material goods, associated with the consolidation of a regional market in the Southern Cone and, finally, in mechanics, whose increase in exports was certainly due to the need to escape the high degree of idleness. Finally, one should note the high presence of industrial goods for which the foreign insertion, in addition to being of little significance, did not change significantly during the decade.

The information analyzed strongly suggests that the export orientation – understood as the search for additional markets as a drive of production –, although with some importance, was clearly insufficient to act as the dynamic element of the Brazilian economy during the decade, due to both its restricted nature in terms of sectors and its intensity. That said, it is worth examining whether there were also other stimulus factors resulting from the change in relative prices, referring to the stimulation of import substitution.

The joint effect of export orientation and import substitution can be seen by the analysis of trade rates (Table 8). It is evident that, for a group of productive sectors, the external insertion was a relevant factor in explaining growth. These segments are essentially represented by those industries that produce intermediate goods (Group 2) and, to a lesser extent, by the automotive and consumer goods segment (Groups 3 and 1). One should note that, for the industry of elaborate inputs or of capital goods (Group 4), foreign insertion changed little during the decade.

Table 8 – Foreign Insertion of the Industrial Sector

	1981				1988			
	Export	Import	(X-M)	(X/M)	Export	Import	(X-M)	(X/M)
Group 1								
Footwear	634.2	33.4	600.8	24.0	1,533.0	239.8	1,293.2	6.9
Textile	749.0	55.7	693.4	13.6	1,054.0	223.9	830.1	5.6
Group 2								
Cellulose, paper, and graphics	544.57	218.10	326.5	2.5	1,143.2	303.9	839.3	3.8
Non-ferrous metals	138.6	641.4	−502.8	0.2	1,374.4	417.7	956.8	3.4
Non-metallic minerals	140.8	130.5	10.3	1.1	247.5	109.8	137.6	2.3
Other metal products	274.2	232.4	41.8	1.2	394.5	148.5	246.0	2.6
Petroleum refining and petrochemicals	1,247.6	1,002.0	245.6	1.3	1,935.0	918.2	1,016.8	2.1
Steel	869.3	458.4	410.9	2.2	3,335.4	311.4	3,024.0	10.9
Group 3								
Motor vehicles	940.7	4.2	936.6	289.4	1,599.1	6.3	1,592.8	278.0
Parts and other vehicles	994.1	920.1	74.0	1.1	1,981.5	1,188.9	792.7	1.7
Group 4								
Chemical elements	224.8	932.2	−707.4	0.2	467.9	1,156.3	−688.4	0.4
Electronical equipment	469.8	590.3	−120.5	0.8	776.9	997.7	−220.8	0.8
Machines and tractors	939.0	1,706.4	−767.4	0.6	1,215.8	1,635.7	−419.9	0.7
Electrical material	345.5	769.2	−423.7	0.4	648.4	710.3	−61.9	0.9
Total	8,512.3	7,694.3	818.0		17,706.6	8,368.4	9,338.2	

Source: Ipeadata, apud MDIC.

There are important distinctions between the sectors benefiting from the export insertion. In the segments producing current consumer goods (Group 1), the increase in exports was accompanied by an also significant increase in imports, attenuating the impact of the former on the dynamization of these sectors. In the sectors of intermediate goods (Group 2), there was a growth in exports at the same time as a reduction or substitution of imports, increasing the effects of export insertion on the dynamics of the sector. The same pattern as in Group 1 is observed in the automotive segment, in which the main highlight is the export of buses and trucks.

From the above, it is evident that the change in relative prices was insufficient to promote a broad integration of Brazilian industry to foreign markets. Strictly speaking, the increase in this articulation occurred, above all, due to the expansion of exports in the segment of intermediate goods, whose implementation had been decided upon much earlier, still within the scope of the Second PND, throughout the second half of the 1970s. This clearly indicates the pre-eminence of domestic markets and growth mechanisms based on their dynamics in an economy such as the Brazilian one, characterized by continentality and by the high degree of diversification of the productive structure.

Observations regarding the 1980s confirm the pattern of export insertion observed in earlier times. Strictly speaking, since the mid-1950s, the expansion of the exported coefficient in the industry occurred as a by-product of the diversification of the productive structure. In other words, the diversification of exports stems from domestic development itself, keeping a secondary relationship with the cyclical aspects, that is, the exchange rate and the pace of growth.

Another highly relevant aspect concerns the evolution of the magnitude of the industrial sector's trade balance, whose growth over the decade was significant. Two aspects should be highlighted here: the expansion of the trade surplus in the manufacturing sector, although extraordinary, took place during a decade characterized by very low GDP growth rates compared to the historical average. The increase in the balance, in turn, resulted from the reduction or stability of trade rates (Groups 1 and 3) and their expansion (Group 2). In other words, the substitution of imports in the sector of intermediate goods allowed for a simultaneous increase in exports and in the trade surplus, making the sector responsible for about 75% of the total expansion of the latter.

The difficulties of the export-led growth can also be detected by the analysis of the industrial cycle. In the 1981/83 recessive period, the only industry segment to show positive growth was mineral extraction, both by replacing imports (oil) and by a greater export effort. The construction industry presented negative rates associated with cuts in public spending, as did the manufacturing industry because of the contraction of domestic absorption (Table 4).

In the manufacturing industry, despite the strong contraction of domestic demand, the expansion of exports acted as a compensatory factor for important industrial branches, especially for intermediate goods and some types of non-durable consumer goods, which had traditional insertion in the foreign market – textile, clothing and footwear, tobacco. As a result, production fell much less for non-durable consumer goods and intermediate goods, and more for capital goods and durable consumer goods, as shown in Table 9.

From 1984 onwards, the effects derived from the export drive had a significant impact on the capital goods and intermediate goods industries. According to Suzigan (1986; 1987; and 1988), in the recovery of production, the multiplier effect of the trade surplus occurred initially by the increase in the wage bill, boosting the sector of non-durable consumer goods. Persistent growth and rising average wages soon recovered the durable goods sector, which began to lead growth. This acceleration of the durable consumer goods sector, as mentioned above, was heavily influenced by episodes of conversion of financial assets into consumption, which marked the entire recovery period, further accelerating the sector's growth. The recovery of investment followed, with the expansion of the production of capital goods, transforming these sectors into growth leaders.

Table 9 – Industrial Production by Category of Use

	1981/89 (Total variation %)												
	1981/89	1981	1982	1983	1981/83	1984	1985	1986	1984/86	1987	1988	1989	1987/89
Capital goods	(6.9)	(19.2)	(15.2)	(19.3)	(53.6)	14.7	12.3	22.1	49.1	(1.7)	(2.0)	1.4	(2.3)
Intermediary goods	17.0	(11.1)	2.7	(3.0)	(11.4)	10.3	7.2	9.4	26.8	1.1	(2.3)	2.7	1.5
Consumer goods	15.7	(3.9)	3.1	(3.9)	(4.7)	0.2	9.0	10.8	20.0	0.2	(3.5)	3.7	0.4
Durable goods	8.2	(24.9)	8.0	(0.8)	(17.8)	(7.5)	15.1	20.5	28.2	(5.1)	0.5	2.5	(2.1)
Non-durable goods	18.1	1.1	2.1	(4.6)	(1.4)	1.9	7.9	8.5	18.3	1.5	(4.4)	4.0	1.1

Source: FIBGE.

After 1987, the industry returned to the recessive process due to the sharp reduction in domestic absorption, because of the foreign-exchange crisis and the acceleration of inflation. The export drive was once again the factor supporting growth, but it was not able to offset the retraction in domestic absorption. Symmetrically with the recovery period, the sectors that suffered the greatest reduction in production were capital goods and durable consumer goods (Table 9).

An important aspect to understand the rapid retraction in the production of durable consumer goods lies not only in the decrease in wage bill and average wages, but in the rapid inflationary acceleration and indexation of financial securities, associated with the increase in nominal interest rates, which had an effect of retraction in the consumption of durable goods, especially those with higher unitary value. The deep oscillation in the production of these goods over the 1987/89 period reflected the sudden shifts of financial assets to the consumption of high-value durable goods.

In summary, data on the cyclical performance of industrial production throughout the 1980s define the following trajectory: from the recovery of current production triggered by the export drive, the durable consumer goods and capital goods sectors regained the lead in growth, in a movement to restore the endogenous cycle, or internal markets as dynamic elements of growth. However, as we shall see below, this pattern of growth was incompatible with the maintenance of high trade surpluses, at least when historical growth rates were re-established.

The trajectory of the trade balance

According to Markwald (1987), there are two conceptions about the nature of the trade surplus in the 1980s. During the recessive period, the prevailing thesis was that the balance resulted from the reduction in domestic absorption associated with the change in relative prices. This would have resulted in an absolute reduction in imports, combined with an expressive growth in exports. With the recovery of 1984, the persistence of the trade balance gave rise to the thesis of the structural surplus. That is, as the recovery did not imply a significant expansion of imports, it was concluded that their reduction was due to more permanent changes in the productive structure.

The central idea of this thesis was that the import substitution process conducted during the Second PND allowed the economy to operate at increasing levels of activity, without significant changes in the import capacity. In the interpretation of Castro & Souza (1985), the possibility of generating surpluses after the elimination of idle capacity was admitted, that is, in the phase of acceleration of the cycle, of expansion of investment, and even with the restoration of historical growth rates.

This conception, based on the character of the structural adjustment carried out in the 1974/79 period, has as one of its main implications denying the relevance of the foreign-exchange constraint on growth throughout the 1980s. Disputing the traditional interpretation of the origin of the trade surplus, which would have resulted from the control of spending and changes in relative prices, the authors argue that exports grew more and imports decreased more than expected.

Concerning imports, they state that, at the beginning of the external adjustment process, not only was the imported coefficient very low, but that almost the entire range was made up of essential imports. The additional reduction in imports in the 1981-83 period covered the products that were the object of the Second PND programs, and whose projects came into operation precisely in that period – non-ferrous metals, chemical products, paper and cellulose, fertilizers, and steel products. In other words, the reduction in imports resulted from the reduction in the imported coefficient per unit of product, concentrated in the intermediate goods industry.

The argument is partially correct. However, it insists in not considering that both the total increase in exports and the global reduction in imports had an important cyclical component, that is, they were partly determined by the recession in the domestic economy. It would be more correct to say, as the authors suggest on some occasions, that with the same import capacity, the economy can operate at a higher level of activity.

The data in Table 10 leave no doubt about the importance of the cycle in the trade balance in the industrial sector. Greater domestic absorption caused variations of around 50% in the magnitude of the latter. Of the three groups with the greatest expression in the generation of the surplus, the one with the greatest sensitivity was exactly responsible for the largest share of the trade balance: the segment producing intermediate goods. The cyclical variation of the balance in deficit sectors is also relevant, confirming the sensitivity of the latter to the behavior of domestic absorption.

Table 10 – Evolution of the industrial sector's trade balance

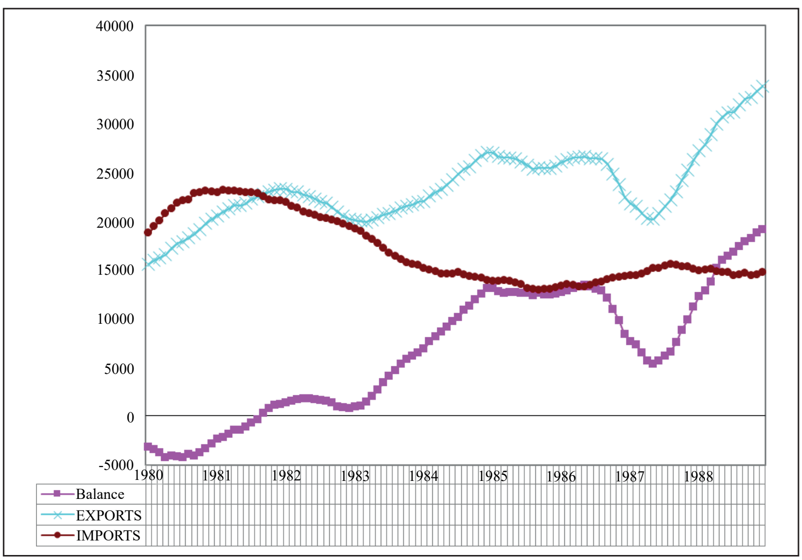
1980/89					
Years	Industrial Sector				
	Total	Group 1	Group 2	Group 3	Group 4
1980	−2,376.1	1,221.9	−1,526.5	571.3	−2,642.8
1981	1,663.0	1,440.1	637.6	1,297.5	−1,712.2
1982	1,627.8	1,220.5	946.4	1,162.9	−1,702.0
1983	5,192.4	1,715.1	3,406.5	941.2	−870.4
1984	8,794.2	2,102.0	5,708.8	1,088.4	−105.0
1985	7,858.1	1,819.9	5,038.5	1,382.7	−383.0
1986	4,555.1	1,559.2	3,498.4	821.9	−1,324.4
1987	6,752.2	2,051.3	4,246.7	1,852.0	−1,397.8
1988	12,427.4	2,324.5	8,833.1	2,578.2	−1,308.4
1989	11,292.5	1,994.0	8,039.0	2,726.3	−1,466.8

Source: Ipeadata, apud MDIC.

Group 1: Current consumer goods; Group 2: Intermediate goods; Group 3: Durable consumer goods; Group 4: Capital goods and elaborated inputs.

The analysis of the trade balance (Graph 8) shows three main periods during the decade: the 1981/84 quadrennium, in which the increase in the surplus was the result of both the growth in exports and the decrease in imports, with greater weight for the latter; the 1985/86 biennium, in which, from the beginning of 1985, the balance stabilized to decrease rapidly in 1986. As imports remained virtually at the same level, showing a minor increase, variations in the surplus were predominantly determined by fluctuations in exports. Finally, the 1987/89 triennium, in which the recovery of the balance occurred primarily as a result of the growth in exports, despite the new increase in the level of imports.[5]

Foreign Trade (US$ million in 12 months)



Source: *Boletim do Banco Central* apud FUNCEX.

A more accurate examination of the surplus indicates the existence of subperiods that deserve a precise assessment in their association with the economic cycle. From the beginning of 1981 until the beginning of 1983, the balance sign was reversed in a context of domestic recession. The reduction in imports was essential in this change of sign, as there was an important oscillation in exports, largely because of the global recession at the beginning of the decade.

5 A relevant exception concerns 1989, since, with exports stabilized, the surplus decreased due to the increase in imports. This year was, however, quite peculiar: with the economy on the verge of hyperinflation, there was a significant conversion of financial assets into real assets – including stocks of raw materials and instrumental goods without a national equivalent –, raising the level of imports.

In the following subperiod – between early 1983 and late 1984 – the surplus was growing, coinciding with the continuation of the recession in 1983 and the beginning of the recovery in 1984. Both the reduction in imports and the expansion of exports contributed to the increase in the balance. One should note, however, that the persistent reduction in imports was the common feature between both subperiods. The increase in exports, on the other hand, is associated with the recovery of international growth, especially in the United States, after 1984.

In the following period, several distinct phases were identified: from the beginning of 1985 to mid-1986, the value of the surplus was stable and, despite the domestic recovery, both exports and imports maintained their level, which was only possible due to the high degree of post-recession idleness. The decrease in the balance observed between mid-1986 and 1987, in a context of cyclical acceleration, resulted mostly from the reduction in exports. When the involution of domestic absorption occurred in mid-1987, it was the growth in exports that explained the recovery in the surplus. One can conclude, therefore, that from the middle of the decade onwards, fluctuations in the trade surplus, due to fluctuations in domestic absorption, were predominantly determined by variations in exports.

The proposition that the cyclical influence on the surplus occurred primarily by exports can be better verified through a disaggregated analysis. The quantities exported are the main determinant of the increase in the value of exports, offsetting the unfavorable evolution of prices between 1980 and 1985. The latter partially recovered in 1986 and grew slowly until 1989 (Table 10). The variation in the exported *quantum* has an inverse relationship with domestic absorption – which can be clearly seen in the years of intense recession, such as 1981 and 1983, or of great growth, such as 1986. Thus, the cyclical effect is of central importance in determining the value of exports, for example, in 1986, when the fall in exported value was only not greater due to the substantial improvement in prices. This, remaining after that year, contributes, along with the drop in domestic absorption, to the rapid recovery of the value of exports and the surplus.

In imports, despite the significance of domestic absorption, other elements affected the imported value. The most significant reduction of the latter occurred in the recessive period (1981/83), because of the sharp decrease in quantities, as prices remained at high levels. The continued decline in imported value during the first years of recovery was due to falling prices, since quantities stabilized. In the biennium corresponding to the peak of domestic absorption (1986/87), the fall in prices offset the rise in imported quantities. In summary, although the imported quantum is closely related to the domestic cycle, its impact on the imported value was significantly altered by price movements, indicating an important difference regarding the behavior of exports.

Table 11 – Foreign Trade: Price, Quantity, and Value Indices

1980/89

1980=100

Years	Export			Import		
	P	Q	V	P	Q	V
1980	100.0	100.0	100.0	100.0	100.0	100.0
1981	94.4	120.4	113.6	111.0	86.1	95.5
1982	88.8	109.9	97.5	107.3	79.1	84.9
1983	83.2	125.7	104.5	101.8	66.1	67.3
1984	85.0	153.9	130.9	96.3	63.5	61.2
1985	80.4	163.2	131.1	90.9	62.6	56.9
1986	86.0	134.2	115.4	72.0	82.6	59.4
1987	86.0	155.9	134.1	78.7	80.9	63.6
1988	94.4	183.6	173.3	86.0	71.3	61.3
1989	96.3	178.9	172.3	92.1	83.5	76.9

Source: Banco Central do Brasil. Relatório Anual (1989).

The above-mentioned questions acquire even greater clarity when analyzing imports and exports according to the main groups. The less pronounced cyclical effect in the case of imports, notably in the recovery phase, was due to a primary item: mineral fuels (petroleum). These, in addition to a reduction in the income elasticity of demand, which attenuated the growth of the imported quantum, underwent an important price reduction, whose intensity contributed to decrease the imported value until 1986. As this is the main item on the list of imports, it is understood why these had a less pronounced sensitivity to the domestic cycle. Strictly speaking, the decline in oil prices explains why the growth in domestic demand did not translate into expressive growth in total imports. Note, for example, that in other groups, especially in capital goods, the cyclical effect was quite intense and was not mitigated by a favorable evolution of prices (Table 12).

Table 12 – Price, Quantity, and Value Indices of Imports, by Groups

1980/89

(1980=100)

Years	Mineral Fuels			Raw Material			Consumer Goods			Capital Goods		
	(Q)	(P)	(V)	(Q)	(P)	(V)	(Q)	(P)	(V)	(Q)	(P)	(V)
1980	100	100	100	100	100	100	100	100	100	100	100	100
1981	95	117	111	75	108	81	68	111	75	93	99	92
1982	92	111	103	66	100	66	67	114	76	63	118	75
1983	87	97	84	50	100	50	61	98	60	55	105	57
1984	81	89	72	62	86	53	66	80	53	68	72	49
1985	72	84	61	58	90	52	66	91	60	74	76	57
1986	80	43	35	91	81	74	214	65	138	91	87	79
1987	88	53	46	81	89	72	130	77	101	74	122	90
1988	92	38	35	52	137	72	73	125	91	62	154	96
1989	87	50	43	60	159	95	163	119	194	63	164	104

Source: Cacex.

The evaluation of exports by main groups (Table 13) shows an evolution defined by exports of manufactured goods. The first reason for this is the growing weight of these goods on the total exports.[6] In turn, the correlation between the domestic cycle and the value of manufactured exports, especially with the exported quantum, is expressive. The latter, after growing systematically between 1981 and 1984, declined in 1985/86, recovering from 1987 onwards. After that year, the clear recovery in prices helped the rapid expansion of the exported value.[7]

In the other groups, these relationships, although present, were less intense. Note, for example, that the exported quantum continued to grow in 1985, in the second year of recovery. Even in 1986, the fall in semi-manufactured goods was milder and was only intense in the case of basic goods, due to the fall in the agricultural harvest.

6 Data from Cacex show that the share of manufactured goods was already high in 1980 (45%), reaching a new level in the recessive period, reaching 56% in 1984 and oscillating around this value in the second half of the decade.

7 The recovery of prices is associated with the overcoming of exchange speculation – under invoicing of exports – that occurred in 1986, as a result of the freezing of the official exchange rate and the rise in dollar quotations in the parallel market.

Table 13 – Price, Value, and Quantity Indexes of Exports

1980/89

(1980=100)

Years	Basic			Semi-manufactured			Manufactured		
	(Q)	(P)	(V)	(Q)	(P)	(V)	(Q)	(P)	(V)
1980	100	100	100	100	100	100	100	100	100
1981	112	94	105	95	95	90	153	86	132
1982	107	91	97	81	76	61	166	68	114
1983	98	101	101	113	67	76	227	55	125
1984	117	88	103	166	73	120	299	56	168
1985	121	83	101	188	63	117	277	56	156
1986	112	77	86	179	59	106	233	59	137
1987	119	79	95	203	67	135	236	70	164
1988	140	79	111	250	83	208	296	72	213
1989	138	82	113	302	82	247	231	89	206

Source: Cacex.

What can be concluded from the previous analysis is that, during the recovery period, the exchange restriction, due to greater domestic absorption, did not manifest itself more intensely in the evolution of imports because the behavior of prices was favorable. It was in exports, particularly in manufactured goods, that it was possible to accurately assess the existence of a trade-off between continued growth and the preservation of trade surplus.[8]

Castro & Souza (1988) does not share such conclusions. The authors reassert their position of believing in a structural surplus, arguing that, even when idle capacity disappears, the surplus could be preserved. To explain the drastic decrease in the trade balance, after two years of recovery, the authors use the speed of demand growth as a central argument. They consider that demand growth may exceed potential product growth within certain limits, due to the use of idle capacity. Nevertheless, when this growth is very fast and intense, only by using stocks or reducing the balance can the excess demand be met.

There are two basic aspects in the authors' argument, which are true: first, it seems undeniable that demand growth was in fact very fast, notably due to the wealth effect triggered by the Cruzado Plan. Furthermore, as the authors warn, in an economy with a small degree of openness this phenomenon may in fact imply a substantial reduction in the balance. What the authors do not

8 Markwald (1988), analyzing the recovery period (1984/86), reaches the same conclusions, advocating the existence of a severe trade-off between growth in domestic demand and trade balance. The growth of imports, but mainly the reduction of exports, would be responsible for this incompatibility.

analyze in detail, however, is the level of utilization of the installed capacity in the main export sectors. Only the persistence of idle capacity in these sectors would attest to the veracity of their theses; otherwise, the speed of demand growth would only have anticipated an inescapable result.

In other words, the fundamental criticism that can be made to this exercise is that it works with the average degree of utilization of productive capacity, therefore disregarding dispersion. In other words, it disregards the possibility of differentiated export insertion and of the sectors responsible for a significant portion of exports reaching the productive capacity limit before the other productive sectors. If this happens, continued growth in domestic absorption will imply a reduction in the surplus, by a reduction in exports or an increase in imports. Let us therefore confront these possibilities with empirical evidence.

The data in Table 14, on the use of the installed capacity in the industry, reaffirm the previous conclusions. The evolution of the degree of utilization means that, in 1986, pre-recession levels was reached. In the same way as the exported coefficient, the dispersion in the degree of utilization increased in the recessive phases and decreased in the recovery, indicating that the export drive unevenly affected the production of the different sectors.

Thus, Suzigan & Kandir (1985), when analyzing the recovery of industrial production from the growth of exports in 1984, point out that, at the beginning of this recovery and as a reflection of the previous period, the industry presents a high degree of dispersion in the levels of use of productive capacity, with higher degrees of utilization in the sectors producing tradables and lower ones in the producers of non-tradables.

Also according to the data in Table 14, the sector with the smallest reduction in capacity utilization in the recessive phase was intermediate goods, reflecting the importance of the foreign market as a destination for production. Therefore, during the recovery phase, this sector quickly reached the limit of the installed capacity, working for six months with the production capacity virtually exhausted, in the last quarter of 1986 and in the first quarter of 1987.[9] In other sectors, the problem existed, but it was more localized.

9 The data in Table 39, as they are average data - whether from the point of view of time (year) or sector (goods) - hides the depletion of capacity in several subperiods and subsectors.

Table 14 – Of Installed Capacity in Industry (in % of Total)

	1980/89											
Items\Years	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	MAX.	MIN.
Average	84	78	76	73	74	78	83	81	80	81	84	73
Sectors												
Consumer Goods	84	74	74	74	72	77	81	77	76	78	84	72
Capital Goods	82	74	65	56	61	67	76	76	75	76	82	56
Construction Material	88	82	80	71	68	72	77	78	76	74	88	68
Other Intermediary Products	88	80	80	79	81	83	86	87	86	86	88	79
Goods												
Production of Non-metallic Minerals	90	85	82	75	68	70	78	81	80	76	90	68
Metallurgy	90	81	76	77	84	87	87	85	85	88	90	76
Mechanics	80	73	66	60	63	72	79	76	75	76	80	60
Electrical and Communication Material	80	72	72	68	68	76	81	81	75	74	81	68
Transport Material	87	71	64	63	64	68	78	72	76	77	87	63
Wood	86	77	80	72	76	79	84	81	78	83	86	72
Furnishing	80	73	76	70	69	77	86	75	72	74	86	69
Cellulose, Paper, and Cardboard	91	87	88	85	88	88	90	90	88	89	91	85
Rubber	95	82	77	70	77	84	88	89	88	84	95	70
Leathers and Skins	78	71	77	77	73	74	75	72	76	74	78	71
Chemistry	89	81	81	82	81	82	84	88	86	87	89	81
Pharmaceutical and Veterinary Products	83	80	78	78	79	78	84	84	82	81	84	78
Perfume, Soap, Detergent	89	85	83	75	74	76	81	84	80	77	89	74
Plastic Material	82	72	74	67	65	71	83	78	71	77	83	65
Textile Industry	90	82	84	80	80	88	91	88	87	89	91	80
Clothing, Footwear, and Fabric	88	84	84	83	79	82	86	84	84	88	88	79
Food Products	76	74	73	73	73	76	74	74	71	73	76	71
Beverages	85	83	81	79	78	77	84	79	81	86	86	77
Tobacco	83	82	78	70	68	76	87	92	93	77	93	68
Editorial and Graphics	73	75	77	75	72	75	82	79	74	81	82	72
Diverse	84	79	76	73	72	85	89	90	81	86	90	72

Source: Fundação Getúlio Vargas. Sondagem Conjuntural

In sectors predominantly producing intermediate goods, capacity utilization was systematically above average in the various phases of the cycle, and, in addition to its smaller variation, full utilization was evident in some segments, such as in chemical, metallurgical, and paper and cardboard ones.

In consumer goods, the lower pressure of the domestic cycle did not exclude the existence of important export goods with virtually exhausted capacity at the peak of domestic absorption, as is the case in the textile sector. In sectors predominantly producing capital goods, the problem was not relevant, with high levels of idleness even at the height of the cycle.

The general conclusion about the data seems obvious: the depletion of domestic productive capacity due to the growth of internal absorption occurred in the intermediate goods industry and in some consumer goods segments, exactly those that presented a high export coefficient. The trade-off, therefore, turns out to be more intense and localized than the average data would lead us to believe.

The above assertion invalidates Castro & Souza's (1988) argument that the decline in exports in the 1984/86 recovery was mainly due to the speed of growth in domestic absorption that have prevented the progressive recovery of the use of productive capacity, diverting exports to the domestic market. As shown, this occurred because important export sectors – in particular the one of intermediate goods – ran out of idle capacity, making it impracticable to maintain the volume exported without expanding production capacity.

CHAPTER 14

THE LIBERAL-CONSERVATIVE COUNTERREVOLUTION AND THE LATIN-AMERICAN CRITICAL TRADITION: a prologue in honor of Celso Furtado[1]

João Manuel Cardoso de Mello

Almost 50 years ago, in the Estudio de 1949, Raul Prebisch showed that the idea of the harmony of interests promoted by capitalist competition was even more fallacious when transposed to the international level in the form of the theory of comparative advantages: the uneven development of the world economy, conceived in terms of the core/periphery relation, tended to reproduce and deepen under the aegis of the free play of market forces.

Celso Furtado, on the other hand, has insisted since the mid-1950s that underdevelopment consists of the asymmetry between the cosmopolitan consumption pattern of a privileged few – who are in fact integrated into the developed world – and the structural weaknesses of peripheral capitalism. And he has shown that the inequality that deforms our societies also tends to reproduce and deepen, if we insist on copying the prevailing lifestyles in central countries, even in the most favorable situation of what he called industrialized underdevelopment.

Based on the tradition of Latin American critical thinking, I intend to discuss here, in a quick and very simplified way, the essential meaning for the peoples on the periphery of what has been called the process of globalization.

Unlike those who have a naive faith in progress, I think the world is facing an extraordinary liberal-conservative counterrevolution, which, for us, means productive regression, more social exclusion, and a return to external dependence.

1 At the base of this article are the notes I wrote, with the always invaluable help of Luiz Gonzaga Belluzzo, to guide my exhibition at the Seminar in honor of Celso Furtado, held in Paris, in March this year. Maria da Conceição Tavares and José Luiz Fiori read them with generous eyes and wanted to welcome them in this journal at all costs. Its transformation into a Prologue is due to a friendly suggestion and, moreover, to the honorable collaboration of Paulo Arantes, to whom I am very grateful.

1.

From an economic and political point of view, I believe the capitalist Core could be defined by three types of controls: the first would be exerted on the process of technological innovation, which supposes forms of capitalist organization in which financial power would be incarnated; the second concerns international money and finance, which in turn presuppose industrial power; the third concerns political-military power, ultimately, the control of weapons.

From England's industrial monopoly, its corresponding financial power and its political-military supremacy, a process of restricted expansion of the Core took place during the 19th and early 20th centuries. This expansion occurred basically in two moments, in fact two successive waves of backward industrializations.

The first of them resulted in the industrialization of the United States, France, and Germany. English production and consumption patterns were copied at a time when technology was simple and was propagated through masters and specialized workers, while, on the other hand, industrial production patterns did not require large scales or gigantic volumes of initial investment. Even so, we can observe a structural discontinuity between the starting point and the financial prerequisites, especially those required by the railroad, the nucleus from which the production goods industry (machinery, metallurgy, and mining) can be established. This same structural discontinuity is also responsible for new emerging forms of capitalist organization. The main one would come to be the development bank, as well as the strategic role assumed by the State, acting decisively in the promotion of industrialization.

The second wave resulted in the industrialization of Japan and Russia, at a time when the Second Industrial Revolution was already underway (steel, oil, soda, and chlorine chemicals, electricity, internal combustion engine, etc.). The conditions under which this new propagation of industrial capitalism takes place are therefore quite different from the previous one. For starters, the minimum scales in terms of investment, employment and sales are now gigantic. There is also an enormous increase in risk and uncertainty due to the "cross-effects" of the technology. At the same time, technology itself changes its nature: not only does it come to depend on the rational use of science, but it also tends to be monopolized by large companies. This scenario results in an even more pronounced discontinuity between the initial conditions – the previous development of capitalism – and the requirements in terms of capital accumulation to be satisfied by the investment block. The role of the State is also accentuated, its preponderance reaching truly revolutionary dimensions. In turn, the forms of capitalist organization – such as "Zaibatsu" – require an even more advanced deepening, gathering, under a single command, industry, financial and mercantile power.

As for the configuration of the underdeveloped Periphery, we can say it is the result of a particular form of expansion of the capitalist Core, which results from the encounter of the Core with societies in which “archaic” social relations and relations of production predominated. Three elements characterize the underdeveloped Periphery: the dynamically dependent nature of the productive system; international monetary and financial fragility; political-military subordination. These are the determinant traits of the peripheral condition and not exactly the production of food and raw materials. Historically, such production of food and raw materials is a particular form of subordination, corresponding to the division of labor imposed by England. From a social perspective, the underdeveloped Periphery presents itself as a society marked by heterogeneity. A small segment of the population enjoys standards of living typical of the Core, while the vast majority find themselves excluded.

As English hegemony declined and the United States, Germany and Japan rose, the Periphery became an object of rivalry between the national capitalist economies. During this stage, called imperialist, the Periphery was disputed as a supplier of raw materials, as a market for industrial products and as a recipient of capital. We know this rivalry culminated in two world wars, which in turn defined the new hegemonic Core, the United States.

At this point, it must be clear that the trente glorieuses (30 glorious years) was characterized by its exceptionality, by a historical peculiarity that has not been sufficiently emphasized, namely: that the American hegemony was in fact exercised in an environment of competition between capitalism and the real socialism. Thus, we cannot forget that the reconstruction of Europe and Japan was conducted in the shadow of the Soviet Revolution and the Chinese Revolution. Decisive particularity, to which was added the struggle of European democratic forces and American new dealers, forged amid two world wars, the Crash of 1929, and the horrors of nasi-fascism. Some sought to build institutions – both internationally and nationally – capable of preventing the catastrophes caused by uncontrolled capitalism. Not surprisingly, this political front of the reconstruction process included, alongside progressive forces, conservatives such as Konrad Adenauer, De Gasperi, and others.

It is unnecessary to remember that the international institutions created in Bretton Woods remained far short of the original project by Keynes or Harry Dexter White – especially regarding the autonomy and scope of action of bodies such as the IMF and the World Bank. Nevertheless, the United States was able to exercise its hegemony to pave the way for national policies of economic development and social reform. As a result, from the immediate post-war period to the end of the Bretton Woods system in 1979 (when the United States unilaterally assumed responsibility for maintaining the position of the dollar as a reserve currency), generalized economic growth took place in the Periphery.

It so happens that only two countries – Brazil and Korea – were able to build integrated industrial systems. But unlike Brazil, only Korea managed to internalize the basic conditions to make its capitalism dynamic, that is, endowed with a minimum of autonomous capacity for financing and innovation. As for other countries, the dissemination of the results of the Second Industrial Revolution was quite restricted and it is not difficult to find out why. In the middle of the 20th century, the absorption of the results of the Second Industrial Revolution required a dramatic leap, an extraordinary mutation of pre-existing economic structures, which supposes practically unattainable financial and technological preconditions. And yet, seen from a social perspective, heterogeneity and exclusion do not cease to be reproduced. This means that only a fraction of the Periphery continues to integrate to the standards of living prevailing in the Core. In short, even in a relatively favorable international situation, peripheral capitalism proved to be incapable of supplying the basic needs of the population as a whole.

2.

We are now witnessing a capitalist restructuring that encompasses the Core and the Periphery. Inside the Core, the movement is of intense concentration of capitalist command at all levels: on technical progress, currency, financing conditions, adjustment of the balance of payments. And, particularly, concentration of military power. We can distinguish several dimensions in this concentration. First, competition intensifies between large companies in the space of the core economies. These same companies, anchored in an extraordinary financial power, in turn, trigger the Third Industrial Revolution. A second dimension can be recognized in the unification of financial markets, which change their nature. Since then, the supremacy of capital markets has imposed itself on the traditional bank credit system. By deregulating the capital market (by the way, deregulation promoted by governments whose growing public debts support the securitization of operations), we return to the system of free movement of capital before the Crash of 1929. Thirdly, this extraordinary private economic power – of productive companies and financial organizations – launches itself in a hostile way against national social protection policies, on the one hand, and on the other, against national policies for the preservation of industrial systems aimed at the internal market, transforming National States into hostages of the policies of the Big Money. With this, the public dimension of the National States – conquered throughout the democratic struggles of the 20th century – is dramatically dwindling. Finally, given the unequal nature of the different national capitals, a hierarchy defined by relations of domination/subordination is established between the National States. Suffice it to note, as an example, the French subordination to the German economic policy. It should also be added that if the United States by any chance lost its productive leadership to Germany and Japan, it certainly maintained its military supremacy, or its monetary and financial power, in the last resort.

As far as the Periphery is concerned, there is another trend that Celso Furtado has been calling our attention to. I refer to a certain alignment of the increasingly uniform positions of the Core regarding the role reserved for the Periphery. Simply all the core countries demand that the Periphery open itself to foreign competition and to investments of its productive and speculative capitals.

I believe I am not exaggerating when I say, in the face of such a capitalist restructuring, which has so profoundly affected the Periphery, that deep down we are suffering from a true liberal-conservative counterrevolution. This can be seen if we turn to the other historical meaning of the term periphery. In the form of structural unemployment, social heterogeneity, the duality of the labor market, the decay of entire regions and industrial disintegration, the periphery is being reintroduced in core countries.

In most of the traditional Periphery, such as in Latin America, the trends are towards productive regression, accompanied by the disappearance of the national currency, the final advance of the cosmopolitanization of consumption patterns, the deepening of inequalities and social apartheid. This does not mean, however, that such a regression diminishes the region's economic significance. On the contrary, the regression in question does not prevent the Periphery from being used by large companies to relocate their investments, taking advantage of cheap labor and the unbridled competition among countries to attract multinationals. This allows the multinational company to distribute its investments in a way that maximizes cost reduction. In most cases, disorganizing and dismantling more integrated production structures.

At the same time, the Periphery becomes a field of application for speculative capital. The cycle of private foreign financing in currency has been affecting the ability of countries to maintain an exchange rate that is favorable to exports and, in general, forcing governments (in the case of sterilization of capital inflows) to accumulate high and costly public debts. Also, in the case of Latin America, the modernization "proposed" by the United States

– through multilateral organizations managed by the hegemonic power – implies transforming the continent into a captive market for American exports and into a territory of expansion for its concentrated capitals, in general, in the privatization of public utility services. Furthermore, the fiscal capacity of the State has been weakening under the growing weight of expenditure on interest, reducing public spending and thus liquidating the Welfare State experiments carried out over the last decades.

It is not surprising under these conditions that military dictatorships have become obsolete. After a short period of political struggle, they were replaced with advantage by the dictatorship of the markets and by the return of American domination, always in alliance with the local elites.

That said, a final note – preceded by the simple observation that, as in all moments of capitalist restructuring, the consequent reconstruction of the Periphery alters the relative positions occupied by the countries. I am thinking, of course, of the great phenomenon of the end of this century, and probably an event that will mark an epoch in history: the development of China. Not just any development, but development induced by a complex strategy carried out by its National State. This strategy simultaneously involves the attraction of foreign capital, the central role of the State and public companies, as well as the maximization of the military geopolitical situation.

Conclusion

- Capitalism generalizes only market relations. It proved incapable of promoting the birth of integrated systems, and of broadly spreading technical progress. In general, the expansion of the Core only took place through national revolutions or national development projects, as it occurred with Korea and China in this century.
- World capitalism has also proved incapable of promoting the social homogeneity of the peoples of the underdeveloped Periphery. Social heterogeneity reproduces itself, while a small portion of the population integrates into the Core.
- These structural tendencies of capitalism, attenuated in the "30 glorious years," were aggravated by the Third Industrial Revolution and financial globalization.

To these conclusions I would like to add some additional remarks about the present capitalist restructuring.

I am convinced that we are living, so to speak, at a time inverse to the immediate post-war period, which Polanyi called the Great Transformation. At that point in the century, capitalism seemed to have been tamed by society. Now that it has broken through the shell that subjected it to protecting the populations, we can speak of capitalism's revenge on society.

Everything happens as if the fundamental trends of capitalism have re-emerged with redoubled intensity. The monstrous development of finance capital showed an indisputable truth. Or on the other hand, a well-known truth from Marx and Keynes, Braudel and Polanyi – we were the ones who walked a little numb through the decades of domesticated capitalism, forgetting that it is a regime oriented towards the pursuit of abstract wealth, in general expressed by money. This destructive abstraction appears with all its raw force in the current speculative rentism. But it appears covered by the technological veil of the productive forces unleashed by the Third Technological Revolution, under which the conflict between productive capital and speculative capital is also camouflaged. Hence the huge disparity between the growth of recent years – mediocre compared to the so-called 30 glorious years of the post-war period – and the immense development potential that the application of modern science could offer to humanity, were it not blocked by the predominant forces of capitalist property.

There remains the growing redundancy of living labor. Another fundamental trend – the devaluation of labor – has returned in full force. The structural unemployment, the precariousness of work, the intensification of income disparity, the heterogeneity of the labor market and the worsening of poverty show what capitalism has always been, a gigantic machine to produce inequality.

That is what I would like to say about the liberal-conservative counter-revolution unleashed by the globalization of Capital. I hope that it is in line with the critical tradition of Latin American economic and social thinking – today, fortunately, against the "pensée unique" – and in the company of Celso Furtado, who continues to teach us lessons of intellectual lucidity and moral courage.

CHAPTER 15

BRAZIL: The national formation dilemma

Plinio de Arruda Sampaio Jr.

1. The formation dilemma

Interpretations of the formation of contemporary Brazil seek to explain the contradictions that hinder the full constitution of our Nation in Western civilization. They concern the identification of how the colonial heritage and the subaltern position in the world's capitalist system compromises the ability of Brazilians to govern their own destiny. This problem is based on the need to ensure the continuity of historical processes responsible for consolidating the material, social, spatial, political, and cultural bases of the nation-State.

Thinking about formation is determined by the opposition of two latent states in dependent society: the condition of barbarism one wishes to avoid and the civilizing project that is sought. The challenge of societies fighting for nation building results in the need to overcome the dark present of a people that cannot overcome the condition of subnation to approaching a paradigmatic situation associated with the ideal functioning of the nation-State. The meaning of formation is defined by oppositions such as anomy and organization; fragmentation and unification; marginalization and integration; heteronomy and autonomy; instability and stability; underdevelopment and development. Using these antinomies as reference, the social changes that point to the latter are associated with the idea of progress, contributing to the consolidation of Brazilian civilization; and those who turn to the former are linked to the notion of decay, leading to neocolonial reversal and the advancement of barbarism.

Rejecting transplanted analyses of hegemonic centers, the central concern of interpreters on Brazil is to find the specificity of our historical problems and their possible solutions. Starting with José Bonifácio, going through Alberto Torres and Oliveira Vianna, to modern authors such as Gylberto Freire, Sérgio Buarque de Hollanda and Antônio Cândido, the thinkers who looked at the dilemmas of formation essentially highlighted the same problems. The difficulties in affirming itself as a nation stem from the terrible contradictions of a social formation marked by the genocide of pre-Columbian civilization; by the ultra-elitism of a society unable to resolve its debt with its slavery past; by the predatory nature of economic activities towards the environment; by the country's extreme vulnerability to the vicissitudes of international capital and the agency of the imperialist system; the inadequacy of the productive base to meet the needs of the people; the obstacles faced in order to assert dominance over a continental territory, composed of poorly articulated and disjointed regions; by the lack of national identity of a recent human cluster from different parts of the globe; the precariousness of the administrative and political institutions that constitute the government; and finally, by the entrenched cultural colonialism of our elites.

Those who reflected on the challenges of the national formation from a democratic perspective, in one way or another, associated nation building to the integration of the whole population, under conditions of relative equality, to technical advancements and humanist values of the modern era. Above its theoretical, historical and ideological differences, a common denominator unifies this view: the idea that the country's problems will not be resolved without profound sociocultural transformations that create the foundations of an equitable and autonomous society.

Devised in opposition to the oligarchic tradition, which defends nation building as an end in itself, democratic thought sees the structuring of the Brazilian government as a means of submitting development to the designs of a society united in the defense of a common destiny for its citizens. Before conditioning the emergence of our nationality to the emergence of a new race derived from miscegenation, to the control of a vast territory rich in natural resources and to the unlimited potential of its economy, to the structuring of a state apparatus capable of imposing the authority of order and the misplaced vainglorious dreams of a hypothetical Brazilian power - chauvinistic notions that conceal the hierarchical and authoritarian nature of our social formation -, democratic thought understands the affirmation of nationality as the necessary crystallization of a homogeneous society, carrying the humanist values of Western civilization, based on moral links between social classes and the existence of organic ties between the different regions of the country.

In this approach, the national space is nothing more than an instrument to protect the collectivity from the destructive effects of transformations that radiate from the core of the world's capitalist system and to plan the internalization of the structures and dynamism of Western civilization in a way consistent with the progressive increase in the degree of autonomy and creativity of society, as well as the elevation of the wealth and well-being of the entire people. Thought of as a center of power that condenses the political will of the collective, the nation form serves here - solely and exclusively - as a means for societies that live overdetermined by the field of force of the world's capitalist system to control their historical time. It is, therefore, a historically determined instrument that should be overtaken by higher forms of social and political organization, of supranational scope, as soon as the world's historical context allows it. That is, as soon as the world order ceases to be under the control of the logic of intercapitalist competition and the interstate rivalries of imperialism.

Within the democratic tradition, which encompasses a broad spectrum of views on the meaning of the formation, it is assumed that, while the contradiction generated by the subaltern position in the world's capitalist system is not irreconcilable with the continuity of the processes responsible for the constitution of the nation-State, the emerging nation grows and develops in the context of dependent capitalism. However, when the contradiction becomes irreducible antagonism, dependent capitalism completely divorces itself from national society, becoming incompatible with the continuity of the civilizing process. Henceforth, the society begins to experience a decisive crossroads of its formative process, because the rupture with the external and internal structures that sustain the current order becomes the only means of avoiding barbarism. From this moment on, it can be concluded that the society enters a revolutionary conjuncture, which can lead both to a positive outcome - the consummation of the Brazilian revolution and the opening of a new historical horizon - as well as to a negative solution - the counterrevolutionary reaction and the strengthening past trends that stifle the future, aborting nation building.

In this chapter, we will present the reasons that led three of Brazil's greatest interpreters – Caio Prado, Florestan Fernandes and Celso Furtado – to the dramatic conclusion that the building of contemporary Brazil has reached a boiling point in which overcoming the situation of dependence has become not only necessary, but urgent. Starting from different perspectives, the analyses of the three authors converge to a common diagnosis: between 1950 and 1980, the contradiction between dependent capitalism and national formation might have become one of open antagonism. Contrary to what the accelerated modernization of consumption patterns and the deepening of industrialization would suggest, dependent capitalism would have exhausted all of its constructive properties and its permanence would be leading Brazil to barbarism. Therefore, in order to survive as a national project, Brazilian society would no longer have any alternative but to break with the economic, social and cultural relations responsible for the subaltern insertion in the world economy and for the perpetuation of the asymmetries inherited from colonial society.

Being a historian concerned with understanding the long-term movements that condition the formation of contemporary Brazil, Caio Prado defends the theory that control by international capital over the import substitution industrialization process - a phenomenon that gains momentum in the post-war period, particularly with Juscelino Kubitschek's developmental policy - causes an irreversible tendency to neocolonial reversal.

A sociologist who investigated the dilemmas of the bourgeois revolution in Brazil, Florestan Fernandes showed how a series of external and internal circumstances, which culminated in the military coup of 1964, allowed the Brazilian bourgeoisie to consolidate its pattern of domination and preserve its bargaining power in the world's capitalist system, thus avoiding neocolonial reversal (albeit at the expense of strengthening its antisocial, anti-national and undemocratic character). In the 1980s, such circumstances dissipated, making the spectrum of Brazil's disaggregation reappear.

Lastly, economist Celso Furtado, who sees development from the perspective of accumulation, warns that the inability to defend the Brazilian economy from the disruptive effects of the transnationalization of capitalism - especially after the outbreak of the external debt crisis in the early 1980s - began to compromise the continuity of nation building, questioning Brazil's very territorial unity. In the next sections, we will systematize the line of argumentation of each of these authors and show the timeliness of their predictions.

2 - The modernity of the Brazilian revolution

According to Caio Prado, the formation of contemporary Brazil is driven by the non-conformist reactions provoked by the deep malaise related to poverty, backwardness, instability and irrationality that characterize the life of the country. It is this long-term historical process that leads to the appearance of a progressive differentiation between the Portuguese colonizer and a new historical character, the Brazilian. Thus emerges the rough sketch of a people struggling to control their destiny. "But - as the author warned - such a more stable, permanent, organic character, of a specific and defined society, will only reveal itself gradually, dominated and smothered as it is by what precedes it, and which will continue to maintain the primacy and dictate the essential features of our colonial evolution."

For Caio Prado, the driving force behind the formation of Brazil is the growing incompatibility between the domination of the imperialist system and the progressive commodification of society, an incompatibility that is manifested by the increasingly catastrophic effects of the structural reversal crises that recurrently shake the country's life. One of the main challenges of an emerging nation is to bring a modicum of stability to capitalist development. The author's brief synthesis of economic cycles before the beginning of import substitution industrialization illustrates well the inadequacy of the colonial economy as the mainstay of a national society: "An international scenario favorable to whichever product that the country is capable of supplying drives its functioning and gives the illusory impression of wealth and prosperity. But once such a situation changes, or once natural resources are depleted for the specific purpose of the export-oriented organization, production declines and tends to annihilate itself, making it impossible to maintain life and its prior activities. In each of the cases in which a Brazilian production branch was organized (sugar, gold and diamonds, cotton, coffee, rubber, cocoa and so many others of lesser importance), nothing was considered other than the momentary speculative opportunity present at that moment. Thus, the necessary elements were immediately mobilized: a certain area of the most convenient territory is populated, or repopulated, with managers and workers of the company that is installed - a true work group -, this is how production is organized. It will not go much further than this, nor do the conditions under which such an organization was made allow for it. And it will continue until the final exhaustion either of the available natural resources, or of the favorable economic situation. Then there is the stagnation and decline of activities. And what is left of the population that cannot emigrate in search of other similar adventures starts to vegetate without having to apply themselves to obtain regular and adequate means of subsistence."

In Caio Prado's view, by stimulating the development of productive forces aimed at serving the domestic market and increasing the differentiation between foreign and native interests, capitalist development nevertheless tends to create the objective and subjective bases for the consolidation of Brazil as an economic space that has "autonomous existence" and "its own strength." On the one hand, settlement, territorial occupation and the economic and institutional organization of Brazilian society generate a growing differentiation between the merely mercantile objectives of capital in the country's economic life and the needs and aspirations for a better life that galvanize the people's imagination. On the other hand, the gradual demographic growth and its greater integration in the consumer market makes the narrowness of the colonial economy as the mainstay of the young nation more and more evident, stimulating the expansion and diversification of the productive system aimed at the domestic market.

In this secular movement of transition from colonial Brazil of yesterday to the nation Brazil of tomorrow - the main line that gives meaning to formation -, Caio Prado postulates that the disarticulation of the international division of labor initiates a period of "final crisis" of the Brazilian colonial system. His argument is that the drastic contraction of international trade, which reached its climax with the collapse of the world economy in 1929, simply made primary-export economy unfeasible as the material base of a society at an accelerated pace of expansion and diversification of the domestic market. For this reason, the contradiction between the reproduction of the imperialist system and the nation-building movement tended to turn into open, irreducible antagonism.

The structural crisis in the external sector, however, opened new perspectives for the Brazilian economy, as the isolation of international competition created a market situation that stimulated import substitution industrialization.

In Caio Prado's interpretation, until the end of World War II, industrialization progressed relatively spontaneously, reinforcing the crisis in the colonial economy and pointing to a positive solution. The use of technologies for widespread use, which did not require large mobilizations of capital, allowed for the pace and intensity of import substitution to be controlled internally, respecting the market opportunities that arose from the unfolding of industrialization itself, as well as from the gradual increase in accumulation capacity of the local business base. Industrialization then contributed to the generalization of wage-earning relations, to the intensification of urbanization, to greater integration of the Brazilian market, to an expressive development of productive forces aimed at the domestic market, and to the strengthening of the national business base.

The import substitution process would have radically changed its meaning in the post-war period, since, in Caio Prado's understanding, the control of international capital over the dynamic sectors of the industry would irremediably compromise the movement to nationalize the Brazilian economy. In addition to distorting the constructive character of the organic relations that were formed between the productive forces, the native business base and the internal market, the dominant presence of the large multinational trusts dangerously reinforced the external dependence ties of the Brazilian economy. For this reason, even when acknowledging the importance of foreign capital in expanding the productive base and, above all, its decisive role in the internalization of the capital goods and durable consumer goods industries, Caio Prado concludes that Brazilian society was beginning to lose control over the finality, the pace, and the intensity of the import substitution process. Contrary to what the expansion of the industrial park and the consequent contraction of the import coefficient might suggest, the Brazilian economy was subject to forces that would tend to rebuild the old colonial system. In the heat of the moment, he summed up the issue in the following terms: "(...) what imperialist undertakings determine in the current Brazilian situation is a deformation and diminishment of what our industrialization process should be. As such they represent a reinforcement of the colonial system that is the core cause for our deficiencies, limiting development to the narrow horizons of that system."

Caio Prado's argument regarding the limited strength of the post-war industrialization cycle and its high vulnerability to structural reversibility unfolds considering essentially four aspects of the problem.

First, the leadership of the large international trusts generated serious distortions in the pattern of commodification of the economy, since, by driving the replacement of increasingly sophisticated products, it required a greater concentration of income, making the divorce between the country's productive structures and the real needs of the Brazilian population even clearer. Differently from what happened in the previous movement of capital internationalization, when international capital adjusts to the contour of the internal market, in the mature phase of monopoly capitalism, the internal market of the peripheral economy must adjust to the commercial interests of foreign capital.

For Caio Prado, the segmentation of the internal market between rich and poor would tend to compromise the continuity of the industrialization movement for two reasons. On the one hand, the limited consumption capacity of large contingents of the population generated a growing incompatibility between the tendency to progressively expand minimum scales of production and the impossibility of a similar movement in society's consumption capacity. On the other hand, the narrowness of the domestic market, by intensifying the heterogeneity between the Brazilian market and that of the more developed countries, would tend to further diminish the relative importance of the national economic space in a worldwide context.

Moreover, the control of the strategic links of Brazilian industry by international capital prevented the consolidation of a business base umbilically linked to the national economic space, generating a growing asymmetry between the degree of development of the productive forces and the technical and financial bases of the Brazilian private sector. Unlike what happened in the 19th century, when the internationalization of domestic markets encouraged the strengthening of private initiative in economies receiving direct investments, the predatory character of monopoly capital during the more advanced phase of imperialism led to the relative atrophy of national capital. Therefore, instead of fostering the development of a national system of innovations, the presence of large trusts blocked the access of native entrepreneurs to new technologies and better funding sources. It is for no other reason that Caio Prado was never tired of warning about the progressive nature of the denationalization process that was gaining momentum in the fifties.

Furthermore, contrary to what a superficial perception of the import substitution cycle might suggest, the author insists that the presence of large international trusts in strategic sectors of the industry did not represent an effective and permanent internalization of the country's technological capacity nor, consequently, an increase in the dynamic competitiveness of the productive park. This is because, as the foreign subsidiaries that moved to Brazil aimed solely and exclusively at controlling the domestic market, they had no reason to invest in the technological development of the Brazilian economy.

The inability to withstand foreign competition made the continuity of the industrialization process fully dependent on the preservation of the historical parameters that had allowed the isolation of the Brazilian economy from the competition of imported products and that had driven the internationalization of domestic markets. However, as it was obvious that the stability of the external parameters that had allowed for this situation could not last forever, Caio Prado never tired of warning that Brazilian industrialization was extremely vulnerable to crises of structural reversibility. “The unique role, unparalleled in the past, that the rapid and continuous transformations of technology play in modern manufacturing industry cannot be ignored. It is no longer just a matter of handling the industrial improvement as well as its promotion and expansion, as was the case a few decades ago. Technological progress and the continuous introduction of innovations represent in today’s manufacturing industry an essential and essential condition for its own subsistence, in particular in its basic and decisive branches such as the chemical industry, electronics and the like. The obsoletism that is proposed here at every moment, it can be said, is not only inconvenient or even intolerable in this case. It is simply impossible. To transform and progress continuously, or else perish, this is the only alternative that presents itself.”

Lastly, Caio Prado points out that the massive inflow of foreign capital to explore business opportunities generated by the expansion of the domestic market would intensify the structural imbalance in the balance of payments, since the internationalization of the economy not only implied greater remittances of profits and interest abroad, but also greater vulnerability of the external accounts to capital repatriation movements, especially when taking into account the greater spatial mobility of capital provided by Brazil’s close integration into the international financial market.

The fundamental point of Caio Prado’s argument is that the discrepancy between the wealth accumulated in the hands of international capital and the capacity to generate foreign exchange meant a strong increase in financial dependence and a quality change in the degree of exchange rate uncertainty in the Brazilian economy. This change entailed a reversal in the causal relationship between balance of payments constraint and import substitution. Because, from this moment on, the mere possibility of a shortage of foreign exchange would trigger defensive movements of capital flight that would paralyze the import substitution process. “Our financial relations with the international system of capitalism - and in this our current situation is distinguished from that of the past - are what rule the mechanism of the country's external accounts. It is not just the vicissitudes of Brazilian exports, as previously occurred, that determine the status of those accounts. It is also, above all and decisively, the flow of capital controlled from abroad and which in different forms (investments, financing, loans, amortizations, income, etc.) is oriented in function of the interests of international finance. Or because of political factors that are ultimately guided by those interests."

Even when acknowledging that the post-war industrialization boom implied a significant contraction in the import coefficient, Caio Prado warned that dependent industrialization would lead to the revitalization of the export sector's strategic position. Before handling this as a quantitative question related to the relative share of exports in Brazilian production, his analysis highlights the vital importance of the export sector in the capital accumulation process of large multinational companies, since, whenever there was a reversal in capital flows, the expansion of foreign sales would be the only means of transforming internally accumulated capital into international currency. The contraction of the domestic market and the revitalization of exports of products with low technological content, in which the country has absolute comparative advantages, would then emerge as the only means of enabling the transfer of real resources abroad and sanctioning commitments to the international community.

However, as the international division of labor no longer opened up enough space for a country the size of Brazil to have a volume of exports compatible with the payment of external commitments and the supply of an expanding internal market, the reconstruction of the old colonial system led, to a paroxysm, the opposition between the need to generate mega-transfers of resources abroad and the continuity of the process of formation of contemporary Brazil. "Here - says Caio Prado - the link between imperialism and our old colonial system based on the export of primary products is particularly clear, as it provides the resources that imperialism uses to achieve the profits that are its raison d'être. Considered from the general point of view of imperialism, the Brazilian economy engages in its system as a supplier of primary products, whose sale in international markets provides the profits of the trusts that dominate that system. The entire functioning of the Brazilian economy, that is, the country's economic activities and its future prospects, is thus ultimately subordinated to the commercial process whose core are the trusts today. Although in a more complex form, the Brazilian colonial system remains essentially the same as in the past, that is, an organization founded on the production of raw materials and foodstuffs demanded in international markets. This production and consequent export are what keeps the country going, as its resulting revenue allows for imports that are essential for our subsistence and for the costly services of the well-remunerated imperialist trusts installed in Brazil for the industrialization and economic development of the country."

The distortions in the commodification process caused by the modernization of consumption patterns, the suffocation of the native bourgeoisie by multinational companies, the lack of international competitiveness of the Brazilian industrial park and the increase in exchange rate uncertainty led Caio Prado to the conclusion that the commitment of the great trusts with the import substitution industrialization process was limited to the possibility of taking advantage of very defined business opportunities. As soon as such opportunities dissipated, the industrialization process would be subject not only to stagnation, due to the impossibility of the consumption capacity of Brazilian society to keep up with discontinuities at the minimum scale of the technological matrix, but even to structural reversibility, if international trusts decided to supply the domestic market using imports.

That is the reason why, long before all the processes responsible for the crisis of Brazilian industrialization had fully manifested, Caio Prado already foresaw its inexorable end: "Considering (...) the already extensive growing participation of these imperialist ventures in Brazilian industry that have key positions of decisive economic significance, it can be seen that the industrialization process is mere expression of the international sales policy of foreign organizations, which have their commanding centers completely beyond the reach of the Brazilian economy and its own interests. For us, it depends on the impulses and initiatives of these centers that the process of industrialization in Brazil is being developed and will continue to develop more and more, if the prevailing circumstances persist. It is not difficult to assess what this means in terms of the deformation of that process."

The assessment that the subordination of industrialization to the logic of international capital would entail a neocolonial reversal led Caio Prado to conjecture that, from the post-war period onwards, the contradiction between the imperialist system and the formation of the nation might have reached its critical point, maturing the objective and subjective conditions for the consummation of the Brazilian revolution. The extremely high instability of the Brazilian economy and its inadequacy to meet the needs of the people as a whole would, little by little, lead to a paroxysm of the feeling of revolt and dissatisfaction against the *status quo*, polarizing the class struggle between revolution and counter-revolution. The urgency of the Brazilian revolution comes from its perception that the inexorable disarticulation of industrialization would enormously aggravate the structural surplus of labor. Which, due to its sheer magnitude and high concentration in urban centers, would tend to make its subsequent integration into capitalist development increasingly difficult and traumatic, further aggravating the social crisis.

It is such a perspective of a situation marked by extreme economic instability and the progressive worsening of the social crisis that leads Caio Prado to affirm, in the mid-sixties, that Brazil was experiencing an unsustainable situation and needed deep changes. "Brazil is in one of these decisive moments in the evolution of human societies where the maladjustment of its basic institutions is particularly evident. Hence the tensions observed, so vividly manifested in widespread and deep discontent and dissatisfaction; amidst frictions and conflicts (...), which tear Brazilian life and weigh on it permanently and without appreciable prospects for an effective and permanent solution (...). Which ultimately leads, perhaps not yet foreseen in concrete terms, to this order mutating towards a relentless race to "every man to himself," where each party exclusively (and erroneously) takes care of themselves, their own interests and in their own benefit, in order to handle the occasional immediate opportunities at reach."

Until the early 1980s, the high dynamism and relative stability of the Brazilian economy gave the impression that Caio Prado's gloomy predictions would have been contradicted by the facts, since, even without having confronted the problem of the marginalized surplus overpopulation in the labor market led by multinational companies, Brazil was the scene of a vigorous movement of industrial expansion and diversification that allowed to internalize practically all the technology of the second industrial revolution, creating the illusion that our productive forces were rapidly converging with that of the more advanced capitalist countries.

However, when everything seemed to indicate that there was no unavoidable incompatibility between national dependence and development, disruptive processes began to surface. In a short time, the external debt crisis, the collapse of public finances, the disarticulation of the monetary system, the stagnation of growth, the unconditional submission to the dictates of the international financial community, the dismantling of the Brazilian government, the exacerbation of federative conflicts, the frightening increase in unemployment and underemployment, the progressive denationalization of the economy and the high vulnerability of the industrial park to the new pattern of international competition began to show the pertinence of his warnings. Brazil's total inability to react constructively to the profound changes brought about in the worldwide economic order by the globalization process leaves no room for doubt regarding the high vulnerability of Brazilian industrialization to the vicissitudes of international capital.

The problem is all the more serious because the growing denationalization of the economy and the extreme mobility of capital amplify the incompatibility between international capital and Brazilian industrialization, increasing the disproportion between the internal accumulation of profits by large multinational groups and the ability to generate foreign exchange for the Brazilian economy, as well as magnifying the vulnerability of the national production park to structural reversibility crises resulting from the displacement of productive units to other regions. The differences between the two movements in the internationalization of the domestic market are substantial. While the logic of conquest by the occupation of the national space prevailed, as it turned out, the dependent economies capable of boosting import substitution would enjoy a certain amount of stability, making industrial cycles have a certain durability. At the moment, conditions are different, as a logic of conquest by dilution in the global market prevails. Under these conditions, it seems reasonable to assume that growth cycles will be very brief, that economic instability will tend to infinity and that structural reversal crises will acquire cataclysmic proportions.

Therefore, even though the author has not adequately evaluated the propagation power of the technological standard that was being disseminated in the post-war period and the extended life span that external indebtedness would give to the industrialization cycle, mistakes that led him to underestimate the potential of the import substitution cycle, the essence of his interpretation - the idea that the "association" with international capital would undermine the process of formation of a national economic system, triggering a tendency to rebuild the old colonial system - must be reclaimed as a fundamental contribution to understanding the true character of Brazilian industrialization and the nature of the current crisis. As we will see below, Florestan Fernandes' interpretation of the Bourgeois Revolution will help us understand why, contrary to Caio Prado's catastrophic predictions, for a certain period it was possible to reconcile the dominant presence of international capital with relative economic and political stability; and, especially since that time has already passed, bringing the urgency of the Brazilian revolution back to the fore.

3. From permanent counterrevolution to neocolonial reversal

From Florestan Fernandes' perspective, the formation of Brazilian society is associated with the emergence and evolution of the modernization process as a way of life. Driven by dissatisfaction regarding the discrepancy between the ideal model of Western civilization and the actual form of its organization and functioning in Brazil, the process of formation is embodied in the need to build the economic, sociocultural, and political conditions that allow the society to control its destiny. The emergence of Brazil as a civilizing project thus involves the affirmation of the autonomy of the government within the world's capitalist system. Being an economy of colonial origin, the formation of the Brazilian society is seen as the product of three interdependent revolutionary cycles: national emancipation, which places the emerging nation on the scene as a national project; the bourgeois revolution, responsible for the expansion and consolidation of capitalism as the dominant mode of production; and, finally, the workers' revolution, whose historic task is to overcome bourgeois forms of oppression.

Within this perspective, the drama of Brazilian society is that the weakness of the process of differentiation of the class regime and its ultra-elitist character ended up compromising the effectiveness of class antagonisms as the driving force of the revolutionary processes that push the formation of the Brazilian civilization. The origin of the problem lies in the fact that social stratification took place in pre-capitalist or sub-capitalist modes of production and suffered the negative impact of the uneven and combined development of the world's capitalist system. Florestan Fernandes summarized the problem as follows: "We did not inherit the mortar for the construction of a *new society* from a feudal world in crisis. A rather crude starting point exposed bourgeois and proletarians to an endless struggle, rooted in colonial and modern slavery, in which they would engage before having their own identities, moved by the structures and dynamism of a mode of production that would grow and, little by little, impose the historical premises of its existence and development (i.e. the contract, civil society, the bourgeois state, etc.)."

A particularly adverse historical-structural context meant that opportunities to consolidate the nation emerged without the appearance of organized social forces capable and willing to turn them into reality. The absence of "bottom-up" nationalist and democratizing pressures and the extreme weakness of "top-down" reformist pressures did not force the ruling classes to broaden the material and political bases of their class power. Both national emancipation and the bourgeois revolution advanced along the path of least resistance as structural processes devoid of economic, social, political and cultural content that could compromise the foundations of dependent capitalism, reducing decolonization to the minimum necessary to meet the basic requirements of each historical situation.

For several reasons associated with the peculiarities of the formation of the proletariat as a social class and the backwardness of the Brazilian industrialization, the workers' revolution, which could determine new directions for the country, completing the tasks that were left aside by previous revolutionary cycles, took a long time to emerge from the underground of history. The proletariat only began to take shape as a social reality capable of influencing the course of events very late, at the end of the 1970s, after the leap to heavy industrialization. And, before it was able to fully constitute itself as a social class, it ended up being hit hard by the devastating impact of globalization on the world of work.

Within the reality common to dependent capitalist economies, Florestan Fernandes believes that the formation of Brazilian society stands out as an exemplary case in which nonconformist reactions against underdevelopment would have acquired sufficient vitality to generate a strong tendency towards autonomization, but not the vitality necessary for allowing the process of national integration to be carried to the end. For this reason, the contrasts between "backwards" and "modern" and the opposition between "heteronomous forces" and "autonomous forces" would have reached a paroxysm, highlighting the potential and limits of dependent capitalism as the mainstay of the civilizing process.

The specificity of the Brazilian case is attributed to the way in which the "conservative consolidation of bourgeois power" took place in the four decades that separated the crisis of the Old Republic and the affirmation of the autocratic bourgeois state in the second half of the 1960s. In this period, the Brazilian bourgeoisie would have gone through a true cultural revolution, stripping itself of the ideologies and utopias acquired from the classic models of bourgeois revolution and definitively purging the "bourgeois ethos" of its traditionalist second nature, inherited from the colonial era. When defining its strategic alliances, the decision of the bourgeoisie was realistic and pragmatic. Adapting its socioeconomic aspirations and political identifications to the needs of the historical moment, it found that, in the era of total imperialism, the conditions for making the transition to monopoly capitalism were too adverse to support nationalist and democratic adventures.

Unable to assimilate monopoly capitalism without establishing a close association with international capital and the imperialist system, the bourgeoisie threw all its energies into negotiating the terms of dependence. With nothing to offer the subordinate classes, the ruling classes abandoned any reformist pretensions and assumed, without hesitation, the defense of the only capital they had left: the almost unlimited capacity to adjust social and economic conditions to the demands of international capital. In other words, the possibility of delinking the acceleration of capitalist development from the national integration process led Brazilian bourgeoisies to opt for a strategic alliance with international capital and hegemonic nations, to the detriment of the formation of mechanisms of organic solidarity with the popular classes.

"The bourgeois strata – writes Florestan Fernandes – have learned to change the quality of their perceptions and explanations of the world, seeking to adjust to the 'pragmatic assessments,' which represent underdevelopment as a self-correcting 'natural fact' and establish as a basic ideal the principle of 'development with security' radiated from the United States. Thus, the last leap was taken in cleaning the attic. The Brazilian bourgeoisie found new links of 'modernization,' discarding its libertarian historical trinkets of European origin, replaced by much more prosaic convictions, but which adjusted their roles to the 'unity of the hemisphere,' to the 'interdependence of democratic nations' and to the 'defense of Western civilization.'"

The potential of monopoly capitalism in Brazil were consolidated in the fact that, despite the maintenance of the double articulation that perpetuated the nexus of external subordination and the asymmetry of colonial society, the country managed to complete the industrial revolution and carry out the bourgeois revolution. With the consolidation of the military regime in the second half of the 1960s, the bourgeoisie acquired the "power surplus" necessary to promote the necessary adjustments to internalize the fundamental structures and dynamisms of monopoly capitalism, integrating Brazil into the economic, sociocultural and political space of hegemonic capitalism.

The leap to heavy industrialization meant that, while the parameters that conditioned the internationalization movement of domestic markets remained unchanged, the expanded reproduction of capital would acquire an autonomous dynamic, becoming an effective mechanism for assimilating and diffusing structures and dynamisms of the Second Industrial Revolution. "A bourgeoisie that cannot trigger, in itself, neither the agricultural revolution, nor the urban-industrial revolution, nor the national revolution, nevertheless goes through *all* the stages of these processes *as if*, in reality, they were products of its historical activity. On the one hand, it gains resources to maintain and intensify the flow of growth of dependent capitalism, continually accelerated and sometimes subverted 'from the outside'. On the other hand, it can appear, in the internal panorama of 'national society,' as the supposed final protagonist of all transformations."

By unifying and centralizing state power under the leadership of modernizing groups, the consolidation of the bourgeois revolution allowed the Brazilian bourgeoisie to acquire strength and flexibility to adapt the economy and society to the demands of monopoly capitalism. "Coherent with its economic and political logic - writes Florestan Fernandes -, the bourgeois power made the private initiative and its system a true bastion, which protects and unites internal and external private interests (now associated with public power at the economic level as well). Thus, in the name of 'accelerated developmentalism,' the incorporation of the national economy and national structures of power into the world's capitalist economy and into the international capitalist structures of power was broadened and deepened."

Externally, the consolidation of the material and political bases of monopoly capitalism gave the Brazilian bourgeoisie the necessary bargaining power to negotiate, with the large transnational corporations and hegemonic nations, the pace and intensity of incorporation of the structures and dynamisms diffused by the hegemonic centers of the world's capitalist system. It was thus able to preserve control over the spatial and temporal matrix of the nation's economic space. In this way, the risk of a neocolonial reversal was avoided. In the words of Florestan Fernandes, "(...) the 'national' bourgeoisies of dependent and underdeveloped class societies do not cede to foreign actors all their political power and, especially, (...) they do not yield (to external domination and imperialization) the positions that are strategic for political control of dependent capitalist development. They accept and even encourage the articulation of internal and external bourgeois interests, which seem to recast bourgeois power at the economic level, thus increasing its flexibility and effectiveness as a source of dynamization of bourgeois domination in general."

Domestically, the unblocking of any kind of barrier to the empire of money allowed the bourgeoisie to assume without hesitation the role of champion of capitalist civilization. By abandoning the philosophy of "everything in due time," according to which the modernization process should be driven relatively spontaneously, the bourgeoisie assumed responsibility for the "acceleration of history," mobilizing all the energy of society towards enabling the expansion of monopoly capitalism. Since then, instead of forcing the more "modern" segments to cooperate with the "backward" segments, the opposite has happened: the accommodation of the "backward" groups to the demands of the "modern" groups. Brazil was definitively entering the era of "(...) 'extremist developmentalism,' the real monopoly capitalism´s infantile disorder in the periphery."

Despite the achievement of a certain degree of relative autonomy and the ability to bring high dynamism to the accumulation process, the development of monopoly capitalism in Brazil has proved to be completely incapable of transcending the *status quo*. On the one hand, the persistence of extra-economic blocks to the monopolization of capital and the perpetuation of mechanisms of primitive accumulation compromised the creative role of economic competition as a driving force for the introduction and diffusion of technical progress. For this reason, despite the intensification of heavy industrialization, capitalist development continued to be a process induced from the outside in, incompatible with the reproduction of mechanisms of organic solidarity between social classes. On the other hand, by making the political circuit hermetic to any type of contestation of order, the Brazilian bourgeoisie lost all its reformist potential. The national question and the democratic question were simply displaced from Brazil's political life. The first became the dilemma of preserving the freedom of action of the bourgeoisie and the second the challenge of ensuring the continuity of "order."

The need to compensate for the extreme pulverization of the ruling classes and to make up for their inability for collective action through a "tactical unity" for the self-defense of the order made the Brazilian bourgeoisie, at the time of rising to the top of the state apparatus and imposing its view of the country, to become intrinsically anti-national, anti-social and anti-democratic. Transformed into a mere instrument of control of society and the country's geographic space, the bourgeois state was irremediably committed to defending the petty and particularistic interests of Brazilian plutocracy. It is the affirmation of bourgeois power as a permanent counter-revolution that leads Florestan Fernandes to point out the need to overcome dependent capitalism as the only way to open up new perspectives for Brazil.

The "power surplus" derived from autocratic strength is not a circumstantial and secondary characteristic of the bourgeois state in Brazil, but an indispensable requirement for its own survival, in fact, the only means the bourgeois classes have to control the rhythms of dependent development. "Ultimately – says the author – 'freedom' and the 'capacity for rational action' of the dependent bourgeoisie end up residing in this autocratic model of the capitalist state. It gives bourgeois classes and class strata not only the foundations for the existence and persistence of bourgeois domination and power, after reaching a critical point for the survival of class society. But also, and more importantly, it gives them the political space they need to be able to intervene, in deliberate and organized manner, according to their relative potential, in the historical course of the Bourgeois Revolution, delaying or advancing certain rhythms, as well as splitting or separating, among themselves, their differentiated times (economic, social and political). Without the absolute control of power that the bourgeois classes can take from the constitution of this nation, it would be inconceivable to think how they managed to appropriate the enormous part that belongs to them in the national economic surplus with such security, or even how they managed to dissociate democracy, development and national revolution almost entirely at will."

According to Florestan Fernandes, the Brazilian bourgeoisie was only able to consolidate its pattern of domination and to acquire a minimum of control over dependent development due to a very particular historical situation, marked by the internationalization of the class struggle and the vigorous dynamism of the industrialization process. As long as such conditions remained, dependent capitalism would enjoy relative stability.

Externally, the bargaining power of the native bourgeoisie cannot be dissociated from the fact that international capital and the great hegemonic powers needed relatively strong partners in Brazil. The demands of the internationalization process of the internal markets of well-defined national economic spaces, protected from the risk of nationalist and redistributive pressures, and the need for zones of influence that would function as a protection belt against the threat of socialist revolutions, all of these factors created solidarity between the internal and external bourgeois interests in the consolidation of the bourgeois revolution in Brazil. Florestan summarized the issue as follows: "(...) the 'weakness' of the bourgeoisies subjected to and identified with imperialist domination is merely relative. The more the capitalist transformation deepens, the more central and hegemonic capitalist nations need 'solid partners' in the dependent and underdeveloped periphery – not just a bourgeoisie articulated internally on national bases, but a bourgeoisie strong enough to saturate all self-defensive and repressive political functions of bourgeois domination. This need becomes even more intense under total imperialism, inherent to monopoly capitalism, since after the Second World War, when entering an era of struggle for survival against socialist regimes, such nations came to depend on the national bourgeoisies of nations that are dependent and underdeveloped capitalists to preserve or consolidate capitalism on the periphery. The national bourgeoisies of these nations have thus become authentic 'internal borders' and true 'political vanguards' of the capitalist world (...)."

Domestically, the expressive growth of the economy worked as an important mechanism for the stability of order. By opening up ample possibilities for accommodating divergent economic interests, the rise in social surplus prevented the adjustment process between modern and backward sectors from provoking fratricidal disputes that could compromise the monolithism of the dominant classes. At the same time, the expansion of jobs linked to higher productivity activities created mechanisms of social mobility that functioned as an important way to legitimize this order with the popular classes. By feeding the myth of growth as a solution to the country's problems, high economic dynamism made it difficult to generalize the criticism of the ills of underdevelopment. In the author's words, "Economic growth, the rise in jobs, technological modernization, the progressive increase in income or consumption patterns etc. only become visible through internal symbols, further manipulated to obfuscate the critical consciousness of the oppressed classes and gain the adhesion of the middle classes. It (the consciousness of the oppressed classes) thus projects the bourgeois condition out of the bourgeoisie and implants, in the very heart of its class enemies, more or less deep identifications and loyalties towards consumerism, the competitive social order and the 'democratic' and 'national' state."

Although Florestan Fernandes did not have the opportunity to systematically study the impact of the new development phase of the capitalist system on Brazil, he did not miss the fact that globalization tends to undermine the external and internal supports of the autocratic bourgeois state, triggering a neocolonial reversal process. Because of this, he warned that the decision to sanction the tendencies emanating from the hegemonic centers, adjusting the economy and society to the imperatives of the great international financial capital and the whims of the international order imposed by the United States, would provoke disruptive processes that could compromise the future of Brazilian society.

When the perversity of subordinate insertion in the process of business globalization still eluded many people, Florestan Fernandes was already firmly denouncing the ultra-regressive nature and the plundering logic of the ongoing capitalist development. Comparing the modernization cycle driven by the liberalization of the economy with that driven by industrialization via import substitution, the author summarized the issue in the following terms: "The fourth modernization cycle is recent and tends to proliferate, due to the lack of autonomous capitalist mentality and civic responsibility of the ruling classes. The requirements of development premises are limited to core nations and their economic blocs. A double-faced modernization is unleashed: imported sophisticated products and the transfer out of speculative fortunes and economic goods. Unlike the previous cycle, there is no need to form a specific infrastructure. The reproduction of the production system is done abroad. The country becomes more peripheral, combines dependence with multiple neocolonial meshes, and succumbs to the claws of regressive impositions from which results the current postmodern condition. What would you expect from this type of devastating capitalist development?".

Two changes in the class regime are enough to characterize why, in Florestan Fernandes' view, the subordinate insertion in the process of economic globalization compromises the future of Brazil as a civilizing project. On the one hand, the new historical context dramatically reduces the relative autonomy of the Brazilian bourgeoisie, dangerously reducing its ability to defend the national economic space and negotiate the terms of its insertion in the economy. On the other hand, the disarticulation of import substitution industrialization breaks the mechanisms of social mobility, making the legitimacy of the bourgeois regime extremely problematic. Hence the forecast of a period of economic and political instability without precedent in the history of Brazil. "We find ourselves in a final cycle, not a starting point, although the end and the beginning appear to intertwine. This is the reflection that should guide the intellectual horizon of Brazilian workers and union members. Oppressed and marginalized from the decision-making centers of power, it is up to them to fight ardently to prevent the capitalist civilization of the tropics from reproducing itself indefinitely like the mallet that crushes the heads of the poor. (...) Until now, the bourgeois classes have dominated the transformations of society and civilization. Now the workers, supported by allied groups, need to recreate the world in their image. Or give in to the unprecedented barbarization of their social existence."

The breakdown of the bourgeoisie's bargaining power at the international level is essentially associated with two phenomena. First, the requirements to participate in globalization - full freedom of capital movement, indiscriminate liberalization of foreign trade, equal treatment of national and foreign capital, privatization of the economy, widespread deregulation of economic activity - leave the country completely vulnerable to demands and threats of the great international financial capital. Second, the collapse of the Soviet Union and the crisis of the socialist movement, by removing the immediate danger of alternative political projects that could question the absolute hegemony of capitalism and by opening up the space for the United States to give free rein to its imperial vocation, left peripheral economies to the discretion of an arbitrary and unilateral international order.

With no leeway to negotiate the terms of dependence, the Brazilian bourgeoisie is trampled by the transformations radiating from capitalist cores, which makes us question its very survival as a ruling class. As a result, a situation of great social instability and latent political crisis opens up.

On the one hand, the disarticulation of the national production system, the accelerated denationalization of the economy and the dismantling of internal decision-making centers threaten the position of the Brazilian bourgeoisie in society. The scale of the ongoing change can be assessed by the impressive speed with which the Brazilian bourgeoisie is being transformed from a privileged partner of monopoly capitalism into a mere commercial intermediary of the great financial capital that controls the globalization process. The distance between a dependent bourgeoisie and a "comprador" bourgeoisie can be objectively assessed - in terms of the degree of economic, social and political instability that the hegemony each represents for the country - by the distance that exists between a national economic space - the reference of action of the former – and a simple mercantile space – the reference of the latter. Lastly, the difference between the dependent bourgeoisie and the new buying bourgeoisie is evident in the abyss that exists between underdeveloped industrialization – the strategic objective of the former – and a simple trading post – the sole interest of the latter. The perception of this difference led Florestan Fernandes to write, in one of his last articles: “Globalization, for Brazil, has the meaning of an ultra-negative signal. A large part of our ruling classes will experience the hardships of the old “comprador” bourgeoisie. ‘Neoliberalism’ spreads myths inferior to those of ‘one world’ and the ‘alliance for progress.’ Thus, foolish formulas like the ‘Washington Consensus’ are preached. The technical gap that separates the automated and computerized economy from the production system set up under the designs of import substitution has such huge proportions that it is impossible to conceive of such an economic-technological leap outside the scope of the old excellent bargains.”

On the other hand, Florestan Fernandes denounces that the devastating effects of globalization on the world of work tend to turn the country into a true pressure cooker. The reversal of the tendency to reduce structural underemployment (which came together with the industrialization movement), the emergence of high rates of open unemployment - an unusual phenomenon in Brazilian modern history - and the accelerated precariousness of formal employment liquidate the only thread of hope that dependent capitalism gives the subaltern classes: the expectation of social mobility generated by economic growth. Globalization thus creates a paradoxical situation. While the labor pole helplessly watches the rapid weakening of its trade union and political organizations, the capital pole, which in the past has never distinguished itself for its capacity to feed its slaves, tends to face increasing difficulties to deceive them indefinitely. Hence the striking conclusion of Florestan Fernandes: “With the shift in the importance from work to technology and the quick increase in the surplus worker exclusion and pauperism, the composition of capital only leaves two options open – social revolution for the wage-earners, and a fascist-style autocracy for the manipulators of capital and giant corporations.”

4. The interrupted construction

Celso Furtado sees the economic formation of Brazil as the historical process of constitution of the technical bases, the social substrate, the spatial matrix, the “internal decision-making centers” and the ideological project that constitutes a national economic system. The axis of his interpretation is articulated around the contradictory relationship between the country’s peripheral position in the capitalist system and the advance of the industrialization process – the backbone of a national economic system. This contradiction is materialized in the impossibility of consolidating an internal market composed of the population as a whole, a problem associated with the lack of control over the “internal decision-making centers” and the reproduction of “structural heterogeneities" - be they productive, social and regional - that characterize the underdeveloped economies.

In Furtado's view, the difficulty in carrying out the transition from a colonial to a national economy stems from the fact that, as the ruptures with the colonial past and the capitalist center were never carried to the end, Brazil ended up tied to the webs of dependence. By subordinating the incorporation of technical progress to the logic of the process of modernization of consumption patterns – a model of capitalist development that places copying the lifestyle of core economies as the primary objective of society -, the ruling classes condemned society to underdevelopment. Even so, the country managed to bring the import substitution industrialization process to a paroxysm, pushing the contrast between the high level of development of its productive forces and the terrible living conditions of the people to the limit. "What must yet be noted – the author reminds us – is that the style of growth established in the previous phase by modernization imposed a certain standard of industrialization. To escape it, it would be necessary to correct the gap between the penetration of modern technology into lifestyle and production processes. More specifically, freezing important segments of the demand for final consumer goods and considerably intensify accumulation in the production system. That is, to set in motion a political process that, due to the magnitude of the interests it contradicts, only takes place in the context of a social upheaval. What was left, as an easy route, was to continue relying on modernization, therefore, reproducing underdevelopment."

Furtado's analysis of the historical evolution responsible for the crystallization of Brazil as a dependent, industrial and underdeveloped economy essentially highlights five aspects:

I. The very low economic level that served as the starting point of the young nation, a fact associated with the primitivism of the colonial economy, the ultra-elitism of a slave society, as well as the dispersion and isolation of the regions that make up a sparsely populated territory of continental dimensions;
II. The delay in the formation of the internal market and the emergence of "internal decision-making centers" capable of articulating a truly national economic policy (which is related to the slow pace of the political emancipation, the abolition of the slave regime, the generalization of free labor and the emergence of dominant elites capable of breaking with the dogmas of liberal thought);
III. The expansion of the relative backwardness of the Brazilian economy compared to the core economies at the time when the industrial

revolution was spread by the countries of Western Europe (a phenomenon attributed to the long discontinuity between the growth cycle of the economy of Minas Gerais - which declines in the last quarter of the 18th century - and the integration of the coffee economy into the international division of labor, which only gained momentum from 1870 onwards);

IV. The late outbreak of industrialization (a phenomenon related to the slowness with which the primary-export economy was definitively overcome, whose final crisis only came after the collapse of the international division of labor in 1929); and finally,

V. The subordination of import substitution industrialization to the logic of consumption patterns modernization (a fact conditioned by the way in which social surplus was used in the primary-export period and enshrined in the institutional reforms of the military regime, whose essence is to adjust this process to the requirements of transnational companies).

Even when deepening “structural heterogeneities” and exacerbating external dependence, Furtado believes that import substitution industrialization played an important role in the economic formation of Brazil, since the significant increase in social surplus and the internalization of the production goods industry allowed the economy to function as an organic system, giving it a surprising dynamism. By expanding employment opportunities in high-productivity activities, the expansion of productive forces contributes not only to making the political legitimacy of the Brazilian “model” viable, but also to crystallizing national unity itself. In fact, the rapid growth of the domestic market that resulted from it unleashed centripetal forces that were decisive in strengthening the economic ties between the different regions of the country and in allowing the full mobility of labor within the national territory.

In Furtado’s view, the disruptive effects of the transnationalization process of capitalism on the Brazilian economy radically modify the relationship between consumption patterns modernization and economic formation in Brazil. Interrupting a long cycle of expansion of the productive forces, the disarticulation of the import substitution industrialization, which advanced along the line of least resistance, anchored in the government, and driven by international capital, breaks the last link that supported nation-building. In *Brasil: A construção interrompida*, Furtado – a notorious moderate – paints the historic moment with dramatic colors: “In a half-millennium of history, starting from a constellation of trading posts, displaced indigenous populations, slaves transplanted from another continent, European and Asian adventurers in search of a better destiny, we arrived at a people of extraordinary cultural versatility, a country without parallel for its territorial vastness and linguistic and religious homogeneity. But we lack the experience of crucial tests, such as those that met other peoples whose survival came to be threatened. And we also lack a true knowledge of our possibilities, and especially of our weaknesses. But we are not ignorant of the fact that historical time is speeding up, and that time is counting against us. This is about knowing if we have a future as a nation that counts in the construction of the human destiny. Or will the forces that strive to interrupt our historic process of nation building prevail."

According to Furtado, the distinguishing feature of the emerging international order is the rupture of economic and political synergies that had given coherence to accumulation regimes anchored in national economic systems. The essence of the problem lies in the impotence of the nation to impose limits on the mobility of capital and to ensure a constructive relationship between capital accumulation and the relative scarcity of workforce. "With the advance of the internationalization of economic, financial and technological circuits – explains the author -, the national economic systems are weakened. Governmental activities tend to be limited to social and cultural areas. Countries marked by high cultural and economic heterogeneity will be subjected to increasing disarticulation pressures. The counterpart of the overwhelming internationalization is the loosening of the bonds of historical solidarity that unite, within the framework of certain nationalities, populations marked by heightened standard of living disparities."

The asymmetric impact of the transnationalization of capitalism on different regions of the globe tends to aggravate the gap that separates Core economies from peripheral economies. In the mid-seventies, long before the changes reached the dimensions known today, Furtado already warned of the dangers of the new order for Latin American countries. "The enormous concentration of power that characterizes the contemporary world - power that manifests itself in the form of national super-states and cyclopean transnational companies, each supported by immense financial resources, in the control of technique and information, and in instruments of intervention open or disguised at a global scale – places Latin America in a blatantly inferior position, given the backwardness that the region's economies have accumulated and the small dimensions of the national markets."

Much more than an increase in the peripheral economies´ backwardness in the incorporation of technical progress, for Furtado, the "new dependence" puts in check the ability of peripheral economies to subordinate the course of capitalist transformations to the designs of national society. As a result, the contradiction between dependence and national development becomes acute. "The atrophy of the command mechanisms of national economic systems – says the author – is nothing other than the prevalence of transnational decision structures aimed at the globalization of decision mechanisms. The biggest question that arises concerns the future of areas in which the process of nation-state building is interrupted precociously, that is, when the homogenization of productivity levels and production techniques that characterize developed regions has not yet taken place."

The external debt trap and the tight integration into the international monetary system reinforce the financial dependence of peripheral economies, leaving them dangerously vulnerable to pressures from the international financial community. By requiring a strong specialization of the economy in sectors where the country has comparative advantages, the adjustment policies imposed by international financial organizations lead to a hierarchical insertion in the international division of labor that undermines the position of the internal market as a dynamic center of the peripheral economy.

If this were not enough, the intensification of the process of diffusion of values from the capitalist Core intensifies cultural dependence. Advances in the areas of communications and transport lead to paroxysm the tendency of the more favored classes to copy the consumption patterns and lifestyles of developed economies. The sacralization of the market as an organizing principle of society paralyzes national decision-making centers, questioning the very notion of national economic space.

Furtado is not unaware of the fact that the continental dimension of the national territory, its immense population contingent, the presence of strong economic, social and regional heterogeneities, as well as the existence of an immense industry unable to keep up with the productivity rates of Core economies make the Brazilian economy particularly vulnerable to the disruptive effects of the emerging international order. "In a country still in formation, such as Brazil, the predominance of the logic of transnational companies in the ordering of economic activities will almost necessarily lead to interregional tensions, the increase of corporate rivalries and the formation of pockets of misery, all pointing to the unfeasibility of the country as a national project."

From Furtado's perspective, Brazil's high vulnerability to the new historical context is fundamentally due to the structural inability of the Brazilian industry to face international competition. Essentially aimed at serving an internal market that has an average income per inhabitant much lower than that existing in developed countries, the production park installed in the country, with few exceptions, is in no condition to take advantage of the external opening to increase the productivity of the production system as a whole through product diversification and increasing scales of production. Even if there were a willingness to modernize the production park, it would be totally unrealistic to imagine that the Brazilian industry could reach international standards of productivity, since, as state-of-the-art technology requires high capital-intensive investments, the saving effort required for the modernization of the economy as a whole would be far superior to the material possibilities of the country. And even if a spectacular increase in the savings rate were achieved, the Brazilian economy would not be able to keep up with the pace of the innovation process of the Core economies, because, given the brutal asymmetry in the level of per-capita income – at least five times lower to those existing in Core economies – there is an insurmountable disproportion in the volume of resources that these two types of society can allocate to research and technology.

As access to state-of-the-art technical progress cannot be generalized throughout the economic system, Furtado draws attention to the fact that a proactive policy to modernize the industry would only aggravate the heterogeneity of the productive structure. "Some industries – ponders Furtado – may present high physical and economic productivity, in line with international standards. However, as high productivity means strong investments per employed individual (...), the existence of cutting edge technology industries and international standards is offset by the presence of large segments of industrial activity placed well below these standards. In this way, there may be industries technologically equivalent to international competition, but the industrial system, as a whole, is not."

For Furtado, the impossibility of reconciling specialized insertion in the international division of labor and continuity of the industrialization process - an impossibility derived from the absolute lack of conditions to increase the dynamic competitiveness of the industrial system as a whole - means that the adjustment of the Brazilian economy to the impositions of the global order threatens the survival of the nationally articulated productive system. On the one hand, the elimination of capital goods industries – precisely those that present a greater degree of obsolescence compared to international standards – dismantles the strategic links that allowed the industry to function as the dynamic pole of the economy**.** On the other hand, by sanctioning the processes that lead to a hierarchical integration in the world's production system, adjusting to the requirements of transnational companies implies specialization of the Brazilian economy in sectors with low technological content, whose international competitiveness depends on the overexploitation of the workforce and degradation of the environment.

From Furtado's point of view, the disarticulation of the national economic system threatens nation-building because the damage to the internal market as a dynamic center of growth and the disarticulation of the industrialization process expose Brazil to centrifugal forces that tend to segment the national economic space between, on the on hand, regions that achieve a positive insertion in the international division of labor - true "islands of prosperity" that seek to increase their degree of autonomy – and on the other hand regions that, either by the disruption of their productive base or by their marginalization from international trade, tend to be disjointed in isolated areas, living restricted to themselves. The new historical context would thus undermine the economic and political dynamics that cemented national unity. On the one hand, predatory competition for attracting investments would stimulate tax wars between regions and encourage the emergence of autonomist dreams. On the other hand, the rupture of the mechanisms of social mobility that supported migratory currents would create an environment conducive to the emergence of active processes of social segregation. Comparing the current historical context with that of the period of import substitution industrialization, the author says: "The regionalization of political interests, which is manifested so strongly by all parties, was contained in the past, in its centrifugal effects, by the exercise of a regional hegemonic power, which was replaced by the interdependence of economic interests, which in turn emerged with the formation of a national system. Having access to a broader market or being able to move across borders in search of employment are factors that lent real content to the idea of national unity. But if the logic of interests is dynamited by international connections, and corporate interests organize themselves to hinder the mobility of labor, the bonds of solidarity between regions will necessarily have to weaken."

Furtado attributes the surprising immobility of Brazilian society in the face of the disruptive processes of globalization to the legacy of the military dictatorship. The problem lies in the perverse impact of the "Brazilian model" - whose essence is to subordinate the economic growth style to the requirements of transnational companies - on internal decision-making centers and on the economy's social substrate. His analysis highlights the particularly negative impact of the government's loss of control over the mechanisms for appropriating and using the social surplus, related to the financing pattern instituted soon after the military coup to enable the "economic miracle," strengthened in the second half of the seventies by the megalomaniac voluntarism of the II PND and exhausted in the eighties with the external debt crisis.

By stimulating an uncontrolled process of external and internal indebtedness that would ultimately cause a vigorous inflation spiral, the growing internationalization of the Brazilian monetary-financial system and the extreme precariousness of public and private financing mechanisms caused irreversible wear of the "means of action" and a progressive loss of state autonomy in face of internal and external economic groups. Discussing the nature of the recent inflationary crisis, Furtado did not get lost in instrumental aspects: "No one ignores that inflation is a simple symptom, the external manifestation of disarticulation, maladjustment or lack of control in an economy. But an inflation of the magnitude we see here is an unmistakable symptom of complete misgovernance. This misgovernance must be corrected, and it cannot be explained without alluding to the complete erosion of the instruments of economic policy. The responsible authorities no longer have the means to apply a monetary policy, control liquidity, discipline the cost of money, supervise financial institutions, define an exchange rate policy, etc, etc. An excessive financial opening was allowed, which considerably restricted the decision-making autonomy of Brazilian authorities. And, as these became immobilized, a favorable climate for all forms of adventurism was established."

The exponential growth of external debt, without a proportional increase in the ability to transfer real resources abroad as a counterpart, meant that the country's future was being mortgaged. The paralysis of the "internal decision-making centers" after the balance of payments crisis generated by the interruption of private international bank loan in the early eighties foreshadowed that the mortgage would be charged in the worst way. That is so because of the lack of instruments and direction to formulate economic policy left the country at the mercy of the international financial community**.** Writing in the early 1980s, the author notes what was at stake: "Brazil is currently experiencing a phase of its history like that of the 1890s when, under the pressure of external financial imbalances, it renounced having an industrialization policy and accommodated itself in the situation of an economy exporting primary products and importing manufactures. As a result, forty years were lost and the physionomy of the country was inexorably marked."

The inability to reverse the immobility of economic policy in the New Republic (after 1985) and the capitulation to the determinations of the Washington Consensus in the 1990s cannot be dissociated from the serious consequences of the "Brazilian model" on social structures. The crucial change is the extraordinary strengthening of middle- and upper-class strata, which deepened cultural mimicry, making the reversibility of the modernization process much more difficult without traumatic disruptions for society. If this were not enough, the denationalization of the Brazilian economy and its greater integration into the world economy have generated bonds of solidarity with the international financial community that are incompatible with the articulation of a national strategy to face globalization. The author makes a grim assessment of the authoritarian period: "For many years we were victims of markedly antisocial policies, which contributed to aggravate malformations coming from the past. Social inequalities deepened, the numbers of the excluded population grew at the same time that the middle class was installed in the illusion of unlimited prosperity. Now we discover that we were also victims of a series of deceptions, that the country was mortgaged to foreign bankers, and that agreements were signed with international financial institutions that imply derogations from our sovereignty."

Before Brazilian society had the opportunity to recover from the long authoritarian nightmare and the setbacks of the atrabilious Collor de Mello, the reintegration of Brazil into international capital flows, by enabling the stabilization of inflation and the accelerated liberalization of the economy, gave impetus to the adjustment advocated by the international community, paving the way for a new round of modernization of consumption patterns. Concerned about the deleterious effects of the strengthening of the "Brazilian model" in the early 1990s, Furtado emphatically warned that adhering to the lifestyles of the global era would exacerbate the drawbacks of underdevelopment, making Brazil's future very uncertain. The absolute impossibility of reconciling the modernization of consumption patterns and underdeveloped industrialization left the Brazilian people at a dangerous historical crossroads. "According to the logic of the emerging international economic order – the author wrote – the economic growth rate that corresponds to Brazil seems to be relatively modest. Thus, the process of formation of an economic system no longer fits naturally into our national destiny. The challenge facing the present generation is, therefore, twofold: to reform the anachronistic structures that weigh on society and limit its stability, and to resist the forces that operate to dismantle our economic system, threatening national unity."

But there was no change of trajectory. By intensifying the subordinate adaptation of the Brazilian economy to the trends of the globalization process, the modernist-conservative coalition led by Fernando Henrique Cardoso is turning into reality Furtado's terrible prediction: "The offensive that aims to vaccinate the new generation against all social thinking not inspired by market logic – and thus devoid of historical vision – has already convinced the vast majority of the naïveté of any attempt at resistance. With the construction of a national economic system interrupted, the role of the current leaders would be that of liquidators of the development project that cemented the country's unity and opened up a great historical option for us."

5. A plan for Brazil

The analyzed interpretations converge to the idea that the process of formation of Brazil is in a dangerous impasse. The perspective that continued external dependence is causing a dangerous neocolonial reversal is all the more serious in that it is perfectly consistent with what is observed in the daily life of society. Refusing the conformism of those who think that Brazil has no choice but to docilely accept the spontaneous tendencies of the world's capitalist system, as well as the escapism of those who refuse to think of alternatives that transcend the milestones of the *status quo*, the reflections of Caio Prado, Florestan Fernandes and Celso Furtado indicate an urgent need to break with the current situation.

The availability of new historical horizons requires the overcoming of the three main ills of Brazilian society: (i) the dependent character of its economic system - a form of organization of material life that leaves the country subject to the vicissitudes of international finance; (ii) the extremely asymmetrical nature of social structures – a pattern of social stratification that creates a chasm among Brazilians; and (iii) the heavy burden of cultural colonialism that prevents the generalization of the benefits of civilization to all people – a narrow worldview, which makes copying the lifestyles of Core economies the absolute priority to guide the organization of the economy and of society.

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CHAPTER 16

REAL PLAN: from success to impasses

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The assumptions of the Real Plan and the nature of the new foreign financing

In its essential conception, the Real Plan followed the basic method used to end most of the "great inflations" of the twentieth century: recovery of confidence in the national currency by guaranteeing its external value. The "anchor" was, as widely recognized, the stabilization of the nominal exchange rate, guaranteed by financing in foreign currency and/or by an amount of reserves capable of discouraging speculation against the chosen parity. It is necessary to consider three prerequisites to understand how the "disinflation" of the Real Plan took place rapidly.

The first concerns the fiscal and indebtedness situation of the public sector. It is true that the fiscal issue was the first concern in the formulation of the Plan announced in late 1993, corresponding to the first phase of its implementation, although the initiatives taken did not represent an in-depth adjustment of the public sector. The main initiative was the creation of the Emergency Social Fund (later the Fiscal Stabilization Fund) allowing 20% of budget revenues to be decoupled from expenses. The fact, however, is that in this matter the Plan was not based on the initiatives of its first phase, but on the legacy of the previous period. As is well known, some of the results of the Collor Plan had transitory significance, including those that turned the 1989 large fiscal deficit into a surplus the following year, and those that allowed for a substantial reduction in the public sector debt. In fact, the 1990 numbers were surpassed in the subsequent years because the accumulation of foreign reserves that took place since then required the issuance of new public sector debt, in addition to the attractiveness of the high domestic interest rate to encourage the inflow of foreign capital, which resulted in a higher interest burden.

But it can be said that the financial situation of the Brazilian public sector was enviable when the Real Plan was launched, an advantage that none of the previous plans could aspire. The Real Plan fiscal and public indebtedness adjustment was made earlier. In 1993, government accounts registered a primary and operational fiscal surplus, and total net and securities debt had never been so low. In the five years that have elapsed since the announcement of the Plan first stage, the economic policy firstly threw away this trump card and then pushed the situation of public accounts to the limit of the unsustainable. There was no concern about coordinating macroeconomic policies in order to protect public finances, much less serious and systematic initiatives for reorganizing government accounts.

In March 1994, the economic team created a new account unit, the URV (the "real value unit," adjusted daily according to an average of three inflation indices), to which wages (wages were compulsorily converted by the average of the last 4 months), prices, contracts and also the exchange rate converted to. This strategy played a role in coordinating expectations, guaranteed information for price setters and created conditions for the "conversion" of contracts, thus eliminating the "causes" of inflation indexing, already at the time the monetary reform was carried out. The 3rd phase of the plan was implemented in July 1994 with the conversion of the old currency and URV values to the new currency unit, the Real.

The Real Plan success was sustained by the intensive use of the "exchange rate anchor." It is necessary to clarify that Brazil – accompanied by other Latin American countries – went from being a "saver", predominantly in the 1980s, to a recipient of financial resources. This was possible thanks to the deflation of real estate and financial wealth observed at the end of 1989 in globalized markets. The American recession, which lasted until mid-1992, and the "burst" of the Japanese speculative bubble were factors that required a great laxity of monetary policies in order to ease the correction of imbalances in the balance sheets of companies, banks and households, hit by the collapse of the exuberant upsurge in asset appreciation that followed the 1987 rescue intervention.

The almost depressive state of the quality asset markets and the situation of excess liquidity, caused by a prolonged period of very low interest rates, combined with a scenario, in Latin American "emerging markets," of depreciated equities, and heavily indebted governments, owners of public companies that could be privatized across various sectors of the economy, in addition to the prospects of exchange rate appreciation and the maintenance of high real interest rates, in a stronger currency, even after stabilization.

Brazil was not alien to these processes and, before experiencing a phase of monetary stability with the Real Plan (and even before solving the political crisis of the Collor Government, suspending the foreign debt moratorium and renegotiating its "old" debt), it managed to triple its foreign exchange reserves in just 2 years. These reserves, held at around US$ 8 billion between 1989 and 1991, reached US$ 19 billion in 1992 and exceeded US$ 25 billion in late 1993, when the Real Plan was announced. At the time of the monetary reform, reserves were already above US$ 40 billion, a level corresponding to 18 months of imports and more than enough to support the exchange rate fixation as an instrument of the stabilization policy. By the way, from then on, until the 1998/1999 crisis, reserves would reach almost double this last value, sustaining and renewing the bet on the exchange rate anchor.

The conditions of the Brazilian external sector could also be considered enviable at the time of the Plan: a trade surplus of US$13.3 billion and a deficit of only US$592 million in the current account.

It is necessary to bear in mind the nature of the "new" external financing that supported the Real. The peripheral countries, including Brazil, until then subjected to the adjustment conditions imposed by the debt crisis, were literally captured by the globalization process, carrying out their stabilization programs in accordance with the rules of the liberalized financial markets. The basic rule of stabilization with financial opening is to create attractive financial assets that can be embraced by the general movement of globalization. This list includes public debt securities, generally short-termed and highly liquid; shares of companies in the process of privatization; bonds and commercial papers from reputable companies and banks; and later, depreciated equity of private companies, especially those most affected by economic opening, currency appreciation and high interest rates.

Given the inherent weakness of newly stabilized currencies, these assets needed to promise high capital gains and/or carry high risk premiums into their rates of return. This creates a situation in which rapid disinflation is accompanied by a much slower fall in nominal interest rates. Real rates cannot be reduced below certain limits established by the **spreads** required by foreign investors to acquire and hold an asset denominated in a weak currency, artificially overvalued.

External Sector - Amounts in US$ Million

	1992	1993	1994	1995	1996	1997	1998	1999	2000
Exports	35,793	38,563	43,545	46,506	47,747	52,994	51,140	48,011	55,086
Imports	20,554	25,256	33,079	49,858	53,346	59,742	57,743	49,272	55,783
Trade balance	15,239	13,07	10,466	(3,352)	(5,599)	(6,748)	(6,604)	(1,260)	(698)
Fees	(7,253)	(8,280)	(6,338)	(8,158)	(9,173)	(10,388)	(11,947)	(15,237)	(15,088)
Profits and dividends	(574)	(1,831)	(2,483)	(2,590)	(2,374)	(5,597)	(7,181)	(4,099)	(3,589)
Internal travel	(319)	(799)	(1,181)	(2,419)	(3,598)	(4,377)	(4,146)	(1,457)	(2,086)
Freight	(1,417)	(2,136)	(2,573)	(3,133)	(2,780)	(3,431)	(3,180)	(3,199)	(3,312)
Transfer Balance Chains	6,143	(592)	(1,689)	(17,972)	(23,142)	(30,791)	(33,445)	(25,396)	(24,595)
In % of GDP	1,5	(0,1)	(0,3)	(2,5)	(3,1)	(3,8)	(4,2)	(4,8)	(4,2)
Budget Internal Reserves	19,008	25,878	36,471	50,449	59,039	51,359	43,617	35,554	32,949
Total External Debt	135,949	145,726	148,295	159,256	179,935	199,998	241,644	241,468	232,290
Foreign Direct Investment	954	954	2,356	4,778	9,580	17,864	26,515	26,903	31,521

Obs.: The external debt position is for the month of December, except for 2000, referring to the month of September.

Source: Bacen.

In big investors' portfolios in globalized markets, the assets offered by economies with turbulent monetary histories are naturally the riskiest ones and, therefore, those that are prime candidates for liquidation in case of changes in the financial cycle. Regardless of what may happen with the financial cycle, emerging markets are also generally more subject to changes in conventional market opinion as to the sustainability of their respective exchange rate regimes. This means that their stabilization processes are undoubtedly vulnerable, in direct proportion to the degree of dependence on the inflow of foreign resources (current account deficit), and are also subject to problems of dynamic inconsistency, as we shall see below. The stabilization achieved under these conditions is placed under permanent threat.

Foreign exchange anchor, price stability and the new growth model

The Real Plan seemed to move towards fixing the exchange rate, with full convertibility to current and capital accounts, in line with the following assumptions:

a) historical experience demonstrates that the fixed rate regime is a decisive instrument in hyperinflation stabilization.
b) certainly, fixed rate advocates imagined that the new liquidity conditions for emerging countries would last; thus, imbalances in the current account could be, at first, offset by capital inflows, given the interest rate differentials.
c) the hard and relentless commitment to a fixed rate and the advance of trade opening would allow the operation of "the law of one price," progressively reducing the differentials of inflation and interest rates between the country and the rest of the world, making the expectations of domestic assets appreciation increasingly important as a way of attracting foreign capital.

In this view, the "disappearance" of the exchange rate devaluation risk would increase the degree of substitution between domestic and foreign assets. In other words, the drastic reduction of exchange risk would determine a greater integration between the national financial market and the international market, improving, in the foreign investors' view, the quality of our reproductive assets and the debt securities issued to hold them. In this case, within a reasonable period, new investments and the improvement in efficiency imposed by foreign competition would lead to a recovery in the trade balance and a reduction in the deficit in the current account.

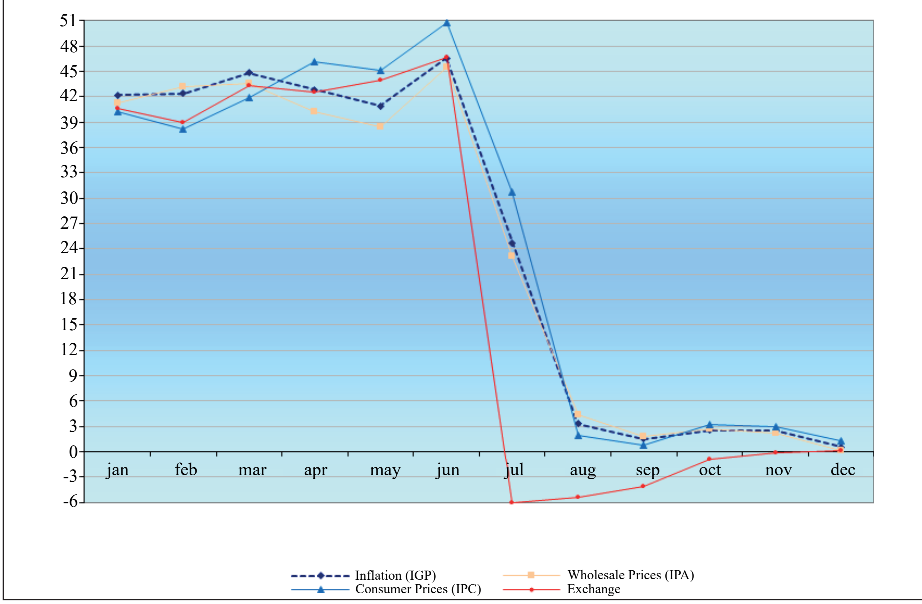
This regime would require the immobilization of monetary policy, as the liquidity conditions of the economy should be determined by fluctuations in foreign exchange reserves that would "cover" the stock of liquid domestic assets. This choice implied the acceptance of the risk of recessive adjustments and price deflation when the liquidity conditions of the foreign financial markets change or when there is a deterioration in the terms of trade.

Those responsible for the Brazilian stabilization program chose, however, a limited convertibility regime, with semi-fixed rates. In this case, and in an international environment where the free movement of capital prevails, the interest rate must necessarily converge more slowly towards international levels, since it must incorporate, in addition to country risk, the expectation of exchange devaluation.

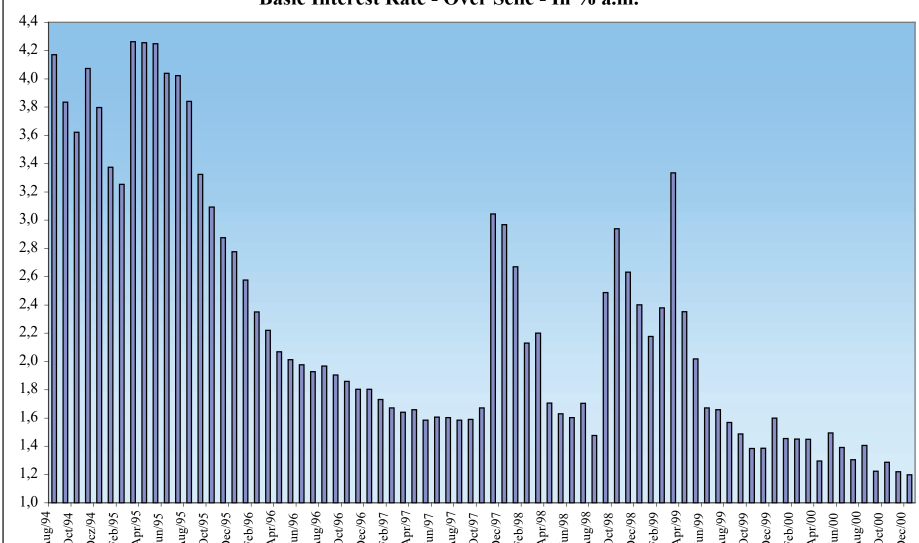
In the program first months, the authorities allowed a strong appreciation of the nominal exchange rate, aiming at a faster convergence between the domestic inflation rate and the one prevailing in the United States, which in fact occurred. After an inflationary acceleration caused by the "race" of readjustments before the previously announced conversion to the new currency, in July 1994, inflation plummeted, reaching in December less than 1% in the general price index.

However, the same exchange rate appreciation that supported the rapid disinflation increased the component that, in the formation of interest rates, is correlated with the expectation of exchange devaluation. The government sought to regulate this expectation by defining a policy of gradual adjustment of the exchange rate, which ended up consolidating, in the interest rate formation, a projected exchange devaluation of approximate 7% per year. Therefore, given the "model" of economic policy adopted, the basic interest rate in the Brazilian economy started having a floor that resulted from the aggregation of the exchange risk component, plus the international interest rate (such as the US rate, around the 6%), and the spread of loans to borrowers in the country, reflecting the "Brazil risk" (around 5% in normal times), in addition to taxes, which totaled something like 22% per year.

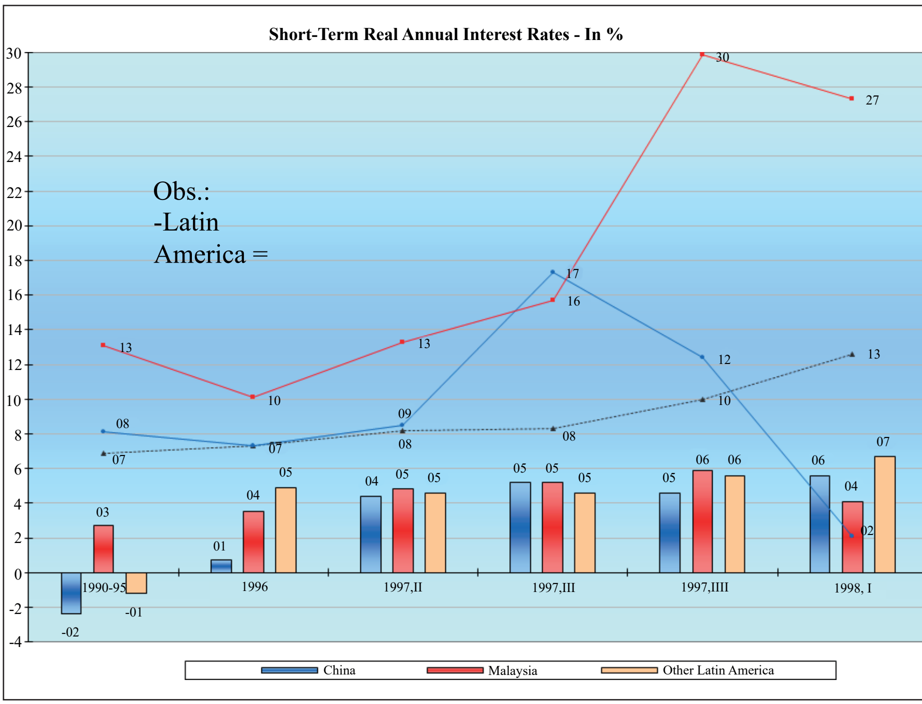
Monthly Price and Exchange Variation - 1994 - In %



Basic Interest Rate - Over Selic - In % a.m.



Higher interest rates were also used at the start of the program to keep the financial "savings" level, discouraging the demand for credit by households and businesses. Sharp rises in interest rates were employed to contain capital flight in the face of foreign crises with potential effects on the country, such as the crises in Mexico in 1995, Asia in 1997 and Russia in 1998, and to combat speculative attacks against the national currency, as notably occurred in late 1998 and early 1999. What we cannot forget about the facts that influenced interest rates in Brazil at the time is that rapid disinflation, strong and abrupt currency overvaluation and very high interest rates were all components of the same economic policy strategy. Therefore, it is not surprising that Brazil had, in the period, the highest real interest rates among "emerging economies" and by world standards.



With the execution of the Real Plan, Brazil was, in effect, abandoning the rules of a non-convertible fiat money regime and a real exchange rate set by the Central Bank. These seemed to be appropriate rules for a peripheral economy endowed with a high degree of industrialization, sustained for decades by very high levels of protection. The Real Plan, observed from this angle, would have been an attempt to place the Brazilian economy under the discipline imposed, first by a regime of restricted financial and commercial convertibility, and then, probably, to advance along the path of full convertibility. Therefore, it was not just a matter of achieving price stability through the classic use of the exchange rate "anchor." The objective seemed to be broader: we were facing a neoliberal development project that supposes the relatively rapid convergence of the productive structure and productivity of the Brazilian economy towards the "competitive" and "modern" patterns of the advanced economies.

Such a development strategy, generally associated with the recommendations of the Washington Consensus and adopted by Latin American governments, is supported by four assumptions:

a) price stability creates conditions for long-term economic calculation, stimulating private investment;
b) trade opening (and exchange rate appreciation) imposes competitive discipline on domestic producers, forcing them to achieve substantial productivity gains;
c) privatization and foreign investment would remove supply bottlenecks in manufacturing industry and infrastructure, reducing costs and improving efficiency;
d) exchange liberalization, combined with predictability as to the evolution of the real exchange rate, would attract foreign savings on a sufficient scale to complement the domestic investment effort and finance the current account deficit.

Suddenly, the Brazilian economy – inspired by this idea – was faced with the following reality, unprecedented in the post-war period: a drastic reduction in the effective protection caused by the drop in tariffs combined with a strong exchange rate overvaluation and a very high real interest rate. Given these conditions, there were those who risked predicting a recessionary trajectory for the economy in the Plan early days. This has not happened.

First, the fall in the inflation tax has increased the purchasing power of salaried employees. Given the low level of pre-existing indebtedness, both for households and companies, the rapid rehabilitation of credit – despite strong credit restraint initiatives and very high interest rates – caused a jump in aggregate demand, which was also favored by the real decline of prices of some industrial segments. In addition, and despite the government's containment initiatives, the fall in nominal interest rates and the end of inflation indexing caused reallocation, at the margin, of private wealth to the detriment of "defensive" financial investments and in favor of durable goods consumption and real assets ownership.

These factors promptly boosted nominal demand with no effect on the prices of tradable goods. The residual inflation in the period of "demand pressure" basically survived due to the prices of services. On the other hand, it was foreseeable that this "leap" in consumption and current production – in a situation of overvalued real exchange rate – would gain sufficient intensity to reduce the trade balance and bring up deficits in the current account. The intensity of changes in the balance of payments at a time when the economy was already sluggish was not so predictable. In fact, 1995 is a milestone for the country's balance of payments, given the magnitude of the changes that took place: the trade surplus of US$ 10.5 billion in 1994 gave way to a deficit of US$ 3.3 billion, and the result in the current account came from a deficit of US$1.7 billion (0.3% of GDP) to US$18 billion (2.5% of GDP). As it is worth repeating, these changes occurred in the absence of an explosion in economic growth (growth in 1995 was 4.2%), which is to say that the results mainly reflect the orientation of economic policy.

Had economic policy not been so rigidly tied to a certain set of conduct and a certain concept of development, it would have taken advantage of the relative "calm" of the international financial markets after the Mexican crisis (since mid-1995, throughout 1996) to reverse exchange and interest rate policies. This would make room for the balance of payments deficits to accommodate a greater economic growth and contain fiscal maladjustment and public debt growth. The indication then would be implementation of structural policies aimed at equalizing the conditions of foreign and domestic competition through fiscal reform, reduction of interest rates and adoption of technical controls and surveillance of imports prices, in addition to policies aimed at boosting industrial segments such as capital goods and industries with a greater trade deficit, also encouraging exports. The economic policy followed its guideline instead, redoubling the bet on the exchange-interest combination, enabling at most a gradual exchange rate adjustment in an implicit recognition of its overvaluation, but at the expense of maintaining very high interest rates and public and balance of payments deficits growth.

It should be noted that, due to the continued economic orientation, "negative" forces were activated, emanating from the deepening of trade liberalization, exchange rate overvaluation and high real interest rates. These forces had a perverse effect on the use-cost ofexisting capital, disfavoring the use of fixed capital for exports, and inciting defensive "rationalization," with cost cuts for companies, which promoted a permanent reduction in jobs in industries subject to competition with foreign producers.

Exchange and interest policy inconsistence, political cycle and external crises

The combination of an overvalued exchange rate and high interest rates, kept by all means, launched the Brazilian economy on a path of mediocre growth. Low growth would still suffer strong fluctuations caused either by the political cycle or by a succession of crises that befell the "emerging" economies. The great increase in unemployment had these characteristics of recent growth as its main determinants.

The Real Plan exchange rate and monetary regime caused the disruption of production chains in various branches of the manufacturing industry, especially in the areas of metalworking (mainly auto parts and capital goods), electro-electronics and chemicals. The loss of linkages in these chains meant the reduction of added value to the same gross production value, which, in practice, represents the elimination of income and employment generation points. Second, the composition between exchange and interest rates negatively affected the sectoral distribution of investment, as it punished the installation of new productive capacity for tradable goods. Data on foreign direct investment show an unsurprising concentration in the most "protected" sectors, particularly in services and areas undergoing privatization. The recent cycle of foreign direct investment has been characterized by a high propensity to import and a low propensity to export.

Finally, this stabilization model was accompanied by a very rapid growth of foreignliabilities, in addition to domestic ones. But unlike the indebtedness process of the 1960s and 1970s that financed, directly and indirectly, projects aimed at substituting imports and/or stimulating exports, the new stage of **dependence** on foreign financing considerably increased the vulnerability of the Brazilian economy to an external shock.

It is necessary to underline the meaning of the abusive use of the exchange rate anchor and high interest rates after the monetary reform that introduced the Real. First, from the current and balance sheet points of view, it determined a transfer of income and wealth in favor of importers, producers of non-tradeable goods and rentiers. The measure of this transfer can be evaluated by variations in the exchange rate and basic interest rate accumulated between July 1994, when the Real was introduced, and December 1998. The exchange rate varied 21% while accrued interest rates totaled 306% against total inflation (measured by the IGP-DI) of 89%. Inflation was lead, as we have already observed, by the rise in the service prices.

By importers we must understand not only those segments directly dedicated to this activity, but all segments that in the Real Plan cycle benefited from subsidized imports, including companies, by importing inputs and capital goods.

As a result, companies, especially national ones, were able to partially compensate for the adverse domestic conditions (in relation to international standards) determined by the levels of interest rates, taxes, and the exchange rate itself. The benefit was extended to middle and high-income consumers, through imports of consumer goods and access to services abroad (such as tourism), which contributed, at first, to expanding the range of support to the Real Plan beyond that segment initially benefited by stabilization: the low-income and low-wage workers.

The transfer of income and wealth took place against the mass of wages, which, due to the increase in unemployment, grew less than inflation in the period, against tradeable goods producers because of the overvalued exchange rate, and against a wide range of debtors forced to contract debts at very high interest rates.

Among these, it is worth highlighting the companies, and among these, again, the national ones, led to bank indebtedness in national currency, especially to finance their turnover operations, and the public sector, which is led to bear the interest rates of its growing domestic indebtedness. As the imbalances caused by the economic policy of the Real Plan worsened, the federal public sector was also forced to absorb debts and mismatches from other private sector agents, but also from public agents at other levels of government. These are the cases of the rescue of banks that had been shut down in the 1995 banking crisis, through a rescue program (PROER); federalization (for later privatization) of state banks; refinancing of the states' debts, and the partial absorption of private foreign debt through the issuance of public debt bonds with an exchange rate adjustment clause. This segment of debtors, comprising mainly the federal public sector and segments of national private companies, was the one who supported the transfer of wealth accumulated by rentiers.

From the point of view of the investment and production structure, the combination of interest-exchange rates of the Real Plan discouraged projects aimed at exports, promoted the "shrinkage" of production chains – affected by "predatory" imports – and increased the share of foreign ownership in the domestic capital stock. The above factors concurred to inhibit exports and favored imports, spending on international travels and increased remittances of profits and dividends abroad.

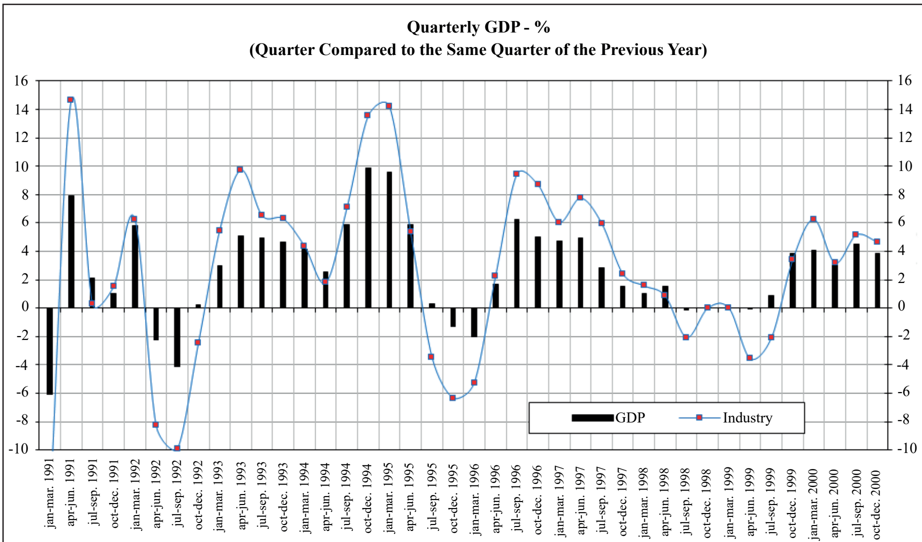
In short, the economic policy of the Real Plan redistributed unfavorably income and wealth against the agents that command investment and spending (the exception is due to the primary effect of stabilization on low incomes and wages, which, together with the recomposition of credit, constituted the most powerful growth inductor in the period) and inhibited productive accumulation and production for exports.

It also determined a structural worsening of the external imbalance, whose medium and long-term consequences on the balance of payments were systematically ignored by the government and its supporters. Both preferred to believe that the international scenario would induce greater productivity in domestic sectors because of foreign competition, penetration of foreign capital in more diversified segments, convergence of domestic interest rates to international standards and, finally, gradual exchange rate devaluation policy which would offset the exchange rate overvaluation during the Real Plan "rapid disinflation." These productivity gains would supposedly serve not only to support the deceleration of the external imbalance – which, moreover, could be easily financed by foreign loan flows, counting on the reinforcement of the wide privatization drive as in fact was undertaken – but also would lay the foundations for long-term development.

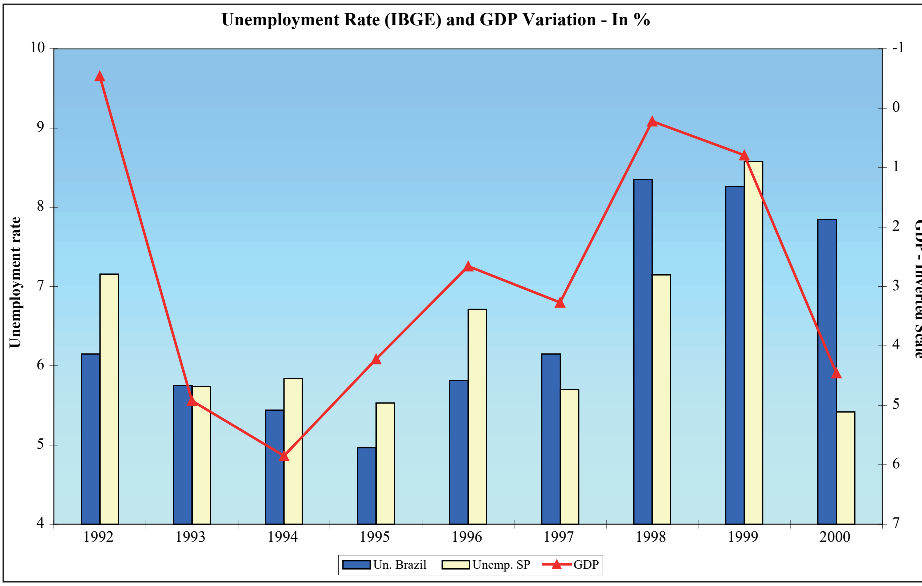
Real GDP Variation - %

	GDP	Industry	Services	Agropec.
1990	(5.1)	(8.7)	(1.2)	(2.8)
1991	1.3	0.3	0.3	1.4
1992	(0.3)	(4.2)	0.3	4.9
1993	4.9	7.0	1.8	(0.1)
1994	5.6	6.7	1.8	5.5
1995	3.4	1.9	1.3	4.1
1996	2.7	3.3	2.3	3.1
1997	3.4	5.8	2.6	(0.2)
1998	(0.1)	(1.3)	0.8	-
1999	0.8	(1.6)	1.9	7.4
2000	4.2	4.8	3.6	2.9

Source: IBGE.



Source: IBGE.



Variation in Price Indexes, Exchange Rate, Wage Mass and Interest Rate -In %

	Inflation (IGP)	Wholesale Prices (IPA)	Consumer Prices (IPC)	Wage-FIESP	Exchange rate	Interest rate[1]
1994, jul	24.7	23.1	30.8	0.3	-6.0	6.9
aug	3.3	4.4	2.0	3.6	-5.4	4.2
sep	1.6	1.8	0.8	1.9	-4.0	3.8
oct	2.6	2.7	3.2	4.7	-0.8	3.6
nov	2.5	2.2	3.0	12.4	-0.1	4.1
dec	0.6	0.2	1.3	3.6	0.1	3.8
jul/dec/94	**38.3**	**37.5**	**44.6**	**29.1**	**-15.4**	**29.4**
1995, jan	1.4	0.9	0.8	-2.2	-0.5	3.4
feb	1.2	0.6	1.3	0.5	1.2	3.3
mar	1.8	1.1	1.9	5.6	5.2	4.3
apr	2.3	2.0	2.6	4.5	1.9	4.3
may	0.4	-2.0	2.0	2.7	-0.8	4.2
jun	2.6	1.6	2.7	0.0	1.8	4.0
jul	2.2	2.2	3.7	0.0	1.5	4.0
aug	1.3	1.7	1.4	-0.2	1.6	3.8
sep	-1.1	-2.4	0.7	-4.2	0.3	3.3
oct	0.2	-0.1	1.5	1.7	0.8	3.1
nov	1.3	1.5	1.2	7.8	0.5	2.9
dec	0.3	-0.6	1.2	2.7	0.6	2.8
jan/dec/95	**14.8**	**6.4**	**23.2**	**20.0**	**15.0**	**53.1**
1996, jan	1.8	1.3	1.8	-1.2	0.5	2.6
feb	0.8	0.5	0.4	-0.3	0.6	2.4
mar	0.2	-0.1	0.2	0.5	0.4	2.2

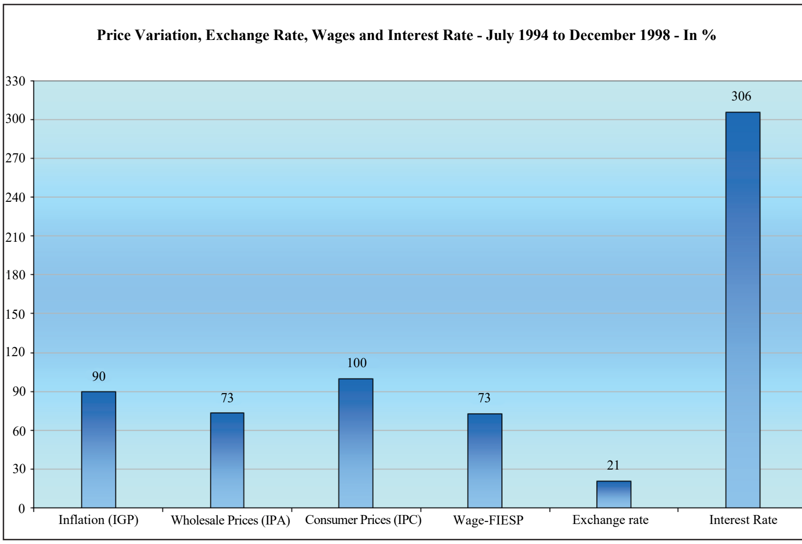
continued...

continuation

	Inflation (IGP)	Wholesale Prices (IPA)	Consumer Prices (IPC)	Wage-FIESP	Exchange rate	Interest rate[1]
apr	0.7	0.4	1.6	1.7	0.5	2.1
may	1.7	1.3	1.3	0.6	0.6	2.0
jun	1.2	0.9	1.4	-0.6	0.6	2.0
jul	1.1	1.4	1.3	1.4	0.7	1.9
aug	0.0	-0.1	0.3	0.6	0.6	2.0
sep	0.1	0.4	0.1	-0.5	0.5	1.9
oct	0.2	0.2	0.6	1.3	0.6	1.9
nov	0.3	0.2	0.3	1.7	0.5	1.8
dec	0.9	1.2	0.2	1.1	0.6	1.8
jan/dec/96	**9.3**	**8.1**	**10.0**	**6.6**	**6.7**	**27.4**
1997, jan	1.6	1.7	1.2	0.7	0.6	1.7
feb	0.4	0.3	0.0	-1.4	0.5	1.7
mar	1.2	1.6	0.2	1.7	0.7	1.6
apr	0.6	0.5	0.6	1.5	0.4	1.7
may	0.3	0.1	0.6	2.7	0.7	1.6
jun	0.7	0.2	1.4	-1.5	0.5	1.6
jul	0.1	-0.1	0.1	-0.1	0.6	1.6
aug	0.0	-0.2	-0.8	0.1	0.8	1.6
sep	0.6	0.9	0.0	-1.3	0.4	1.6
oct	0.3	0.4	0.2	0.3	0.6	1.7
nov	0.8	1.1	0.5	2.5	0.6	3.0
dec	0.7	0.9	0.6	1.0	0.6	3.0
jan/dec/97	**7.5**	**7.8**	**3.7**	**6.2**	**7.4**	**24.8**
1998, jan	0.9	0.8	0.2	-3.1	0.7	2.7
feb	0.0	-0.2	-0.2	-1.5	0.6	2.1
mar	0.2	0.1	-0.2	2.6	0.6	2.2
apr	-0.1	-0.3	0.6	-0.3	0.6	1.7
may	0.2	0.1	0.5	2.4	0.5	1.6
jun	0.3	-0.2	0.2	-2.1	0.6	1.6
jul	-0.4	-0.6	-0.8	0.9	0.6	1.7
aug	-0.2	0.0	-1.0	-0.5	1.2	1.5
sep	0.0	0.1	-0.7	-2.3	0.7	2.5
oct	0.0	-0.2	0.0	0.3	0.6	2.9
nov	-0.2	-0.2	-0.4	2.4	0.7	2.6
dec	1.0	1.7	-0.1		0.8	2.4
jan/dec/98	**1.7**	**1.5**	**-1.8**	**-1.4**	**8.5**	**28.8**
Acum. Real	**89.7**	**73.1**	**99.6**	**72.8**	**21.0**	**305.6**

Source: Bacen, FIESP.

1 Interest rate: over.



The association of the Real Plan economic policy with the political cycle - as it was first conceived by Kalecki -[1] should not disregard the fact that the economic policy implemented between 1994 and 1998 was presented as a step in the construction of a new "model" of development, whose central characteristics can be summarized in the binomial openness and competitiveness, given the assumption of inflationary stability.

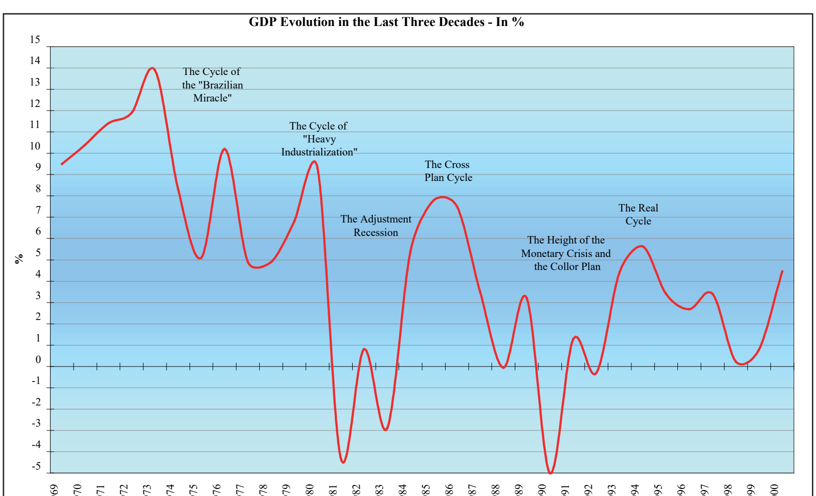
The fact that economic policy has brought together domestic and external conditions to serve the political cycle and has been subordinated to it as never before certainly changed the pace of the expected "convergence" and amplified the mismatches caused by the new strategy, without, however, changing its essence.

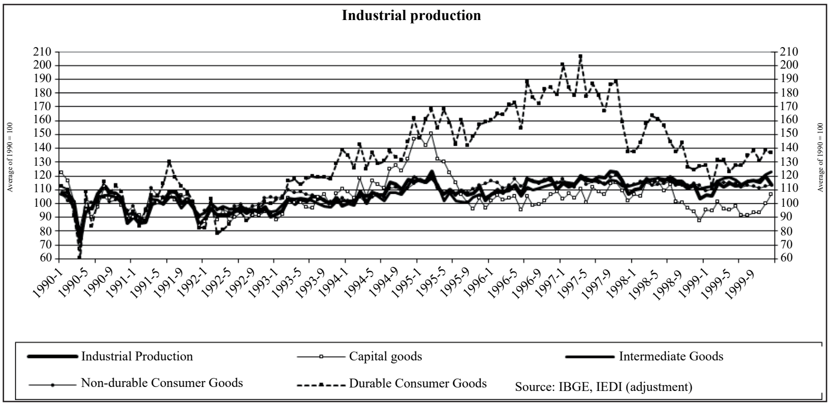
External conditions defined the ease of financing in foreign currency, and domestic ones determined the costs of interest and exchange rate policies on public finances, not to mention the initial income gain provided by stabilization in favor of a broad stratum of the population. This allowed economic policy to serve three rounds of the political cycle: first, the election of the government in 1994, for which "rapid disinflation" was decisive; then, the 1997 campaign, before the National Congress, for the approval of the constitutional amendment that would allow Presidential re-election; finally, the 1998 electoral campaign for Fernando Henrique Cardoso re-election, already conducted in a context of growing deterioration of the external situation and deepening of domestic imbalances, whose consequences the economic policy still gathered forces to momentarily neutralize.

1 Kalecki, M. (1971B).

It is known that, in parallel to the political cycle, there were shocks resulting from the "emerging market insertion" of Brazil in the international financial system. The succession of these episodes began as soon as the Real Plan was implemented, with the 1995 Mexican crisis, repeating itself in 1997 and 1998 with greater intensity. The sudden and elastic fluctuations in interest rates, the retraction of growth and employment exposed the effects of external crises on expectations and on the performance of the economy "real side." We have already observed that low growth and high interest rates "appear" as immediate consequences of the conjunctural fluctuations, determined by the political cycle and external crises, but, in reality, they are constitutive of the adopted economic policy "model."

The Real Plan was not able to change the basic trends that prevailed in the economy during the 1980s and early 1990s: growth, in decline since the beginning of the "lost decade," continued its trajectory in the "Plano Real cycle." The quality of the recent industrial growth has also deteriorated: the "mediocre rate" of industrial expansion has been supported by a single segment, durable consumer goods. The retraction of public investment and privatizations caused a decline in spending on new infrastructure construction, auguring the emergence of bottlenecks, especially in the strategic areas of energy and transportation. Also, for this reason, the capital goods industry, which had rehearsed a leading role in growth at the beginning of the Real Plan, succumbed to adverse factors and its production levels began to oscillate below the growth average. Finally, the accumulation of imbalances - the external deficit transformed into the public sector's domestic financial fragility - and the precariousness of the "emerging market insertion," periodically has thrown the economy into monetary crisis, now accompanied by threat of recession.





While it was possible to count on the abundance of foreign financing, with the constraint of trade and financial openings, the combination of exchange and interest rate policies left producers and markets on the defensive. This was true both for the price decisions of production destined for the markets of tradeable goods, and for the assets markets, foreign exchange and money markets. The impression of stability was formed while the favorable conditions of the "emergent market insertion" lasted. But the causes of macroeconomic instability have not been overcome. On the contrary, they worsened. They came out forcefully when globalized capital markets flashed the yellow light. It is possible that the instability factors would break out anyway. If it were legitimate to imagine the continuation of the foreign financing flows, the doubt of the holders of the domestic public debt would fall on the quality of the wealth accumulated against the State. To this we could add the growing social dissatisfaction in absorbing a rising tax burden to support a model of low growth and high unemployment, source of fiscal imbalance and balance of payments vulnerability.

The 1999 real plan survival and crisis

In theory, the assertion that the use of the exchange rate anchor should be temporary is correct and that, with the basic conditions of foreign financing for "emerging economies" maintained, definitive stabilization could only be achieved through a consistent inter-temporal fiscal adjustment. In the opinion of the financial markets, countries with a tradition of high inflation and frequent monetary disruptions would need to offer, for some time, the guarantee of a structural fiscal surplus, even though the emergence of temporary deficits determined by cyclical fluctuations in the economy is admitted.

The difficulty of estimating, in the midst of very high inflation, the real financial situation of the public sector is well known, since one of the effects of inflation, even with generalized but always imperfect indexation, is to make it difficult to calculate the value that the stocks of debt and revenue streams (enhanced by the financial revenues of the floating of bonds) and expenditure, as well as the real costs of indebtedness, will have after the currency stabilized. This is also true, of course, for other expenses with a nominal value very imperfectly indexed to price indices. In the case of Brazil, the effect of stabilization on government revenues seems to have been less important than in other countries, because the long coexistence with high inflation promoted a more appropriate indexation of State income.

Although the government can count on the possibility of limiting expenditures by reducing transfers and containing investments and social spending, the suspicion of the inexistence of a fiscal situation at least close to that considered ideal almost always accompanied the Real Plan implementation. Thus, stabilization resulted from the overuse of nominal exchange rate and high interest rates as the only instruments of disinflation. One caveat must be made to this conclusion: it fails to emphasize properly that these instruments are not neutral on public accounts, so that demonstrating fiscal soundness and dispelling suspicions about the solvency of the public sector became increasingly difficult tasks as the stabilization plan advanced, that is, as economic policy advanced in using these instruments. For these reasons, the interpretation that, “on the side” of stabilization, the plan “was going well,” while on the “fiscal side” – regarded as an independent matter – “was going badly” is wrong and posed as an obstacle to the stabilization policy continuity if the instruments that seemed to ensure its success simultaneously compromised and concurred to misadjust the public sector.

Success in the stabilization program and growing fiscal imbalance went together and were two sides of the same coin, the Real. It has already been observed that the formation of large current account and domestic deficits, as well as the very rapid growth of foreign debt - in this case, under the leadership of the private sector - and internal public sector debt, were entirely results in the execution period of the Real Plan. It is also convenient here to establish a clear distinction between the maladjustment motivated by the political cycle, which undoubtedly contributed to the fiscal imbalance of the spheres of government and the inherent maladjustment of the stabilization model, which would present itself anyway.

As expected, the rapid accumulation of foreign reserves - temporarily interrupted by the successive crises in emerging markets - and the real interest rates - which rose immeasurably after such episodes, falling very gradually afterwards - provoked an accelerated growth in public debt, increasing financial fragility in all spheres of government. This happened despite the high growth rate of tax revenue, which raised the gross tax burden from around

22% in 1994 to a level above 30% of GDP in 1998, and the execution of a large-scale privatization program.

Since this program started in 1991, until 1998, sales revenues totaled US$ 68.6 billion between federal (US$ 46.2 billion) and state-level (US$ 22.5 billion) companies, plus a total of US $16.5 billion in debt transferred to the private sector. Privatizations were very expressive in telephony (US$ 28 billion), electricity (US$ 21.7 billion), steel (US$ 5.6 billion), mining (US$ 3.3 billion), petrochemicals (US$ 2.7 billion), railroads (US$ 2.3 billion), and the financial sector (US$ 1.3 billion). One estimates a value close to US$ 40 billion in companies that can still be privatized, predominantly in the electricity sector. In order to compare the amounts involved, note that the global value of privatizations calculated after 1994 - 90% of the total - was equivalent to the public debt in December of that year. Sales revenues in the two years of the height of the privatization process (1997/98) corresponded, on average, to 3% of GDP in each of these years. These numbers contrast with the results of the public debt and the fiscal imbalance that continued as if a privatization of such magnitude was not underway. They are one more illustration of how the Real stability, in line with the economic policy adopted, required an unimaginable expansion of the public debt and the imbalance of public accounts. Consider the hypothesis of carrying out the Real Plan without a prior “shock” in the public debt that would substantially lower its value – Collor Plan legacy – and the absence of such a vast privatization program. The economy would not resist the Real Plan economic policy for more than three years.

The fiscal effects of the management of instruments for stabilizing and constraining markets would become clear at the beginning of 1995 when the government – harassed by the trade deficit projected for 1995 and given the doubts that arose for “emerging economies” due to the Mexican crisis – took new and severe quantitative initiatives to restrict credit and raise interest rates, causing a rapid deceleration in product and income growth and reversing an intense but short cycle that was nourished by two factors: the “wealth effect” motivated by stabilization, and a credit expansion that, although it took place at high interest rates and was held back by economic policy controls, was nonetheless expressive. The fiscal result was immediate, causing a rapid conversion of surplus (in 1994) to public sector deficit (in 1995).

Furthermore, the emergence of default levels well above the historical average hit the banking system, already weakened by the loss of inflationary revenues. The 1995 banking crisis broke three large banks, in addition to several smaller ones, paving the way for a significant sector denationalization. Foreign banks came to dominate 35% of total banking assets in 1998 – 9% in 1994. A special program designed to absorb the “bad part” of bank assets so that the “good part” could be passed on to another (preferably foreign) institution, PROER, amounted to 4% of GDP in direct costs or 10 % including indirect costs. Thus, the effects of the inflection of the economy trajectory on public finances were not restricted to the loss of tax revenue, but also impinged on high-cost interventions by the Central Bank in the banking system.

The same circumstances worsened the financial imbalance of states and state banks, which entered a phase of scarcity of resources and unbearable growth in stocks of securities and contractual debt. The renegotiation carried out in 1997 between the Union and the states sought to dilute over a very long term (30 years) the effects of very high interest rates on state debts, which, for this reason, had their values multiplied, even though they did not grow on account of the financing needs of productive expenditures. Had it not been for the renegotiation, whose motivation can also be associated with the political cycle and the privatization strategy (in the case of state banks), rigorously the main states would have failed in the first term of Fernando Henrique Cardoso administration already. However, even the longer terms and the lower interest rates still left Federation units with debt service burdens that can become very heavy in times of recession.

Public Deficit – % do PIB

Year	Operational	Primary	Real Interest	Nominal
1992	2.1	-2.2	4.4	42.7
1993	-0.3	2.6	2.4	58.2
1994	-1.4	-5.3	3.9	45.2
1995	4.9	-0.4	5.1	7.2
1996	3.8	0.1	3.7	5.9
1997	4.3	0.9	3.4	6.1
1998	7.4	0.0	7.4	7.9
1999	3.4	-3.2	6.7	10.0
2000	1.2	-3.5	4.7	4.6

(+) Déficit (-) Superávit

Source: BACEN.

To solve these serious financial and equity imbalances that arose from the way in which the stabilization plan was implemented, the government would have to reduce interest rates more quickly. However, given the dependence on globalized financial markets, monetary policy managers had to respect the interest differential required by those who purchase and maintain assets denominated in Reais in their portfolio. In a certain sense, the Brazilian refusal to adopt the "convertibility" scheme with a fixed exchange rate (Argentine model), therefore maintaining the possibility of devaluation, but not exercising it unless very slowly, led to the permanence of very high interest rates differentials together with continued exchange rate overvaluation, with all the difficulties that this entailed for fiscal administration and the bad consequences for the balance of payments and economy growth.

Given this, it is curious that the defenders of the current exchange rate regime have tried to invoke the emergence of a "new macroeconomic configuration" to affirm the adequacy of the real exchange rate level. They wanted to believe that the macroeconomic configuration is – itself – a product of the exchange rate regime. Perhaps they intended to claim that the stabilization had caused such an increase in confidence in the financial markets to the point of ensuring a steady flow of good quality foreign financing. This would justify the exchange rate "revaluation" and would make fears about the evolution of the trade deficit and the current account imbalance unsubstantiated. As long as the latter did not exceed certain limits (in principle projected at 4% of GDP), concerns about the risks of interruption of capital inflows would be unfounded.

This assumption systematically ignored three important issues: a) the possibility of changes in international financial conditions; b) the sensitivity of markets in relation to the situation of deficit and debtor countries, particularly those in "emerging markets", c) the latent risk of a flight from the Real, given the disproportion between the mass of liquid domestic assets and the country's foreign exchange reserves.

It is needless to say that, since the Asian crisis of the second half of 1997 and, above all, after the collapse of Russia in August 1998, the availability of financing and capital to developing countries has been reduced, which means that if the international financial market was willing to finance that projected level of current account deficit, now it would no longer be. On the other hand, the interest rates spreads between US government bonds and those paid by "emerging" countries, which tended to retreat after each unmeasured rise in the acute phases of the liquidity and distrust crisis, hardly receded enough to replace interest rate differentials at the levels that prevailed before each turbulent episode. Finally, the markets started to work with the hypothesis that the possibility of a price correction on the stock exchanges that were still showing strong capitalization upsurges, as in the case of the American ones, should not be excluded either.

For this reason, after the Russian crisis and even after the Brazilian agreement formalized with the IMF in early December 1998, the foreign and domestic financial markets´ reaction was so significant in assessing the risks associated with positions in Brazil. Internally, the futures exchange and interest rate markets, for example, continued to show great sensitivity to changes, even slight ones, in foreign financing conditions, whether resulting from a negative balance in the foreign exchange markets on consecutive days, a concentration of amortizations in a given month, or a rising tendency in trade deficit. Externally, the opinion of the markets regarding the inadequacy of the Brazilian exchange rate and the deterioration of public accounts showed a hypersensitivity to problems that were not new, but which had been growing progressively, revealing a confidence deficit.

This confidence deficit was aggravated by the perception that the exchange and monetary regime endogenously generated an current account deficit now considered excessive – 4.4% of GDP in 1998 –, an unsustainable fiscal deficit – 8% of GDP in the nominal concept –, and a huge growth of the mass of domestic financial assets in relation to the volume of foreign reserves and GDP, inflated by the high domestic interest rate and, as before, endowed with the characteristic of quasi-currencies. During the execution of the Real Plan, the total means of payment, in its broadest concept, "M4," jumped from 1/3 of the GDP in 1994 (27% in 1993) to about 50% of the GDP. Furthermore, despite the authorities' efforts, it was not possible to significantly change the relationship between the Central Bank and the banking system regarding the turnover and liquidity of public securities.

As for the fiscal deficit, the data show that the explosive growth in 1998 resulted exclusively from the interest paid by the federal public sector to sustain the Real stability and the economic policy continuity.

In this process, Brazil would lose no less than US$ 25 billion in reserves, with US$ 20 billion in September alone. The fall in reserves would continue in the following months, interrupted only by the disbursement of the first installment of the financing agreement negotiated with the IMF. This agreement, formalized in December and intended to provide resources[2] to ensure the Real stability, did not stop the wave of distrust in the currency. In the two months after the agreement with the IMF came into effect, capital flight reached US$ 15 billion.

Payment options – in % of PIB

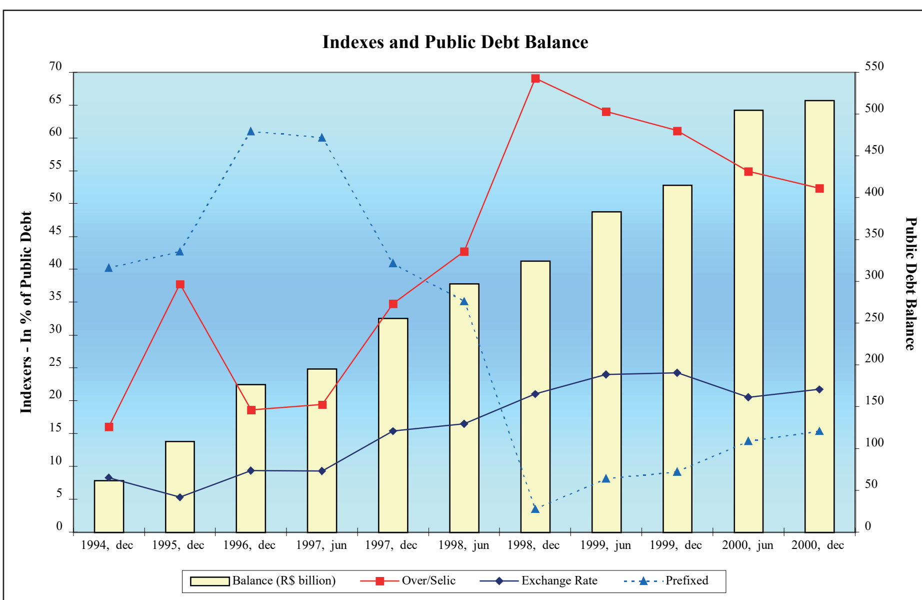
Period	M1	Near money	Federal Bonds	State and city bonds	M2	Savings deposits	M3	Private securities	M4
1994 Dec	4.4	1.8	5.7	1.4	13.9	8.6	22.4	11.0	33.4
1995 Dec	4.2	1.9	8.3	1.4	15.7	9.3	25.1	11.7	36.7
1996 Dec	3.7	2.9	12.9	1.4	20.9	9.0	29.9	10.4	40.3
1997 Dec	5.2	0.7	15.5	1.0	22.4	10.7	33.2	10.3	43.5
1998 Dec	5.7	0.8	20.7	1.1	28.3	12.1	40.4	10.5	50.9
1999 Dec	6.0	13.7	12.4	1.2	33.3	10.6	43.9	8.8	52.7
2000 Dec	6.8	19.0	14.5	0.1	40.3	10.2	50.5	8.0	58.6

Source: BACEN.

2 US$ 41.5 billion in total, joining IMF, IDB, IBRD and central banks coordinated by the BIS, with disbursements throughout 1999 – around US$ 9 billion immediately.

Thus, a total of US$ 45 billion – or US$ 50 billion if we consider the peak of foreign exchange rate reserves in April 1998 – was the amount, in net terms, of the capital flights in view of the Real imminent fall. The insistence on keeping the exchange rate overvalued, even in the face of the opposing certainty that was dominating all evaluations, is no longer explained by the logic of economic policy – at this point completely surpassed by the facts. It only finds an explanation in the political factor – in this case, in the third political cycle, that of the second-term election of Fernando Henrique Cardoso, which took place in the first round of October elections.

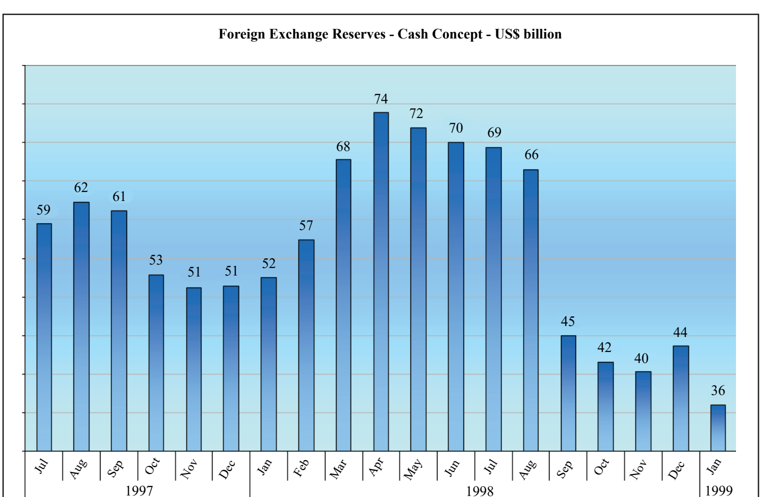
The cost of the extended life span of the economic policy in 1998 is extraordinary: it is equivalent to the amount mentioned above – corresponding to 6.5% of GDP – multiplied by the difference in the exchange rates after the Real collapsed, in other words, compared to the overvalued exchange rate through the which resources were remitted before the fall. Comparing the average value of R$1.18 per dollar in the remittance period to a quotation after the devaluation of R$1.80, the "subsidy" for those who sent dollars abroad was 52% for each dollar remitted, R$ 26 billion or almost 3.5% of everything that was produced in 1998. This is the value of the wealth reduction (or, alternatively, indebtedness increase) of the public sector and the domestic producers of tradable goods, so that the economic policy was maintained for a while longer and, with it, the imaginary stability of the Real. The public debt with exchange rate correction costed an equivalent amount, also as an extreme expedient to sustain the foreign value of the currency.



After the extended life span was passed, there was really no alternative but the formulation of an immediate fiscal plan to improve the weakened public finance situation and, on the external plane, resorting to the IMF to restore part of the foreign reserves. The Brazilian government came up with a three-year "Fiscal Stabilization Program" to qualify itself for the Fund's resources. The IMF evaluated and complemented it.

The government proposed a strong adjustment. With the economy in recession, very high interest rates on the public debt and continued exchange rate overvaluation, it set a target for 1999 to halve the nominal deficit of 8% of GDP, in an adjustment of R$28 billion. Increases in taxes – CPMF, a tax on financial transactions, increasing from 0.20% to 0.38% and Cofins, the social contribution levied on sales, rising one percentage point, from 2% to 3% – would contribute with just under half the adjustment; spending cuts would add up to R$8.7 billion, and R$6 billion would come from the social security area, where an increase in the contribution of civil and public retirees was foreseen. This, added to a fiscal effort also by the States and Municipalities, would ensure in 1999 a primary surplus of 2.6% of GDP (2.8% in 2000 and 3.0% in 2001), necessary to cover part of the estimated 6,5% of GDP as interest service on the debt.

As for the IMF, it estimated a 7% growth in exports for 1999. Also, despite the low growth forecast for the world economy that year, a drop in commodity prices and an overvaluation of the national currency, it projected a trade surplus of US$ 3 billion (deficit of $6 billion in 1998). This amount would make it possible to reduce the current account deficit from US$35 billion in 1998 to US$24 billion in 1999. The IMF did not impose exchange rate adjustments or even more elastic interest rate variations, as might be expected.



The agreement partially recomposed the foreign reserves and made possible a new round of capital flight at the subsidized exchange rate. But that was it. Financial markets can make mistakes and often do so in the face of real changes, which they may not anticipate correctly, but they hardly fail to accuse the purest fiction. The international distrust in the currency continued and with it the instability of the Real Plan. Domestically, the aforementioned features of public debt markets were accentuated after the Asian crisis and the Russian collapse. Investors' growing uncertainty about sudden price fluctuations, with the risk of huge losses for government bond holders, forced monetary policy administrators to progressively accept the replacement of fixed-rate bonds with floating-rate ones. This was done simultaneously with the dollarization of another important fraction of the domestic public debt, an expedient intended to offer protection to those who had liabilities denominated in dollars and which, in practice, corresponds to a partial nationalization of the foreign debt contracted predominantly by the private sector during the Real Plan cycle. As it is common in situations like this, where uncertainty and acute mistrust prevail, private agents pass on or try to pass on to the government the "interest rate risk" and the risk of an uncertain currency depreciation.

In this way, the agreement with the IMF served to give the Real Plan a second extended life span. It is very important to note that this agreement, that was structured in a relatively short time, mobilizing expressive amounts from different sources, and grounded on unrealistic bases, was only possible due to the risk – at that time considered very high – of contagion in the globalized financial markets of a Real collapse. Contagion had been a feature of previous crises and now threatened to repeat itself from a larger economy, such as Brazil's, which, moreover, maintains closer commercial and financial relations with the world's leading economy. The agreement itself helped to minimize this risk, either because it denoted a determined international financial assistance in anticipation of a crisis that was more than announced, or because it allowed the completion of portfolio adjustments and/or the formation of hedge positions for foreign and national banks and investors against the "Brazil risk."

The time taken for an announced outcome and for the defensive adjustments by banks and investors in the face of the prospect of a currency collapse allowed the contagion effect of the crisis to be dampened. The Brazilian exchange crisis did not fail to have repercussions on other economies, but the impacts took place through foreign trade, which was all the more profound the greater the gain in competitiveness of Brazilian exports and the retraction of imports resulting from the Real depreciation. The long preparation for the outcome prevented the transmission of the crisis through financial channels, as has been characteristic of contagion processes in recent years. The isolation of the Brazilian crisis meant higher domestic adjustment costs in view of the lesser willingness of the international financial system and the IMF to contribute resources to stabilize the Real after the exchange rate liberalization occurred in January 1999.

The situation is paradoxical because, if the collapse of the international value of the currency was inevitable, it would be necessary that, at the time of the exchange regime change, the IMF and other international entities reinforce the Brazilian foreign reserve position to avoid an overshooting. This “exaggeration” in the currency devaluation occurred in Asian countries in 1997 and also affected the Real shortly after the fluctuation. In fact, in Asian countries, such as Malaysia, Thailand and Korea, the currency depreciation was very strong (between 70% and 110%) over the 3 to 6 months after the fluctuation, and then receded. In Brazil, with the changes undertaken in the exchange rate in January 1999 (the extension of the “currency band” on January 13th implied a devaluation of 9%), the institution of free floating on January 18th made the quotation of the dollar reach R$ 1.98, representing a 63% variation in relation to the R$ 1.21 on the day before the change.

The currency depreciation resulted in a significant transfer of income and wealth in favor of tradeable goods producers. To the same extent, it resulted in a loss for what was previously defined as “importers” and net debtors in foreign currency, particularly those who are unable to offset the initial loss by increasing domestic prices (inflation). The other “loser,” following the Real Plan´s playbook, was the public sector, mainly due to the increase in the amount of public debt pegged to the dollar and the rise in interest payments, which were partially offset by the increase in the tax burden, by means of, above all, the surge of the worst quality taxes, and by the reduction of wages due to inflation.

CHAPTER 17

OLD AND NEW MYTHS OF RURAL BRAZIL

José Graziano da Silva

In very synthetical form , we can say that our research under the Rurbano Project (1) in its phases I and II (2) contributed to overthrow some old myths about the Brazilian rural world, but which unfortunately may be serving to create new ones.

We will present below what we believe to be the main conclusions reached by the research so far and a list of what we are proposing to research in phase III, which began in May 2001 and will continue until 2003.

The old myths

"The rural is synonymous with backwardness"

We show that the rural is not opposed to the urban as a symbol of modernity. There is still a lot of backwardness and violence in the Brazilian countryside, for reasons that are partly historical, related to the way in which our colonization was carried out, based on large properties with slave labor.

But there is also the emergence of a new rural, composed both by ***agribusiness*** and by new social subjects: some ***neo-rural,*** which exploit the market niches of new agricultural activities (snail farm, exotic plants and animals, etc.); residents of upscale rural condominiums; clandestine allotments that house many domestic workers and retirees, who cannot survive in the city on the minimum wage they receive; millions of family and pluriactive farmers, agricultural and non-agricultural employees; and still millions of "***without-without***," excluded and disorganized, who in addition to having no land, also have no job, no home, no health, no education and not even belong to an organization like the MST (Landless Workers' Movement) to be able to express their demands.

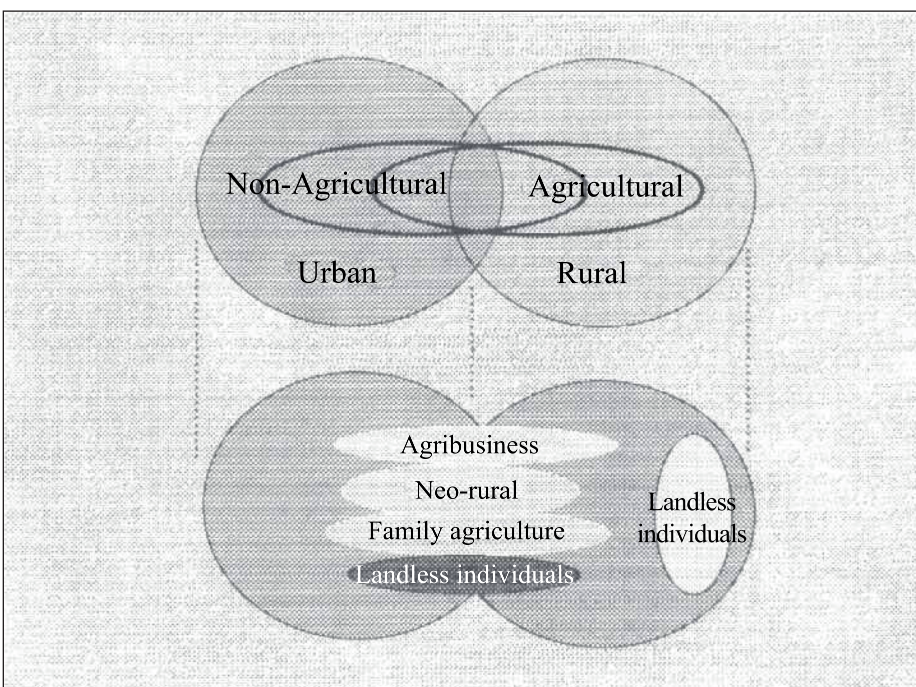
Unfortunately, this category of "without-without" has been growing rapidly, especially since the second half of the 1990s. The 1999 PNAD data allow an approximation of this contingent of rural poor: there are almost three million families (or 15 million people) surviving on a ***per capita*** disposable income of US$1 or less per day (R$ 34.60 monthly at the exchange rate of September/99) (3).

More than half of these poor rural families have their income exclusively from agricultural activities: they are self-employed families (30% of the total) with insufficient land areas and/or with precarious access to land (partners, squatters, assignees) or families of agricultural employees (25%), the vast majority without a formal contract.

A third of these poor rural families live in households without electricity, almost 90% do not have running water, sewage, or septic tank. In almost half of these poorest families, the head or person of reference never attended school or did not complete the first grade of elementary school, and may be considered illiterate.

But, unfortunately, none of this is a privilege of the "old backward rural": of the 4.3 million poor families residing in non-metropolitan areas (small and medium-sized cities), 70% also do not have a sewage collection system or septic tank, almost 30% do not have running water, although less than 5% do not have electricity in their homes. In a third of them, the head of the family can also be considered illiterate. Only the difference between rural and urban is evident with regard to access to electricity, which currently constitutes one of the fundamental basic services, without which it is difficult to talk about modernity. Unfortunately, this difference is largely explained by the possibility of the urban poor making clandestine connections ("gatos").

Figure 1 – The new rural



The rural is mainly agricultural

We show that an increasing number of people residing in rural areas are now engaged in non-agricultural activities.

The 1999 PNAD data also show that of the nearly 15 million economically active people in rural Brazil (except the Northern region), almost a third - or 4.6 million workers - were working in non- agricultural rural occupations (NARO): as mason servants, drivers, caretakers, maids, etc.

More importantly, non-agricultural occupations grew in the 1990s at a rate of 3.7% a year – more than double the country's population growth rate (see table 1). Meanwhile, agricultural employment, due to the mechanization of harvesting activities for our main products, has been falling more and more rapidly, at a rate of-1.7% per year. Our projections indicate that if this pace continues, by the year 2014 most rural residents of the country will be engaged in these non-agricultural activities. In some states, such as São Paulo, this is already happening.

Table 1 – Evolution of the Brazilian population (a), 1981-99

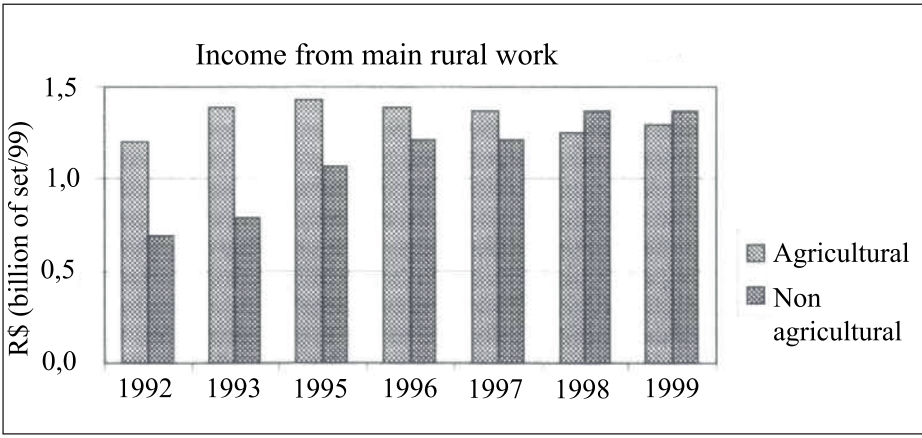
Job	People (in millions)				Growth rate (in % p.a.)		
	1981	1992	1996	1999	1981-92	1992-99	1996-99
Urban	85.2	113.4	122.4	127.8	2.6	1.7	1.4
Employed (b)	31.7	46.5	50.4	52.8	3.6	1.8	1.5
- agricultural	2.6	3.7	3.4	3.4	3.3	-1.6	-0.2
- non-agricultural	29.1	42.9	47.0	49.3	3.6	2.0	1.6
Rural	34.5	32.0	31.7	32.6	-0.7	0.2	1.1
Employed (b)	13.8	14.7	13.9	14.9	0.6	-0.2	2.1
- agricultural	10.7	11.2	9.9	10.2	0.4	-1.7	0.4
- non-agricultural	3.1	3.5	4.0	4.6	1.2	3.7	6.1
Total	119.7	145.4	154.0	160.3	1.8	1.4	1.3

Source: Special tabulations of the 1981 and 1992-99 PNADs, Project Rurbano, November 2000.

Notes: a) does not include rural areas in the North region, except for the state of Tocantins b) Restricted economically active population, which excludes unpaid workers who work less than 15 hours a week and those who dedicate themselves exclusively to self-consumption.

Another fact that confirms the importance of these activities is that the sum of non-agricultural income of people living in rural areas surpassed in 1998 and 1999 the income derived exclusively from agricultural activities, according to the PNADs. In other words, although it is known that agricultural incomes declared in the PNADs are strongly underestimated, the non-agricultural incomes of residents in rural areas in Brazil exceed the total agricultural incomes since 1998 (see graphic 1).

Graph 1 – Evolution of income from the main job of people employed in the Brazilian rural environment, according to the field of activity. Brazil, 1992-99

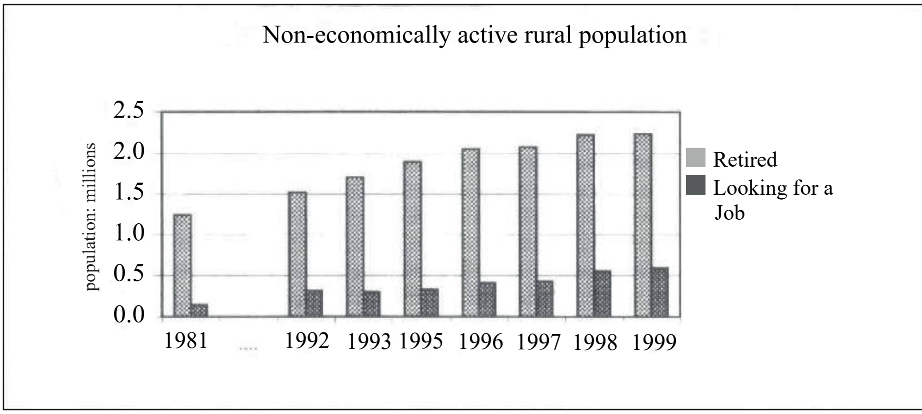


"The rural exodus is inexorable"

The most recent statistics from rural Brazil reveal a paradox that interests all of society: employment of an agricultural nature is dwindling practically throughout the country, but the population residing in the countryside has returned to growth; or at least stopped decreasing. These exchanged signals suggest that agricultural dynamics, although fundamental, no longer alone determines the course of demography in the countryside. This new scenario is explained in part by the increase in non-agricultural employment in the countryside. At the same time, the mass of unemployed, inactive and retired people who maintain rural residence increased (see graphic 2). If it is true that some exodus still persists, especially in the southern region, it no longer has the strength to condition this new emerging pattern of recovery in rural areas in most regions of the country.

Data from PNADs show that the rural population hit rock bottom in 1996 (year of population count), with 31.6 million people (4); since then, it has been recovering, having reached 32.6 million in 1999, that is, almost one million people more, meaning an annual growth rate of the rural population of 1.1% per year, very close to the total population growth of 1.3% per year in the same period. In the Northeast, the two rates were equal (1.1% per year) and in São Paulo, the growth of the rural population was twice the total (3% per year against 1.5% per year), indicating a true "return to the fields" which is not to be confused with a return to agricultural activities, as a significant part of this population now resides in rural areas close to large cities in the interior and the state capital. In the southern region, however, the rural population still shows signs of decline, especially in those areas we call agricultural rural or deep rural.

Graph 2 – Evolution of inactive people and residents in rural areas, according to the field of activity. Brazil, 1981-99



It is dangerous, however, to harbor illusions that the market, by itself, has implemented a new sustainable dynamism in the Brazilian countryside. We show that the inevitable is the agricultural exodus which, however, can be, at least partially, compensated by the growth of NARO. If we add to that the inactive (mainly retirees) who seek rural areas as a place of residence, a policy to contain the significant rural exodus still existing in certain regions of the country, such as the South, may be feasible.

“Agricultural development leads to rural development”

We show that agricultural occupations generate the lowest income; and that the number of agricultural families is decreasing, as they cannot survive on agricultural income alone. Not even the number of pluriactive families, whose members combine agricultural and non-agricultural activities, has been increasing. Given the drop in income from agricultural activities, rural Brazilian families are becoming increasingly non-agricultural, guaranteeing their survival through social transfers (retirements and pensions) and in non-agricultural occupations.

Unfortunately, earnings from the period prior to the Real Plan cannot be compared due to the distortions introduced by the monetary changes that took place in the first half of the 1990s. But the data we have for the period 1995-99, entirely under the Real Plan, indicate that for self-employed rural and pluriactive families, the only portion of ***per capita*** family income that grew significantly in the period was that from the social transfers (+6.7% and+ 4.9% p.a., respectively). The fraction of income from agricultural activities (which represents 3/4 or more of the total income of these families) fell for both rural self-employed families (-4.2% p.a.) and pluriactive ones (-5.3% p.a.). To further aggravate the situation, non-agricultural incomes only grew for rural self-employed non-agricultural families, remaining stagnant for pluriactive ones.

In short, agricultural and pluriactive families became poorer in the second half of the 1990s. And the fall in their ***per capita*** incomes was not only greater because of the growing "compensation" of social transfers for retirement and pensions. It is for this reason that rural households are increasingly becoming non-agricultural.

"The management of small and medium rural properties is familiar"

We show that small rural district (generally less than 2 ha, the size of the smallest rural module) are growing, which are much more of a rural residence than a productive agricultural establishment. And that the management of small and medium-sized agricultural properties is becoming individualized, with the father and/ or one of the children in charge of the activities, while the other family members seek other forms of productive insertion, generally outside the property. Also, an increasing part of the agricultural activities that used to be carried out inside the properties are now being contracted externally through third-party services, regardless of the size of the farms. That is, who runs agricultural establishments today is no longer the family as a whole, but one (or a few) of its members, which undermines the idea of a social division of labor based on the availability of distinct family members of a capitalist division of labor.

The typical rural family no longer gathers around agricultural exploitation. The family patrimony to be preserved includes the land and, above all, the parents' house, which becomes a kind of territorial base, welcoming close relatives on some festive occasions and increasingly becoming a point of refuge from crises, especially unemployment, in addition to remaining as an alternative to return at an old age. In addition, family management now includes other non-agricultural "businesses" as part of its survival strategy (most cases) or even accumulation. In other words, the center of the family's activities is no longer agriculture because the family is no longer agricultural and has become pluriactive or non-agricultural, although it remains residing in the countryside.

The new myths

"NARO is the solution to unemployment"

A disaggregated analysis of the main occupations performed by people living in rural areas in the period 1992-99 shows that almost all agricultural occupations showed a strong reduction, especially those more generic such as "rural worker" and "agricultural employee," which aggregate workers with lower level of qualification: about one million fewer people employed in 1999 compared to 1992.

On the contrary, almost all non-agricultural rural occupations showed significant growth in the same period, accumulating about 1.1 million more people in 1999, as if "compensating" for the fall in agricultural occupations. Here, too, those activities that are not very differentiated stand out, such as those employed in domestic services, mason's assistants and various service providers, which together make up a third of the non-agricultural rural jobs generated in the period.

Our work has shown that agricultural activities continue to be the only alternative for a significant part of the rural population, especially the poorest. The portion of the agricultural labor force that becomes surplus due to technological progress and productive restructuring (crop replacement, for example) does not automatically find non-agricultural occupations to engage. And this is fundamentally due to the inadequacy of the personal attributes of agricultural workers who are dismissed (middle-aged men and women without professional qualifications and without formal education) to exercise the available NAROs.

Most of the non-agricultural rural occupations in Brazil, although they provide a generally higher income than agricultural ones and are not as hard as these, they are also precarious and low-skilled jobs. They are basically personal services derived from the high concentration of income existing in Brazil and not from the modernization of agricultural activities, nor from the provision of services aimed at leisure and environmental preservation, or even productive non-agricultural activities such as agribusiness or civil construction. No wonder we find in all regions of the country a strong growth in domestic employment of people residing in rural areas. Domestic employment plays today, for women, the role of civil construction in past decades for men: it is the gateway to the city as it provides, in addition to a fixed income, a place to live. Especially for younger rural women, this seems to have been one of the few forms of entry into the labor market in the 1990s, given the growing restrictions on their entry into the agricultural labor force.

*"NARO can be the engine
of development in backward regions"*

One of the most important contributions of the Rurbano Project was to show that the new dynamics in terms of employment and income generation in the Brazilian rural environment have urban origins, that is, they are driven by non-agricultural demands of urban populations, such as the real estate dynamics for country residence and services related to leisure (rural tourism, environmental preservation, etc.).

We also show that NAROs are more dynamic precisely in those rural areas that have developed agriculture and/or are closer to large urban concentrations. In other words, in the most backward regions, there are no agricultural jobs and much less non-agricultural occupations. Thus, there is no alternative but compensatory policies such as minimum income and active social security, for example. Furthermore, there is a certain "cyclical reversal" to subsistence production in these backward regions.

This is what seems to be happening in the Northeast: the agricultural occupations that had been falling, started to grow again in 1999, in part due to the end of the drought that has devastated the region in recent years. The PNDA registered an additional 450 thousand people employed in rural areas in 1999 compared to the previous year, the vast majority of them in unpaid agricultural activities; and a small reduction in NAROs, a similar situation to what had already happened between 1993 and 1995. And this "resumption of subsistence production" is financed in large part by social transfers of income (the main one being from rural retirement) and by the work of small producers' wives who become domestic workers in the cities of the region and are responsible for significant part of the monetary income of families of rural employees in the Northeast.

In summary, the lack of rural development in the vast majority of "backward" regions of the country is fundamentally due to the lack of development of non-agricultural activities.

"Agrarian reform is no longer viable"

We show that agriculture is no longer the best form of productive reintegration of landless rural families, especially due to the low level of income generated by the traditional activities of the sector. Small designated areas to produce only rice and beans, as well as other traditional agricultural products, especially grains, are really no longer viable. But, fortunately, traditional agricultural activities are no longer the only alternatives available today for generating employment and income for rural families. Thus, it is possible, and increasingly necessary, for an agrarian reform that creates new forms of productive insertion for rural families, whether in "new agricultural activities" or in NAROs. For example, in the domestic agribusiness, which allows them to add value to their agricultural production, as well as in market niches provided by the new agricultural activities mentioned above, or even in the provision of personal services or production auxiliaries.

"The new rural does not need public regulation"

We show that the new rural is not only made up of ***amenities,*** to use an expression that is very fashionable in developed countries. As we have already said, in Brazil, most NAROs, for example, are just precarious jobs, also with low pay. We also show that the growth of unemployed people in rural areas exceeded the rate of 10% a year in the period 1992-99, only part of this is due to the "temporary return" of children who had previously migrated to the cities and return to their parents' homes until they find another job. And, above all, there are millions ***of*** homeless people to join the rural exodus as soon as industrial growth generates new work opportunities in the cities, because the local conditions for education, health, housing, etc., are minimal.

The common feature between the new and the old rural is its heterogeneity, which prevents the generalization of specific local situations. There are new forms of pollution and destruction of nature associated with both new agricultural and non-agricultural activities. Even in rural condominiums inhabited by high-income families, waste treatment and sewage disposal are very precarious in most cases. Likewise, although even the maid earns better than the rural worker, the higher level of monetary income provided by NAROs does not always mean an improvement in the living and working conditions of non-agricultural rural families, especially when this implies loss of access to land and the possibility of combining non-farm incomes with subsistence activities.

The emergence of new functions (mainly leisure and housing) for the rural, added to the loss of sectorial regulation (via agricultural and agrarian policies) resulting from the emptying of the national state, left spaces that demand new forms of public and private regulation. This is the exemplary case of city halls fighting against the disorderly proliferation of rural condominiums that are basically new forms of clandestine allotments, which end up demanding services such as electricity, water, garbage collection, etc.; or the fee-fishing ponds, which have to submit to inspection by the Health Service, IBAMA and INCRA, entities that have contradictory legislation for framing the same activity; or else new forest reserves outside the property, which are not legally recognized, although they have much greater ecological value than the maintenance of small discontinuous areas inside small and medium-sized rural properties. These are just a few glaring examples that we need ***a new institutionality for the new rural Brazilian,*** without which we run the risk of seeing it age prematurely.

*"Local development
automatically leads to development"*

The new approach to sustainable local development has the undeniable merit of allowing for the overcoming of the already archaic urban/rural and agricultural/non-agricultural dichotomies. As we know today, the rural, far from being just a space differentiated by its relationship with the land - and more broadly with nature and the environment - is deeply related to the urban that adjoins it. We can also say that agricultural activities are profoundly transformed by non-agricultural activities, so one cannot talk about modern agriculture at the end of the 20th century without mentioning machines, fertilizers, pesticides and all the other non-agricultural activities that support it.

Our work has shown that the pursuit of agricultural development through an eminently sectoral approach is not enough to lead to the development of a region. They also showed that the lack of social organization - especially in civil society - has been characterized as a barrier as strong or stronger than the misery of rural populations, especially at a time when globalization revalues local spaces as arenas of political, economic and social participation for organized groups.

The focus on local development presupposes that there is a minimum of social organization so that different social subjects can be the real protagonists of the processes of transformation of their places. But this organization does not always exist at the local level; and when it exists, it is restricted to those "old" social actors who are ultimately responsible for the local underdevelopment.

In this sense, we can say that sustainable local development must also be understood as political development in the sense of allowing a better representation of the different actors, especially those majority segments that are almost always excluded from the process by local elites.

In the Brazilian case, for example, actions aimed exclusively at agricultural development, although they had achieved an enviable modernization of the techno-productive base in some regions of the Center-South of the country, these were not accompanied by the long-awaited rural development. One of the main reasons was the privilege to the technological and economic dimensions of the rural development process, relegating social and political changes to the background, such as, for example, the trade union organization of landless rural workers and small producers. With globalization, the disparities that currently exist in our country, whether in regional terms or in relation to family farming ***vis-à-vis agribusiness,*** tend to increase even more.

It is essential to mention that the scope of these actors is not restricted to agricultural producers - family or not - no matter how different they may be. Urban individuals who inhabit the rural environment or who simply regard it as an almost idyllic reference for a new relationship with Nature should also be considered. This is because another component, increasingly important in strengthening local spaces, has been the growing demands and concerns with the management and conservation of natural resources. Here, too, the organization of social actors can boost the participation and implementation of local development plans aimed at their interests, although there are still many restrictions on the forms of participation and representation, not only due to their little mobilization but also to the difficulty of having all social segments duly represented, given the presence of operational impediments and biases linked to institutional structures in force at the local level and to the domination of decisions by the strongest groups.

What remains to be researched

In May 2001 we started what we call ***Phase III*** of the ***Rurbano Project,*** with the objectives of:

- identifying the main conditions of income distribution of ***rural and/or agricultural individuals and families,*** such as the degree and intensity of pluriactivity in Brazilian agriculture, land distribution according to the occupation position of household members, the effect of different forms of access to land (owner, partner, tenant and self-employed) on family income, different forms of occupation of family members according to sex, education, characteristics of households and their availability of essential goods and services etc.;
- researching the importance of ***domestic work*** as an alternative occupation and income for rural families, isolating this category of workers as a new position in the occupation and another specific type of activity;
- researching the importance of ***agribusiness*** and ***rural industry*** as generators of employment and income in rural areas, particularly in the state of São Paulo and Minas Gerais, which have one of the largest agro-industrial parks in the country;
- characterizing rural and/or agricultural families with ***retired and/or unemployed persons***, with the objective of proposing an active social security policy for disadvantaged regions of the Brazilian rural environment;
- characterizing the ***landless families*** in relation to the income and occupation of their members at the level of large regions and main units of the Federation, aiming to delimit what could be called the "***hardcore"*** of rural poverty with the objective of subsidizing the national policy on rural settlements.

In addition to these themes, which arise from the conclusions and preliminary results already obtained, Phase III of the Rurbano Project is intended to carry out some ***case studies with a*** view to:

- identifying the possible causes of the ***underestimation of variable incomes*** in the PNADs, particularly of agricultural incomes;
- deepening the analysis of the ***dynamics of generation of non-agricultural occupations identified*** for some specific Brazilians regions that stood out in previous analyses (tourism in the Northeast; recreational farms in the Southeast, etc.);
- investigating the issue of the ***identity of rural pluriactive and/or non-agricultural families*** in face of the new social subjects of the new rural world, including caretakers, residents of closed condominiums, retirees, etc.;
- deepening the theme of the relationship between ***local development and local power***, highlighting the ***competence in the different levels of action of the public power*** (municipal, state and federal), as well as what would be the main forms of public and private intervention in the areas;
- assessing the ***environmental and socio-economic impact of the "new" activities developed*** in rural areas, introducing the issue of environmental and labor legislation and the need for a code on the use of land, water and other natural resources for the management of the "rurban" territory;
- deepening the theme ***of public policies for the new Brazilian rural***, with emphasis on the ***rural tourism policy*** as an alternative for generating new business opportunities and occupations in the rural environment.

In order to fulfill the described objectives, 20 research subprojects, eight doctoral dissertations, seven master's theses, in addition to several scientific initiation projects were outlined. Our research project currently involves 45 people, including university professors, professionals of various origins and undergraduate and graduate students, distributed across 20 research institutions in 11 states of the country, 25 of them with a doctorate degree or higher.

In addition to case studies, in 2002 /we intend to start analyzing data from the 2000 Demographic Census, which will allow us to treat less than the meter/non-meter cut allowed by the PNADs, such as micro-regions, basins and even municipalities.

NOTES

1. Thematic project called ***Characterization of the New Brazilian Rural, 1981-95,*** which has partial funding from FAPESP and PRONEX-CNPq, which aims to analyze the main transformations that have taken place in rural areas in 11 units of the Federation (PI, RN, AL, BA, MG, RJ, SP, PR, SC, RS and DF). Visit our ***homepage*** on the ***internet*** (http://www.eco.unicamp.br/projetos/rurbano.html).
2. In ***phase I***, the types of occupations of people living in rural areas were basically explored; in ***phase II,*** the income of agricultural, pluriactive and non-agricultural families residing in rural areas. The main publications are available on our ***homepage*** and in a four-volume collection organized by C. Campanhola & J. Graziano da Silva, ***O novo rural brasileiro: uma análise nacional e regional.*** Jaguariúna, Embrapa- Meio Ambiente/IE-Unicamp, 2000.
3. By imputing the value of agricultural self-consumption and discounting rent payments and the provision of home ownership, when applicable, this methodology adopted by the World Bank was developed by M. Takagi; J. Graziano da Silva & M. Del Grossi,***Pobreza e fome: em busca de uma metodologia para quantificação do fenômeno no Brasil.*** Campinas, Instituto de Economia/Unicamp (text for discussion 101, www.eco.unicamp.br/publicacoes).
4. Unfortunately, there are increasing indications that population count data are heavily underestimated. In the case of rural areas in the interior of São Paulo, for example, the underestimation is evident when there is a general increase in population growth rates between 1996 and 2000, after having shown strong drops between 1991 and 1996. As the 1996 count was carried out together with the 1995-96 Agricultural Census and there is another survey for rural areas in São Paulo in the same period (LUPA), it is possible to highlight the most affected regions.

Marcio Capovilla/Abril Imagens

The rural is deeply related to the urban that adjoins it.

CHAPTER 18

PROMETHEUS BOUND: Brazil in the world industry at the beginning of the 21st century

Mariano Laplane
Fernando Sarti [1]

Introduction

Since the second half of the 1970s, the industrial dynamics at the international level have been Schumpeterian. The combination of technological and organizational changes, corporate mergers and acquisitions, construction of international supply networks, and geographical shifts in production capacity have fueled the vigorous expansion of world industrial production since the second half of the 1980s.

In the 1970s, Brazil completed an important stage of its industrialization process. Since then, the debate about the industrial development strategy has registered antagonistic positions: on the one hand, those who believe that neoliberal reforms, added to macroeconomic stability, constitute sufficient conditions for the Brazilian manufacturing industry to insert itself positively into the new dynamics of world industry; on the other, those who argue that, in order to achieve results comparable to those of successful international experiences, it would be necessary to articulate a set of measures aimed at the deliberate construction of competitiveness, through joint strategies between the State and the private sector.

The debt crisis in the early 1980s induced a strong bias in economic policy. The need to generate significant trade surpluses to face the retraction of foreign sources of financing established as priorities the containment of imports and encouragement to exports. In the second half of the decade, during the New Republic (i.e., the post-military dictatorship period), there was a deliberate effort to capture opportunities in the new frontiers of innovation. The strategy prioritized strategic technologies for developing the competitiveness of the Brazilian manufacturing industry: information technology, biotechnology and, to a lesser extent, new materials. The large national groups timidly rehearsed some diversification moves towards the electronics complex,

1 Núcleo de Economia Industrial e da Tecnologia (NEIT), of the Unicamp Institute of Economics.

taking advantage of the positions already consolidated in the sectors of industrial inputs, in the financial system or in the heavy mechanics segment, implemented in the II PND (the 2nd National Development Plan). However, the decade was marked by strong macroeconomic instability and relatively low levels of investment, both by national, public and private companies, as well as by foreign ones. Thus, the context was not favorable for sustaining more ambitious industrial development strategies.

In the 1990s, changes in international finance and frustration with the "Lost Decade" created a favorable context for testing the neoliberal strategy for stabilization and development in Brazil. With inflation defeated, it was believed that the new strategy would start a wave of intense productive modernization, particularly in manufacturing industry. Industrial production in Brazil would be strengthened. The fittest companies would survive the competitiveness challenge.

Corporatist interests, seen as the main responsible for the stagnation, would be disarticulated. The country could rely on the generous aid of foreign capital, whose financial support, technology and knowledge of the new rules of the game of the globalized economy, would be essential in the new phase of growth[2].

The new policy for the industrial sector marked a paradigm shift in relation to the policy implemented in the developmental period: trade opening, elimination of subsidies, flexibilization of rules for foreign capital and privatization of the productive sector and state infrastructure. It was essential to promote competitiveness through market mechanisms. The ***a priori*** choice of strategic industries and companies became anathema. Instead of sectoral policies, "horizontal" policies should be implemented, which would simultaneously encourage all sectors of the manufacturing industry to produce at price and quality conditions compatible with the global market.

In this general context of neoliberal orientation, there were some exceptions, in the first half of the 1990s. At the beginning of the decade, the seriousness of the crisis resulting from the failure of the Plano Collor opened space for the installation of Sectorial Chambers, which acted as spaces for negotiation between businessmen, workers and the government for the reactivation of industries. Mercosur granted preferential treatment to trade opening at the regional level. Some industries, such as automobile, were subject to special protection regimes to promote local production and investment.

2 Mendonça de Barros; Goldenstein. Avaliação do processo de reestruturação industrial brasileiro. *Revista de Economia Política,* v. 17, n. 2 (66), 1997a; Mendonça de Barros; Goldenstein. Reestruturação industrial: três anos de debate. In: Vellosso, R. (Org.). *Brasil:* desafios de um país em transformação. Rio de Janeiro, Forum Nacional/José Olympio Editora, 1997b; Moreira, M. M. A indústria brasileira nos anos 90: o que já se pode dizer? In: Giambiagi, Fábio; Mesquita, Maurício Moreira (Org.). *A economia brasileira nos anos 90.* Rio de Janeiro: BNDES, 1999. p. 293-332.

The 1999 crisis also brought changes. In the second term of the Fernando Henrique Cardoso administration, the Ministry of Development, Industry and Commerce developed an unequal struggle with the Ministry of Finance to implement some form of Industrial Policy. The efforts resulted in the implementation of the "Foro de Competitividade" (Competitiveness Forum) experience. It was a test of coordination between the main actors in the production chains. Instead of aiming at the reactivation of industries, such as the Sectorial Chambers, the intention was to promote competitiveness so that the Brazilian industry could face the new opening rounds that would result from the ongoing international negotiations (FTAA and Mercosur-European Union Agreement). Despite Development's initiatives, the Ministry of Finance maintained the veto of the Industrial Policy until the end of FHC's second administration.

The manufacturing industry's response to the FHC administration's options will be analyzed in detail later. It is enough for this introduction to note that, although from a microeconomic point of view, there has been a rapid reaction to changes in relative prices resulting from economic policy (high interest rates and an overvalued exchange rate, from 1994 to 1999) with a strong increase in productivity and competitiveness, from the point of view of macroeconomics the low level of investment in manufacturing industry and the resulting trade deficits were totally unsustainable. In terms of dynamism, the results were totally disappointing, with growth rates much lower than those of industries in other developing countries.

From 2003 onwards, the Lula administration, on the one hand, effectively lifted the veto of industrial policy, implementing the "Industrial, Technological and Foreign Trade Policy" (PITCE), but on the other hand it maintained the economic policy regime. As will be detailed later, the results were also insufficient compared to those obtained by developing countries competing with Brazil.

When the performance of Brazilian manufacturing industry is evaluated from a long-term perspective and in a comparative manner with other developing countries, it becomes evident that the picture is far from satisfactory. In the period that began with the debt crisis to date, Brazil has not been able to keep up with other countries in taking advantage of the opportunities that changes in world industry offer to developing countries.

Bounded, as Prometheus in Aeschylus's play, by its inability to resume industrial development, Brazil wastes available opportunities in a favorable international context. The wasted opportunities in this period can be measured by the advance of countries that, not so long ago, lagged Brazil in terms of stage of industrial and technological development.

The concern with lost opportunities may seem contradictory with the observation of the significant modernization effort carried out by Brazilian industrial companies since the opening of the economy, their ability to survive in unfavorable macroeconomic conditions, the incipient internationalization movement of national companies that survived the wave of acquisitions by foreign investors, and the high levels of profitability of large industrial companies. It is not, however, about questioning the performance or individual strategies of industrial companies, it is about evaluating the performance of the manufacturing industry as a whole from the point of view of its contribution to growth and to the strengthening of the insertion of the Brazilian economy in the international scene. From this point of view, wasted opportunities represent a loss for the country as a whole, although not necessarily for individual companies or industries.

The criterion for evaluating the degree of success of any industrial development strategy for Brazil must be the reduction of the distance that separates us from other developing countries, that have been able to take advantage of the opportunities offered by transformations in manufacturing industry and the world economy. From this point of view, the neoliberal strategy must be evaluated as a resounding failure. Likewise, the attempts at industrial policy in recent years can be characterized as insufficient.

The argument summarized above unfolds, in this work, into four sections. The first analyzes the performance of the Brazilian manufacturing industry from the 1990s to the present, with the aim of characterizing the responses to changes in economic policy. In the second part, recent essays on industrial policy are discussed with the intention of identifying their limitations. The third section compares the performance of Brazilian manufacturing industry with that of other developing countries with the objective of measuring the growing distance that results from wasted opportunities. The last section summarizes the argument.

1. Brazilian manufacturing industry performance, 1990-2005

There were notable differences in the performance of industrial production between the first and second half of the 1990s (Graph 1). In the first, there was a recovery after the strong retraction associated with Plano Collor. Recovery began in 1992 and continued until 1995. In the second half, the most striking aspect was the strong instability. The growth of industrial production was frequently interrupted by downturns that drastically reduced production levels. The industrial production index reached its highest values in 1997, 2001 and mid-2002, only to suffer sharp falls in the following months. In moments of peak, the level of production in Brazilian manufacturing industry was only slightly higher than that of the "Lost Decade."

Although official explanations blamed "exogenous" factors (crises in Mexico in 1995, Asia in 1997, Russia in 1998, exchange rate devaluation in 1999 or the "Blackout" in 2001) for the instability and the modest growth of the manufacturing industry in that period, the unsatisfactory results obtained were, in large part, a consequence of the productive transformations that took place. In other words, regardless of the role of exogenous shocks, changes in the productive structure are important explanatory factors for the poor performance of industrial production. These transformations were, in turn, induced by the logic of neoliberal reforms and the orientation of economic policy. With modest export performance, the slowdowns were, above all, associated with the vicissitudes of domestic demand.

Graph 1 – Production and employment indices in the manufacturing industry (2002=100)

Source: Ipea.

Throughout the 1980s, Brazilian manufacturing industry was subjected to successive shocks in a context of strong macroeconomic instability. The companies reacted by reorienting growth strategies to the foreign market, reducing indebtedness levels, increasing markups, making localized investments (in the export industries) and of a defensive type (rationalization and modernization of existing capacity), to the detriment of investments in expansion or installation of new production units. In terms of industrial structure, the results were the deepening of structural heterogeneity between industries, within industries (between exporting and non-exporting companies), and between firms (between modernized and non-modernized products and production lines).

The adjustment in the 1990s was even more intense. The companies reacted to the opening and to the economic policy, deepening the specialization and rationalization of the productive capacity, with a strong reduction in employment (Graph 1). The adjustment was carried out with low investment, introducing organizational changes and abandoning product lines. Brazilian companies sought foreign partners to establish agreements to complement imported product lines and provide services in the domestic market.

The adjustment showed marked inequalities between industries, between companies and even within companies. The overvaluation of the exchange rate and high interest rates made industrial companies look for shortcuts to quickly improve their competitiveness, updating products, replacing national inputs for imported ones and modernizing equipment. Paradoxically, the rapid improvement in the efficiency of local producers (both national companies and subsidiaries of foreign corporations) was facilitated by the relative technological backwardness accumulated in the 1980s, particularly in industries aimed at the domestic market.

Once again, the Brazilian manufacturing industry reaped the benefits of its latecomer condition. In contrast, once again local producers were restricted to imitating advances previously developed abroad and, with rare exceptions, did not make genuinely innovative efforts. The typical forms of technological updating consisted in the adoption of "incorporated" technology in product projects and in equipment acquired abroad[3]. Imports were, from the companies' point of view, the shortest and cheapest way to gain access to innovations "available" abroad and to increase its competitiveness.

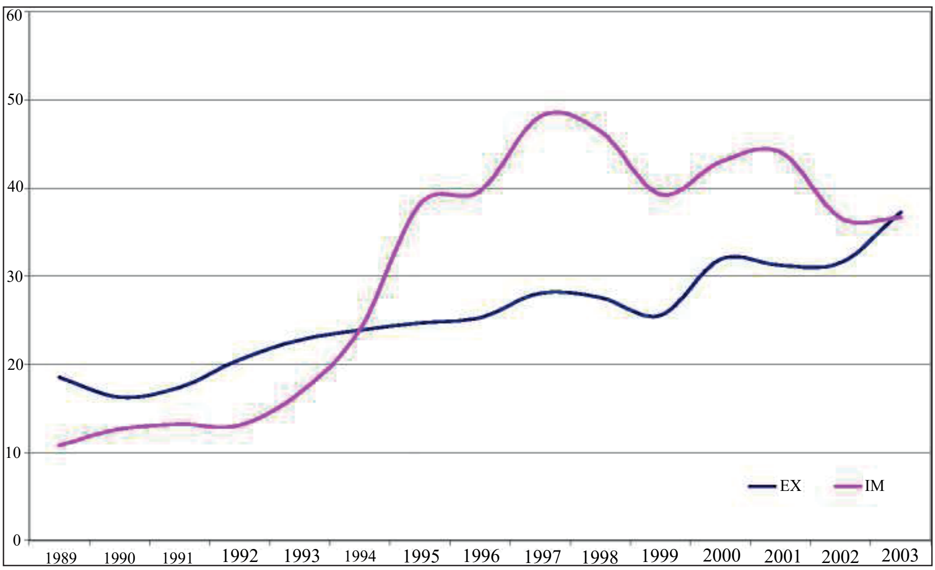
Companies abandoned all activities in which increased competitiveness could not be achieved with the speed and economy of investment required by the overvalued exchange rate and the high interest rate. Regardless of the immediate gains in productivity that these movements may have generated, the consequence, from the point of view of the structure of industrial production in Brazil, was the specialization in activities that are intensive in natural advantages or with less exposure to foreign competition. The disarticulation of production chains and the abandonment of more innovation-intensive activities characterized a process of "regressive specialization" of Brazilian industrial production[4]. The main exception was the metal-mechanics production chain, which combined natural resources (mineral extraction), technology and scale (steel) and other advantages built by public policies, in line with the strategies of foreign subsidiaries (automotive complex).

3 Tigre, P. B.; Cassiolato, J. E.; Souza Shapiro, M. H. de; Ferraz J. C. Mudanças institucionais e tecnologia: impactos da liberalização sobre o Sistema Nacional de Inovações. In: Baumann, R. (Org.). *Brasil:* uma década em transição. Rio de Janeiro: Editora Campus, 2000.

4 Coutinho, L. A especialização regressiva: um balanço do desempenho industrial pós-estabilização. In: Velloso (1997b).

At the same time, the expansion of industrial production began to demand a greater amount of foreign exchange. The transformation of the trade surplus in manufactured goods in the first half of the decade, into a deficit, as of 1995 (Chart 2), clearly signaled the difficulties in sustaining the economy's growth trajectory. The negative balance of trade was more expressive precisely in 1997, at a time of greater expansion of industrial production, reinforcing the interpretation that the growing imported content in industrial products was a factor that aggravated the deficit.

Graph 2 – Exports and imports of manufactured goods (in USD billions)



Source: UNCTAD.

Exports of manufactured goods increased progressively over the decade, but as the pace of growth in imports was higher, deficits were significant. The optimistic expectation that commercial opening would induce an investment cycle that would promote an export drive, accompanied by a progressive import substitution, did not materialize. On the other hand, the conditions of international finance after the Russia crisis generalized the perception that the deficit in the current account of the Balance of Payments was unsustainable. Thus, the exchange rate devaluation at the beginning of 1999 became inevitable. After the devaluation, the trade deficit in manufactured goods decreased until it disappeared in 2003 (Graph 2).

An aggravating factor for the external vulnerability was the process of denationalization of the manufacturing industry that took place in parallel with the trade opening. The acquisition of domestic companies by foreign companies was stimulated by the privatization process, the exchange rate overvaluation, and the interest rates differential. Acquisition of national companies by foreign ones occurred particularly in the services sector, but the advance of foreign companies in economic activity was generalized. In the manufacturing industry, denationalization increased sharply in the industries of processed food, packaging, auto parts, household appliances and cement.

Denationalization increased the demand for foreign exchange from industrial activity in Brazil, as the remittance of profits and dividends by foreign companies came to add to the increase in expenditure on imports of final goods, capital goods and components, as well as the increase in technology imports. The increase in the total demand for foreign exchange associated with the expansion of industrial production, both as a result of imports of goods and services, as well as remittances of profits and interest from foreign companies, aggravated the pressure on the current account of the Balance of Payments.

It is true that, in theory, the total foreign exchange demand of industrial companies, national and foreign, could have been more than covered by the foreign exchange flow generated by exports and, in the case of foreign companies, by the inflow of foreign resources for investment. This was, in fact, the expectation of national authorities and government managers, at least in the first Cardoso term. The exchange rate devaluation of early 1999 was, in a way, an acknowledgment that reality had frustrated these expectations.

The expected resumption of investment did not materialize either. Surveys carried out by CNI in partnership with Cepal showed that there was a short-term increase ("mini-cycle") of investment between 1996 and 1998, with a focus on rationalization[5]. Foreign companies concentrated their resources on the acquisition of national ones, and investments to create new productive capacity ***(greenfield)*** were relatively scarce. The automotive and telecommunications equipment industries were the ones in which foreign investors built new facilities and significantly expanded productive capacity.

The large national groups concentrated their resources on the reorganization of assets in the industries of privatized intermediate inputs (steel and petrochemicals). High indebtedness constrained their investment levels in the second half of the 1990s. Despite the acquisitions made, the scale of the large national groups remained relatively small compared to international competitors.

In 2003, the change of administration marked a radicalization of the use of monetary policy to control inflationary pressures. From the manufacturing

5 CNI/Cepal. Investimentos na indústria Brasileira 1995/1999, características e determinantes. Rio de Janeiro: CNI, 1997. Mimeografado; Bielschowsky, R.; Abicalil, M. T.; Oliveira, J. C. de; Soares, S.; Wohlers, M. Formação de capital no ambiente das reformas econômicas brasileiras dos anos 1990: uma abordagem setorial. In: Baumann (2000).

industry's point of view, the positive news was the sharp exchange rate devaluation at the end of FHC's administration, which contributed to zeroing the trade deficit in manufactured goods in 2003 (Graph 2). The manufacturing industry's performance in the first year of the Lula administration was disappointing (Graph 1) but improved significantly in the following year. Industrial growth in 2004 was accompanied by employment growth, reversing the trend verified in the adjustment since the 1990s.

With monetary policy recurrently curbing domestic demand growth, the main stimulus for expanding industrial production could only come from abroad. In addition to the favorable exchange rate, the demand for inputs from fast-growing Asian economies (notably China) contributed to the increase in Brazilian exports, including manufactured goods. The expanding external demand caused a significant increase in exported quantities, to a lesser extent, in prices (Graph 3).

The favorable evolution of manufactured exports, in addition to boosting industrial production, drastically altered the situation of the Brazilian trade balance (Table 1). In 2002, the small deficit in trade in manufactured goods (labor and natural resources-intensive products or with some degree of technological intensity) was financed with a part of the surplus in primary commodities. In 2005, the balance of all manufactured goods was in surplus, despite the high deficit in products of high technological intensity.

Graph 3 – Price and quantum indexes of manufactured exports (1996=100)

Source: FUNCEX.

Table 1 – Trade balance by product type (in USD million)

	1999	2002	2005
Primary Commodities	14,682	17,833	39,686
Labor and Natural Resources Intensive	3,256	4,856	7,624
Low Technological Intensity	2,123	3,046	8,411
Medium Technological Intensity	-6,639	-3,942	4,342
High Technological Intensity	-10,532	-7,524	-11,532
Others	-4,088	-3,783	-3,774
Total	-1,199	13,125	44,757

Source: SECEX. Elaboration: NEIT/IE/Unicamp.

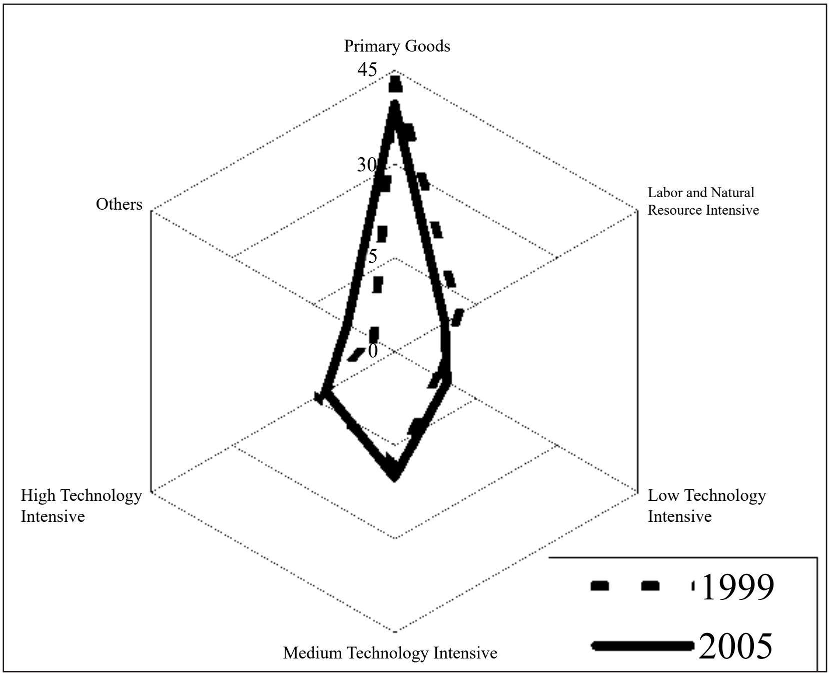
The ability of the Brazilian manufacturing industry to generate favorable results in the trade balance in recent years results not only from exchange rate conditions (increasingly unfavorable since 2005), but also of its peculiar international insertion. Since the opening of the economy and the adjustment of the FHC years, the manufacturing industry, a traditional importer of equipment, also became a strong demandant for parts and components for the assembly of durable consumers goods in the country. Thus, the volume of imports depends on the level of investment and, in general, on the level of domestic industrial production. For this reason, the demand for imports of manufactured products has remained relatively low.

On the export side, the Brazilian manufacturing industry performs well in labor-intensive products as well as natural resources-intensive ones (footwear, furniture and plywood and veneer wood), products of low technological intensity (semi-manufactured iron or non-alloy steel products, cast iron, flat laminates and ferroalloys), of medium intensity (passenger cars, parts for motor vehicles and for vehicles for transporting goods) and of high intensity (airplanes and helicopters, cell phones and undenatured ethyl alcohol and ethylene polymers in primary forms)[6].

Since the opening of the economy and the adjustments in the 1990s, the main component of the export basket is primary products, which represent around 40% of total exports. The sum of the various types of manufactures represents approximately the same value. The composition of the basket has been relatively stable, although there are changes from one year to the other (Graph 4), mainly in the participation of different types of manufactured goods.

6 For an analysis of the structure and evolution of the list of manufactured exports, see the *NEIT* Bulletin, available at:www.eco.unicamp.br.

Graph 4 – Exports by product type - 2005

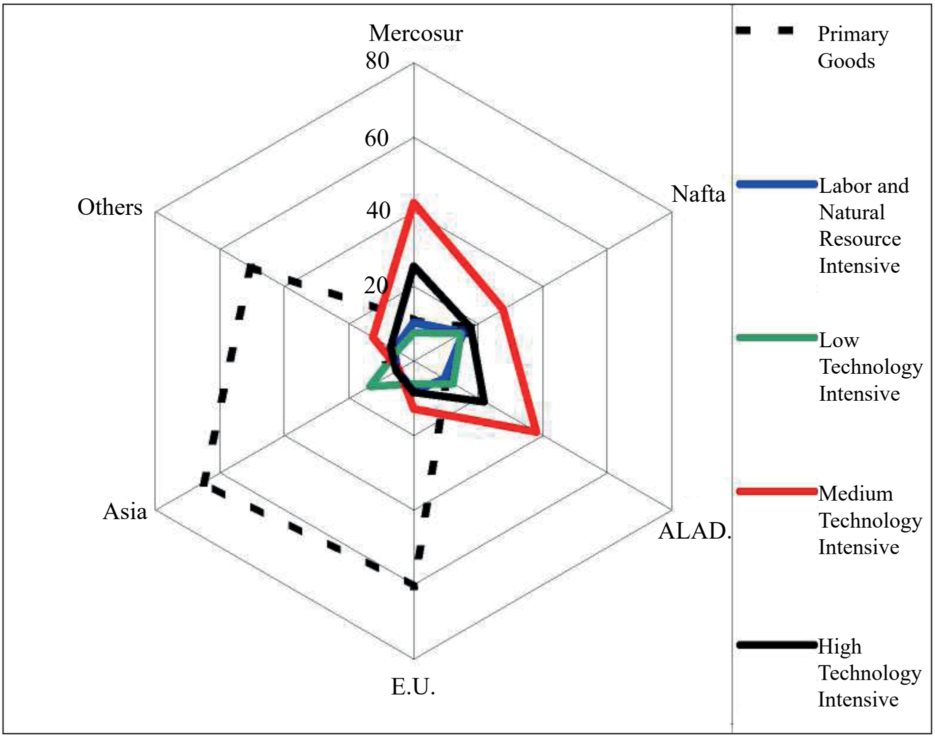


Source: Secex. Elaboration NEIT/IE/Unicamp.

The destination of the different types of products is regionally differentiated (Graph 5). Exports of primary products are predominantly destined for countries in Asia and the European Union. NAFTA, Mercosur and Aladi countries are the privileged market for high and medium technological intensity products. Thus, trade with Asia and the European Union is predominantly of the inter-industry type, while with NAFTA, Mercosur and Aladi it is relatively more intra-industrial. In terms of exports to the Americas, trade agreements (Mercosur, Aladi and the agreement with Mexico) are decisive, in addition to the commercial strategies of Brazilian subsidiaries of multinational corporations.

Thus, the good performance of Brazilian exports depends both on sustaining the demand for primary commodities in Asia and the European Union, as well as on maintaining the role of subsidiaries of foreign companies as suppliers of medium and high intensity products to the Americas. The importance of intrafirm exports by foreign subsidiaries for the trade balance of manufactured goods is significant. The reversal of the trade deficit in manufactured goods, as of 2003, is largely a consequence of the significant increase in exports by subsidiaries of the automotive chain, mainly to NAFTA. The high level of idleness, the technological updating of the plants built in Brazil in the second half of the 1990s, the favorable exchange rate and the trade agreements with Mexico contributed to the increase in foreign sales of these subsidiaries.

Graph 5 – Exports region of destination and by type of product - 2005 (%)



Source: SECEX. Elaboration: NEIT/IE/Unicamp.

Although during the Lula administration there was a substantial improvement in the performance of the trade balance, it should be noted that from a structural point of view there were no significant changes in the Brazilian manufacturing industry. Manufacturing industry continued to be subject to periodic monetary policy shocks stopping the expansion of domestic demand, with investment levels restricted by the lack of prospects for sustained growth. As of 2004, there was a significant improvement in the companies' profitability and capacity for accumulation, but there was a scarcity of investment opportunities. Foreign subsidiaries increased their remittances abroad. National companies that depended on the domestic market to sustain their expansion increased their sales and investments abroad, looking for alternative markets. Resources that could have been earmarked for investment were distributed in the form of dividends or transformed into financial investments to increase non-operational profit.

The performance of manufactured exports was supported by relatively low investments. There was an expansion of capacity in the export sectors of industrial inputs (steel, aluminum, cellulose pulp). In the case of medium technological intensity goods, exports took advantage of excess capacity in the automobile industry, inherited from the Automotive Regime. The increase in exports of high-tech products was made possible by Embraer's investments and the installations of foreign subsidiaries to assemble cell phones, attracted by the boom in the consumption of this equipment in the domestic market and by incentives.

The balance of the performance and transformations of the manufacturing industry shows more continuity than rupture between the FHC period and the Lula administration, a result of the maintenance of the basic orientation of the economic policy. In a panoramic view, the table shows that the industrial sector carried out an intense adjustment during the two administrations, with an increase in competitiveness, but was unable to resume a trajectory of sustained expansion.

This problem cannot be considered just a reflection of the transformations that took place at the same time worldwide. They cannot be treated as the inevitable consequences of the "Third Industrial Revolution" or "Globalization." The transformations that took place in Brazilian manufacturing industry in the 1990s, particularly during the FHC administration, but also during the Lula administration, were a consequence of the combination of international trends with conditions peculiar to Brazil, strongly influenced by the orientation of economic policy.

Brazilian industrial production underwent successive expansions in an exceedingly short breath. During the FHC's administration, severe restrictions on foreign financing acted against the continued expansion of industrial production. Were it not for the fact that the expansion of industrial production itself aggravated external fragility, these restrictions could be considered exogenous. The endogenous roots of restrictions on industrial growth are associated with the characteristics of the modernization strategy adopted by industrial companies, in response to stimuli established by the administration itself. Specialization aggravated by denationalization established a strong restriction on the continued expansion of Brazilian industrial production, as it accentuated external vulnerability. Thus, in the late 1990s, Brazilian manufacturing industry found itself in the paradoxical situation of having significantly improved its competitiveness without, however, having managed to contribute to alleviating the main obstacle for its continued expansion: the foreign exchange restriction. In practice, the strategy of adapting to the distortions of economic policy and the open economy adopted by the manufacturing industry itself aggravated the problem, that is, the pattern of internationalization, instead of removing obstacles to development, aggravated them.

The FHC administration chose to define the macroeconomic conditions and let the companies themselves choose the most adequate strategy for their needs. It was intended, in this way, to avoid the errors attributed to state intervention in the period of developmentalism. It was expected that the increase in demand for foreign exchange from industrial companies, both domestic and foreign, would be resolved due to the increase in competitiveness that would allow for expansion of exports. The currency crisis of 1999 made it evident that the strategy of carrying out the modernization of manufacturing industry with only the instruments of macroeconomic policy, as the neoliberal vision intended, was a resounding failure.

The industrial and technological policy, which could have conducted the process with greater efficiency and at a lower cost of foreign exchange, income, and employment, was belatedly rehabilitated in an attempt to bring the Brazilian economy and manufacturing industry out of the impasse. Even so, until the end of the FHC administration, the Ministry of Development's initiatives were blocked by the Ministry of Finance.

Under Lula's administration, external restrictions significantly diminished, but economic policy continued to curb any chances of reactivating domestic demand in order to stabilize prices. The monetary policy not only restricted growth, but also aggravated the fiscal situation, hampering the availability of resources for investment and development.

2. The Industrial, Technological and Foreign Trade Policy (PITCE)

Since the 1930s, Brazil has implemented policies aimed at promoting industrial development. The results were, in relation to the experiences of other developing countries, significantly favorable, in the sense that in the beginning of the 1980s, Brazil had a diversified and relatively integrated industrial structure. During this period, industrialization was the driving force behind the development of the Brazilian economy.

Mechanisms to promote industrial development were varied. In general, instruments aimed at promoting the accumulation of capital in manufacturing industry predominated. Industrial investments were directly stimulated with subsidized financing by the public sector, and indirectly, by improving the relative profitability of industrial enterprises through tax mechanisms and initiatives to protect the domestic market.

In the post-war period, several bodies were created with the function of coordinating government initiatives and regulating the actions of the private sector (Work Groups, Executive Groups, Councils, etc.). The National Bank for Economic and Social Development (BNDES) was also created.

In the 1960s, the issue of reducing regional inequalities and the spatial concentration of industrial development gained importance, and as such specific bodies and mechanisms were established for this purpose.

The most direct and intense public intervention took place in the 1970s when efforts focused on the implementation of heavy industry (industrial inputs and capital goods). There was also a special program for the telecommunications sector aimed at articulating the expansion of infrastructure with foreign investment in the production of equipment, with the transfer of technology to private national companies and the development of national technology by state-owned service providers. At the same time, as a reaction to the oil shock, there was a change in the energy matrix in favor of hydroelectricity, the exploration and extraction of oil, and the production of alcohol as a fuel for motor vehicles.

The debt crisis in the early 1980s established new priorities in the formulation of Brazilian industrial policy. The need to generate significant trade surpluses to face shrinking foreign sources of financing shifted the policy emphasis in favor of an effort at import substitution and export promotion. Administrative systems were put in place to restrict imports and mechanisms were established to promote export growth. ***Ad hoc*** instruments were created to offset the anti-export bias of the policy implemented in previous decades (***draw-back*** regime, tax incentives and various forms of subsidies to exporters). At the same time, new rules were established so that private companies could pay their debts in foreign currency.

In the second half of the 1980s, with the return to democracy, an attempt was made to order the complex universe of instruments inherited from the five decades of support for industrialization. This attempt was shaped by the economic chapter of the 1988 Constitution and in the subsequent legislation that regulated the main articles. The creation of the Ministry of Science and Technology and the attempt to explicitly articulate industrial and technological policy in high tech industries also date from this period. The most notorious example was that of the National Informatics Policy.

In the 1990s there was a break in relation to the trajectory of the previous fifty years. In general terms, the change consisted in reducing the role of instruments with a differentiated sectorial scope (vertical) in favor of horizontal instruments. Thus, non-tariff protection instruments were eliminated, sectoral differences in tariff protection levels were reduced and subsidies were eliminated. The conditions for financing investments were also more uniform for all industries. Within this framework of horizontal interventions, the exception was the assembly sector of the automobile industry, which received differentiated favorable treatment between 1995 and 1999. From the year 2000 onwards, only the undertakings of the assemblers carried out in the Northeast, North and Midwest regions continued to receive incentives.

At the same time, many of the coordination and planning bodies that played an important role throughout the industrialization process were dismantled or disassembled during this period (interministerial councils, planning bodies, etc.). The privatization of public companies also dismantled planning and coordination instances in the infrastructure sectors, only very partially re-established by regulatory agencies.

After the currency crisis of 1999, there was a greater emphasis on supporting exports, mainly through the supply of domestic financing, compatible with international conditions, and the progressive elimination of taxes and fees that affected their competitiveness. In the case of the agricultural sector, financing was offered under special conditions to promote investment in agricultural machinery and equipment, tractors, harvesters, etc. under the BNDES' Moderfrota Program. Funds were also established to finance innovation activities (Sectorial and Technological Development Funds), based on contributions from the private sector. In all these cases, interventions were defined as necessary to correct tax distortions or in the financing conditions offered to national producers (levelling the playing field).

Despite the obvious change of course, the legacy of the 1990s cannot be characterized as a tabula rasa in relation to previous decades. First, because despite the profound changes, a set of institutions and instruments inherited from previous decades survived, in harmony with those created in the 1990s. Secondly, because after the currency crisis of 1999 there were some isolated initiatives to minimize some of the distortions generated by the economic policy (monetary and fiscal regime), as seen above.

Thus, the "old" agencies responsible for promoting regional development (Sudam, the Superintendency for the Development of the Amazon and Sudene, for the Northeast), the incentives and the Constitutional Funds for Financing the Midwest, North and Northeast Regions (FCO, FCA, and FCNE, respectively) survived[7]. The BNDES, as well as the other two large financial institutions of the federal government, Banco do Brasil and Caixa Econômica Federal, also survived, although with some of their functions reformulated. The same happened with SEBRAE and other institutional arrangements created in previous decades.

In 2003, the Lula administration began formulating a new policy: the Industrial, Technological and Foreign Trade Policy (PITCE). By the end of 2005, this process had resulted in a very comprehensive set of initiatives,

7 Although they were subject to changes at the end of FHC's administration.

in very heterogeneous stages of planning and implementation. Horizontal actions strongly predominated, some of which represent new actions (such as the Modermaq Program, from BNDES, inspired by the success of the Moderfrota Program, which replaces variable interest rates with fixed rates in financing), while others were adaptations of preexisting programs (such as support programs for small and medium enterprises).[8]

There was an effort to exempt taxes on investment, production, and exports. The IPI rates for capital goods were zeroed (Decree no. 5468, of June 15, 2005). The tax equality between imported and domestic products was established, applying the Cofins contribution to the former. The exemption from the contribution to PIS/Pasep and Cofins was approved for the purchase of machinery and equipment by exporting companies that exported at least 80% of their production (Law n. 11,196 of November 21, 2005).

Additionally, PITCE established that sectoral initiatives would be implemented to strengthen the production of semiconductors, pharmaceuticals, software and capital goods. Despite this announcement, these industries were not the object of large-scale development actions, although they were the object of specific BNDES Programs (Modermaq, Prosoft and Profarma, for example). The most visible sectorial initiative was the exemption from contribution to PIS/Pasep and Cofins, incident on the retail sale of microcomputers (Law n. 11,196, of November 21, 2005). Also, in the field of microelectronics, the government is negotiating with the developed countries counterparts in the form of investments and technology transfers for the definition of the Brazilian standard for Digital TV.

The initiatives were not capable of significantly influencing the level of investments, nor of reversing structural problems, but they managed to face problems that had been pending since the FHC administration. The Innovation Law, for example, was enacted in October 2005. The most articulated actions were in the area of export promotion, whose instruments were in the hands of the Ministry of Development and demanded less from the Ministry of Finance.

After more than a decade without any attempt to make industrial policy in Brazil, the difficulties faced by the Federal Government in structuring the planning, implementation and monitoring of development actions could not be underestimated. Perhaps for this reason, the implemented measures were far from being an articulated and finished set.

The PITCE has faced two types of problems since its inception. First, serious difficulties in coordinating government actions. The Federal Law that created the Industrial Development Agency and the National Industrial

8 For a detailed description of the measures implemented after the creation of ABDI, see the PITCE balance in 2005, available at: www.desenvolvimento. gov.br.

Development Council, the responsible bodies for this task, was only approved on December 21, 2004. Even after the Law was approved, it took a long time for the Agency to have the minimum resources to make it work. Second, the rigidity in the use and availability of resources to implement high-impact projects. An important part of the available resources was earmarked for financing exports and the resources available for investment had a high cost for potential investors. Attempts to introduce interest equalization mechanisms in investment credit, similar to those used in export financing (Proex), faced insurmountable resistance from the Ministry of Finance.

Regardless of its limitations, the experience of the Lula administration in formulating and implementing the PITCE leaves important lessons for the future. An important reflection in this regard concerns the relationship between industrial policy and macroeconomic policy. In theory, both are not incompatible; on the contrary, they can and should be implemented simultaneously, generating synergies. This perspective goes beyond the dualistic view that they are exclusionary mechanisms for allocating resources. It also overcomes the simplistic view that industrial policy is inevitably onerous from a fiscal point of view and that it therefore compromises the public accounts equilibrium and price stability itself. On the contrary, a competent industrial policy could help to remove obstacles that eventually restrict the macroeconomic policy effectiveness and undermine stability. These issues are closely linked to the debate in the 1990s, when industrial policy was stigmatized and orthodox monetary and fiscal practices were considered panaceas in promoting growth and development.

The Lula administration set aside prejudices related to industrial policy, starting from a slightly more realistic view of the capacity to promote growth and development exclusively through "responsible" macroeconomic policies. It tried to transfer some of this responsibility to PITCE, but fiscal targets severely restricted the type of instruments and scope of government programs.

Evidently, fiscal restrictions are important constraints on the availability of resources and the viability of some industrial policy initiatives. Restrictive fiscal conditions impose greater selectivity on industrial policy actions and require more modest targets. Thus, paradoxically, short-term fiscal restrictions end up limiting the scope and scale of the contribution that industrial policy could make to improve the macroeconomic environment in the medium and long term and increase the degrees of freedom of economic policy.

Even more serious was the effect of monetary policy, which recurrently aborted any resumption of growth, subjecting the economy to interest rate shocks that aggravated the fiscal situation, increased the opportunity cost of capital and discouraged private and public investments. As if these effects were not enough, the monetary policy also induced, from 2005 onwards, a strong exchange rate appreciation, thus eroding the profitability of manufactured exports. Under these conditions, it is naive to imagine important initiatives that transform the structure of the Brazilian manufacturing industry.

The general characterization of the transformations experienced by the Brazilian manufacturing industry in the previous item shows that, after more than a decade of more intense exposure to international competition, it still suffers from two serious structural deficiencies that severely compromise its expansion possibilities: a) a relative incapacity to generate innovations (recurringly and insufficiently supplied with access to technologies generated abroad); b) serious limitations on access to finance (resulting in heavy reliance on own capital for investments and working capital needs). Both deficiencies, as old as the Brazilian manufacturing industry itself, can no longer be attributed to the closing of the economy or distortions in the import substitution process.

Restrictions on obtaining financing (credit availability and cost, and capital market limitations) force Brazilian industrial companies to compete at a severe disadvantage with those of other countries with more favorable credit conditions and access to third-party capital. The low level of indebtedness is the counterpart of the predominant use of own resources for investment. Self-financing places restrictions on the expansion of industrial companies, limiting their scale and capacity to accumulate vis-à-vis international competitors. As a result, companied with less concentrated equity structures and relatively undercapitalized family businesses are more observed in Brazil than in other industrialized countries.

The replacement of local technological development by imported technology, although it constitutes a useful resource for ***late-coming countries*** such as Brazil, limits the possibilities of increasing domestic and international market shares. The competition with products of mature and widely available technologies requires that Brazilian producers conquer markets with a strong emphasis on lower costs, restricting value addition. The generation of proprietary technology would allow for advancements in product differentiation, leveraging the creation of brands and enhancing value addition and capital accumulation.

Although structural problems affect national companies more intensely, foreign subsidiaries face similar difficulties, as they compete, generally at a disadvantage, with other subsidiaries of their parent company for access to resources for technological development, to expand capacity and export to new markets. The disadvantage of Brazilian subsidiaries stems from their small size in relation to other subsidiaries of the corporation. The vast majority of foreign subsidiaries in Brazil wield a limited degree of autonomy, restricted to projects that can be financed with resources from the subsidiary itself or obtained in the local market.

The role of foreign corporations in industrial development is critical given the advance of denationalization in the 1990s. It is true that for multinational corporations, the stimuli created by the global competitive regime are very important, but the stimuli created by the local regime are not necessarily insignificant and can be exploited to induce behaviors that are more compatible with the objectives of industrial policy.

In this sense, it is worth noting the occurrence, in the second half of the 1990s, of a reversal in the relative performance of industries producing final consumer goods for the domestic market and of intermediary producers for exports. In the 1980s, the former, whose performance was tied to the domestic market, accumulated technological lags and idle capacity. The latter, favored by the exchange rate and by various export incentives, had a more favorable performance and presented higher levels of technological update at the end of the decade.

In the 1990s, the conditioning factors for the relative performance of these two groups of industries changed substantially. The first group benefited from the recovery of domestic demand, the reestablishment of consumer credit mechanisms, and the possibility of replacing local suppliers for imports; with this, performance was improved. The second groups faced an unfavorable exchange rate and trade barriers to expand its sales abroad. The performance of the second group was relatively weaker than that of the first.

In the few cases in which multinational companies (which lead the durable consumer goods industries) faced favorable conditions in the domestic market, with convenient sectoral policies and strong pressures from the local and global competitive regime, they reacted in a non-defensive way; that is, making greenfield investments, renewing products and processes. The most illustrative cases are that of automakers and cell phone assemblers.

It is not, of course, about making the Automotive Regime a model to be implemented in other industries led by multinationals. It is merely a matter of registering that multinational companies are sensitive to macroeconomic conditions, incentives, and conditions of the local competitive regime. In other words, there is room to implement policies that target these companies, in addition to national companies.

PITCE's experience shows that the effectiveness of industrial policy must be evaluated by its ability to put Brazilian manufacturing industry back on a path of sustained growth. To a large extent, it will only be able to achieve this result if it is properly articulated with macroeconomic policy and if it correctly identifies emerging opportunities on the international stage.

3. Wasted opportunities

The ongoing transformations in world industry present opportunities and threats to developing countries. The first are related to the possibility of being able to exploit, in a more open regime of world trade, the cost advantages arising from the availability of natural resources and cheap labor. The threats are linked to the high cost of competing with other countries to attract new investments, especially if the return is relatively low for the local economy in terms of added value.

In this context, developing countries that have some industrial base and a dynamic and large domestic market are the most apt to explore opportunities, minimizing costs, since they have more favorable conditions to attract and internalize the multiplier and accelerator effects of investments in the manufacturing industry. In this group of countries, those that have large companies with national capital, capable of mobilizing resources to invest in productive capacity, technology, international networks and brands, constitute the best positioned sub-group.

In Asian developing countries, the manufacturing industry reveals its ability to promote growth in economies with very different profiles and at different stages of industrialization (Table 2). Manufacturing industry acts as an engine of growth in countries with incipient industrialization, such as Vietnam, Malaysia, and Thailand, but also in countries with more mature and diversified industries, such as India and South Korea. The manufacturing industry promotes growth in relatively small countries with more outward-facing industries such as Malaysia and Thailand, but also in countries with large domestic markets such as China and India. Finally, the manufacturing industry's growth potential reaches both countries that depend on imports of raw materials, such as South Korea and China, as well as those with abundant natural resources, such as Indonesia. These data suggest that there are diverse opportunities available to countries on different development trajectories.

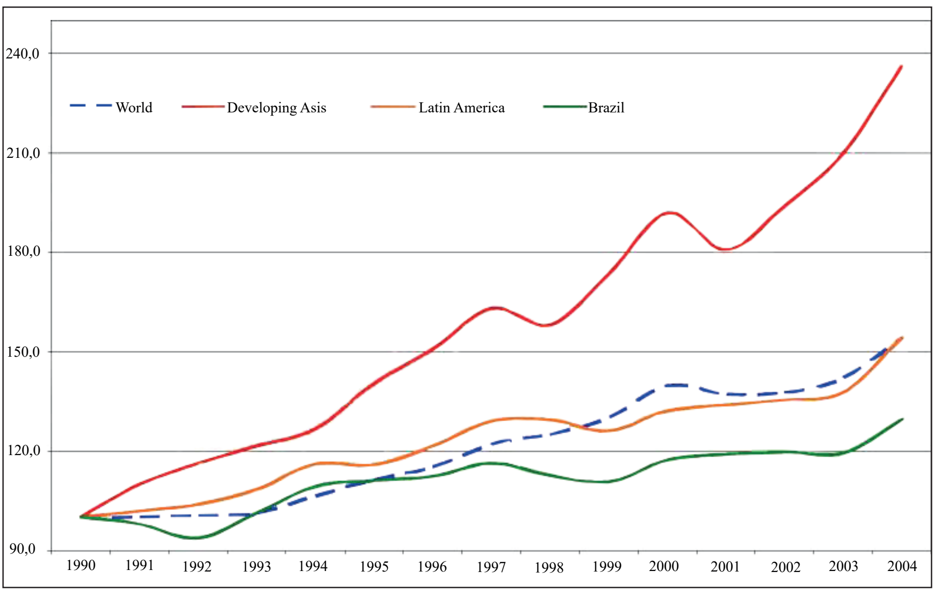
Table 2 – Growth rates: GDP and the Manufacturing Industry 1990-2003 (%)

	GDP	Industry
China	9.6	11.7
Vietnam	7.5	11.2
Malaysia	5.9	7.9
India	5.9	6.5
Korea	5.5	7.4
Thailand	3.7	6.0
Indonesia	3.5	5.5
Brazil	**2.6**	**1.6**

Source: World Bank *World Development Report* (2004).

In Brazil, as seen in the same table, the situation is different: low industrial growth and, consequently, lower GDP growth than in all the Asian countries listed above. The high cost of the inability to resume industrial growth in Brazil is illustrated in Graph 6, which shows that developing countries in Asia doubled their industrial output between 1990 and 2004. In Latin America and the Caribbean countries, the accumulated growth in the same period was only 40%. It should be noted that the Brazilian performance was inferior to that of Latin America over the fifteen years.

Graph 6 – Industrial product growth: 1990-2004 (1990=100)



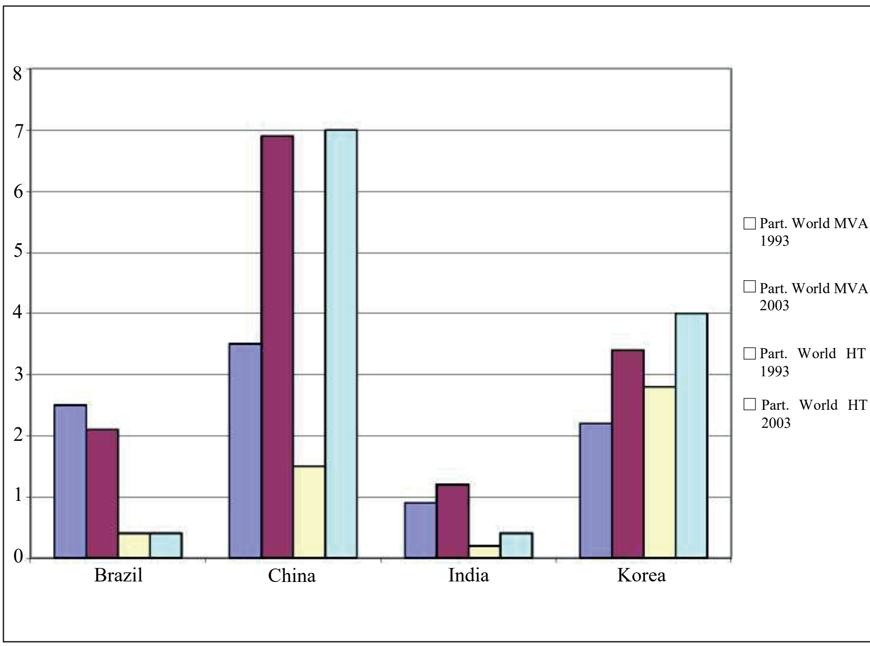
Source: United Nations. Monthly Bulletin of Statistics (various numbers).

It is not just about lost opportunities for the Brazilian manufacturing industry, but about wasted growth potential for the Brazilian economy as a whole. While other countries explored manufacturing industry growth opportunities to leverage the economic growth, Brazil adopted an Olympic attitude, supposedly neutral, which left the field free for competitors and wasted growth potential for the country.

Over the last fifteen years, the countries that compete with Brazil have increased their industrial competitiveness and strengthened their economies through the exploitation of economies of scale, the constitution of global industrial companies, the alliance with multinational companies, the conquest of important market shares in developed economies and the strengthening of the capacity for innovation.

Lost opportunities can be measured by comparing Brazil's ***market share*** with that of competitors in the world industrial product and in the world high technology-intensive product (Graph 7). Brazil's share of world industrial production declined between 1993 and 2003, while that of China, India and Korea increased. In the case of products of high technological intensity, the participation of these countries also increased, while Brazil's remained constant at a very low level (0.4% of the world total).

Graph 7 – Participation in the world industrial product and in the production of high technological intensity goods (%)



Source: Unido.

A consistent combination of macroeconomic regimes that do not impede growth, adequate long-term financing and selective policies to support innovation would have allowed Brazil to seize some of the opportunities captured by other countries. Missed opportunities mean that additional effort must be made in the future to recover the competitiveness of the Brazilian manufacturing industry in relation to its competitors.

Final considerations

The inability to take advantage of existing opportunities in the favorable world context to promote expansion and industrial development partly explains the mediocre performance of the Brazilian economy since the 1990s. Other countries explored opportunities that Brazil was unable to take advantage of and achieved better economic performance.

Brazil has painstakingly built, for fifty years, a complex and sophisticated industrial structure that has shown an incredible capacity to survive in contexts of adverse macroeconomic regimes. Despite its weaknesses, Brazilian manufacturing industry could contribute more to growth and development.

The low growth of the Brazilian manufacturing industry is a consequence of its defensive adjustment, primarily financial and profit margins-related, of industrial companies during a succession of short expansions recurrently interrupted by economic policy shocks since 1994. The agility shown by the companies, especially in the financial sphere, reveals a pronounced survival instinct and aversion to the risks inherent to investing in productive capacity and in technological development.

The non-adoption of bolder expansion strategies meant that the structure of the large national groups did not evolve towards activities with a high technological density and greater growth potential. In the case of foreign subsidiaries, few have made investments that would enable them to participate as global suppliers in the international division of labor established by the headquarters. The exceptions are those inserted in the trade flows to the neighboring countries of Mercosur and Aladi or to NAFTA.

The waste of opportunities for the growth of Brazilian manufacturing industry is a result of the anti-growth bias of macroeconomic policy and the absence of an industrial development strategy in the FHC era. The Lula administration was not able to reverse this situation, despite initiatives to resume the industrial development policy.

CHAPTER 19

(DE)INDUSTRIALIZATION AND (UNDER)DEVELOPMENT[1]

Wilson Cano

Introduction

To carry out a more rigorous reflection on the issue of deindustrialization, one must first consider three fundamental questions: ***i)*** the meaning and composition of the industrial sector, as it appears in the national accounting systems; ***ii)*** the concepts of the development ***process*** and economic underdevelopment; and ***iii)*** the meaning of industrialization in such processes.

The industry sector is an aggregation of four segments: mining; civil construction; public utilities (PU, such as gas, energy, water); and manufacturing industry. It is this last segment that involves greater technological complexity, which enables and promotes the dissemination of greater content of technical progress to other sectors of the economy (agriculture, other industries, and services) and which, in addition, represents approximately 40% of the added value of the industry sector today. In addition to being the main vector of development policies, especially industrial and foreign trade policies, it is also the most susceptible to international competition when faced with crucial adversities such as dumping, long-term financing, access to S&T, overvalued currency, and others. Thus, there is little or no meaning in using the entire industry sector to inquire about possible deindustrialization problems; it is correct to use only the manufacturing segment.

Development is the result of a long process of economic growth, with a high increase in average productivity, without which the surplus does not grow enough to accelerate the investment rate and diversify the productive and employment structure. This process intensifies industrialization and urbanization to progressively transform the country's social and political structures[2]. Furthermore, it will also change and modernize society's habits and customs.

This process, which started in the 19th century, was led by England, and was followed by a restricted group of countries until the beginning of the 20th century, and hence led by the U.S.. It included Japan, Canada, and the main countries of Western Europe and Oceania. The exception was the inclusion of South

1 Text presented at the Second International Congress of the Celso Furtado Center, on 8/18/2014.

2 In the capitalist system, there may be, at the same time, the predominance of authoritarian political regimes leading the process. Economic evolution, however, strengthens the class struggle, expands, and diversifies social interests and conflicts, inducing a process of social and political change towards, at least, a formal democracy.

Korea, thanks to the support and "invitation" from the U.S., in a long process that began in the 1950s and matured in the last two decades of the 20th century.

Underdevelopment, as Furtado (2000) has clearly shown, does not represent a stage of development or a "lower degree of development". It is a process that began with the insertion of other countries in the international capitalist market, notably from the 19th century, and resulted from the capitalist relations of production that were internalized in them, maintaining, however, a promiscuous coexistence with old and predominant precapitalist relationships preexisting in peripheral countries, without extinguishing most of them. Therefore, according to Pinto (1979), there is a perverse accumulation dynamic that is incapable of promoting economic and social homogenization and maintains the economic and social traits of this process, such as structural heterogeneity, latent inflation, and weak foreign accounts, long-term financing, and taxation.

When a country develops, it shows some basic economic indicators that are close to those already obtained by other developed countries: a high level of per capita income and a strong decrease in the participation of the agricultural sector in the gross domestic product (GDP) and in employment. This, in all historical cases, was due to industrialization. Agriculture starts to represent less than 10% of employment due to the more than proportional increase obtained by the sectors of industry and services, which are also expanding thanks to urbanization. The decrease is only relative, since the growth of other sectors and of urbanization forces agriculture to grow, diversify, and modernize, reducing the difference in its results regarding other sectors, thus providing greater economic and social structural homogeneity. If industrialization does not advance and diversify, agricultural modernization will be hampered or will depend on large imports of modern inputs and capital goods.

For this to happen, industrialization has to advance and grow more than other sectors, increase productivity, and change its structure – in the sense of implementing departments of capital and intermediate goods, thus contributing to diversifying the export basket and, if possible, improving foreign accounts. Historically, there is no country that has developed without generalized industrialization and a strong and active role of the National State. This expansion and transformation show a diversified structure in which capital goods make up between 30% and 40% of the added value of the manufacturing industry[3]. It is this remarkable expansion, diversification, and transformation that intensifies urbanization, inducing and demanding enormous growth and diversification of all types of services: trade, transport, finance, health, education, personal and others, not only predominantly linked to domestic consumption but now increasingly interdependent with the needs of agricultural and industrial companies. Upon reaching this high standard, the productive and employment structure

3 On the meaning and composition of this sector in developed and underdeveloped countries, see: Cepal (1965), Furtado (1969 and 2000), Fajnzyilber (1983), Teixeira (1983), and Valderrama (1966).

starts to move toward further expanding, modernizing, and diversifying services, more than agriculture and the manufacturing industry, decreasing the relative weight of both, which lose position for services. This is how deindustrialization should be understood in a positive or normal sense[4].

Very different is the situation that can occur in an underdeveloped country. Many of them also introduced industrialization processes in their territories. Few, however, managed to surpass, with any expression, the production of nondurable consumer goods and the simple industrial processing of primary products. Even in Latin America, only Argentina, Mexico, and Brazil managed to install an industrial park, and of these, only Brazil advanced in the most expressive, albeit partial, creation of the capital goods sector.

This text has two sections. In the next section, I will briefly present some facts and arguments that I believe are relevant for us to understand the meaning of ***normal*** and ***precocious*** deindustrialization. For that, in subsection 1.1 I will analyze data and information about some of the main developed countries and comment about the performance of China; in subsection 1.2 I will make some mentions of the “China effect”, also including some references to India, addressing some of the main countries in Latin America. In section 2, I will discuss the case of Brazil.

1. Normal (or positive) and early (or negative) deindustrialization: considerations about some developed and underdeveloped countries

In 2003, UNCTAD had already exhaustively dealt with this problem, showing that the first case refers basically to developed countries, which, between the 1960s and 1970s, had matured their industrialization processes and maintained a strong manufacturing export presence, especially in capital goods and more complex and advanced technology[5]. In that period, the share of the manufacturing value added (MVA) in the total value added (VA) was approximately 30%, and thereafter, it would be reduced, as seen in Table 1.

1.1 Deindustrialization in some developed countries

With the maturity of these industrializations and their respective urbanizations, the services sector had a strong expansion and diversification and started to grow at higher rates than industrial ones, causing the manufacturing industry to gradually lose weight in the share of GDP. However, this industry not only continued to grow – inside and outside these countries – but also kept its investments high, its S&T development, and the increase of its productivity and its international

4 On the role of industrialization and structural change in development, see: Furtado (2000) and UNCTAD (2003).

5 See UNCTAD (2003). A synthesis, which includes the case of Brazil, is in Rícupero (2014).

competitiveness. This is what, in short, UNCTAD called "***normal*** or ***positive*** deindustrialization". Some countries had their industrial maturity later, such as Italy, in the 1970s. South Korea, not only because it was the most latecomer, continued to increase that share, which, from 18.5% in 1970, today reaches 33.1%.

After the maturation of industrialization in developed countries in the early 1970s, the international economy went into crisis. As it deepened, the American hegemony, helped by England, started what would come to be called neoliberalism and globalization, with the policies of commercial, financial, and labor deregulation (precariousness and lowering of its costs), in addition to social security reforms and the minimization of the role of the State. On the way to the 1980s, in the midst of these policies and the need to face the crisis, the world witnessed the U.S.'s master move, with its draconian monetary policy that broke all internationally indebted countries, having even been the anteroom of the collapse of the socialist regime.

As defense mechanisms to the crisis, there was a strong intensification of international competition, fueled by the constitution and intensification of the so-called "international blocs" (EU, Asia, and later NAFTA and Mercosur, among others). There was then an intense process of purchases, sales, and mergers of international companies, concentrating and centralizing capital even more, triggering huge flows of internal and external investments that would provide the basis for a deep international productive restructuring, the so-called "Third Industrial Revolution". I also remember that since the 1960s, financial capital has been showing a growing presence in the movement of international capitalism, exacerbating its action in the 1970s, and from then on, exercising an unmistakable dominance over it and spreading its harmful effects throughout the world, whose greatest example would come to be the 2007-2008 crisis, which has not been resolved until today.

The set of these facts, embodied in the so-called "globalization," had different effects throughout this period. Among the developed countries, the economic and social effects, positive and negative, were unevenly distributed. Before the outbreak of the 2007-2008 crisis, the huge growth in foreign investment to consolidate the formation of the blocks and the substantial increase in foreign trade provided, to most, positive gains in product growth but also negative gains in distributive inequality. The loss of profits in the parent company home country was compensated – certainly even more advantageously – by the remittances of profits, interest, and royalties sent by its affiliates and associates in the host countries[6]. However, the massive unemployment and the labor precariousness caused in the home country were entirely borne by the working class of the country itself, mitigated, it is true, by the related expansion in services.

6 In addition, of course, to the international financial gains that these same companies – in addition to banks – obtain in the international market.

One must understand that a large part of these "losses" of production in developed countries actually only means a ***geographical displacement of production***, as the home country continues to appropriate a good part of the value added of this production, via recipiency of royalties, profits, and other rights (trademark use, for example). Recent studies on value production chains show much of this phenomenon, drawing attention especially to the production of product processing (***intermediate or final goods***), which account for these remittances and for a large volume of re-exports, masking the effective volume of the international trade in these goods. However, in the last ten years, China has increased its value addition in these processes, thus decreasing appropriation by the home country[7].

However, the structural quality of this growth, whether in terms of employment, production, or consumption, has been little discussed[8]. With the deepening of the 2007 crisis in Europe, the "poor cousins" (the "pigs," as they were called) of this family bore the worst of the burdens, and the pains of their draconian adjustments commanded, in fact, by Germany, are still bitter today. Japan was unable to escape the strong deflation and recession imposed by the U.S. fiscal policy and the readjustment of the value of the dollar, suffering a violent recession between 1990 and 2002 and low growth thereafter until today. The U.S. was the big winner – although its population would suffer a sharp worsening in income distribution and high unemployment – followed by Germany.

The outbreak of these facts exacerbated the debilitation that was already noticed in most socialist economies and was the main vector in the downfall of the regime in those countries. However, in the opposite direction, it is worth highlighting the case of China – the new "guest" of the U.S. since 1971 – which also indirectly contributed to the downfall of the USSR. Favorable political conditions for the U.S. and the relentless pursuit of cheap labor were key elements that – productively – benefited China and some others, notably Asian countries.

Let us see Table 1. It contains data from selected countries: developed, underdeveloped, and China. Its first part presents the average annual growth rates of VA and MVA, and we can summarize our observations as follows:

a) for most developed countries, these rates decreased between 1980 and 2012. The exceptions are South Korea and China, which have higher MVA growth rates than VA ones, which are the result of industrial intensification in these countries. South Korea lowers its rates, but they are still high and the highest among developed countries. China has rates that are even higher than all of them and that suffer a small drop in the post-2007 period. South Korea managed to articulate better

7 See about the topic: De Morais (2012).

8 Without a doubt, I believe that the need for extensive research on structural changes in production and investment is essential for a greater understanding of this deindustrialization.

with the dynamics of China's economy. Although Japan has also benefited from this articulation, it has not managed to overcome some negative effects accumulated during its long crisis since the 1990s.

b) The MVA/VA ratio also decreases for almost all these countries, showing deep drops, especially after the 2007 crisis, placing it, for the U.S., Canada, and Western Europe, between 10% and 12% only. Canada, however, deserves a caveat, which I will comment further on. The large exceptions are Germany (23.8%), leading the EU bloc, and Japan (18.7%), in addition to the already mentioned Korean and Chinese rates, which are more than twice as high as those of most of the selected countries.

Table 1 – Total value added (VA) and manufacturing value added (MVA)

	Average annual VA growth rate(1)					Average annual MVA growth rate(1)					Participation of MVA in VA(2) (%)				
	1970/1980	1980/1990	1990/2000	2000/2007	2007/2012	1970/1980	1980/1990	1990/2000	2000/2007	2007/2012	1970	1980	1990	2000	2012
U.S.	2.70	2.80	3.00	1.90	1.20	1.70	2.50	3.80	1.90	−0.50	24.40	21.30	18.20	15.30	12.30
Canada	4.10	2.70	2.90	2.60	1.20	3.50	2.30	4.10	−0.60	−2.00	21.60	18.80	17.10	13.30	10.80
Germany	2.90	2.30	1.90	1.40	0.70	1.80	2.00	0.40	3.00	0.10	33.30	28.60	27.10	22.30	23.80
France	3.70	2.40	2.00	0.80	0.20	3.40	1.10	2.10	1.30	−1.50	22.50	20.60	17.60	15.20	10.00
England	1.50	2.85	2.90	2.90	−0.40	1.20	1.90	0.90	−0.20	−1.80	27.50	21.70	19.20	15.60	10.00
Italy	3.80	2.40	1.50	1.20	−1.30	6.10	2.20	1.30	0.80	−3.40	26.60	28.00	22.50	20.00	15.50
Japan	5.10	4.00	1.40	1.60	−0.40	4.50	4.70	0.80	2.40	−0.80	33.10	26.00	25.00	20.50	18.70
South Korea	7.40	8.90	6.00	4.60	3.00	15.80	12.20	8.40	6.80	5.00	18.50	24.60	26.60	28.30	31.10
China(3)	4.80	9.20	9.80	10.60	9.20	9.30	11.00	13.90	11.60	9.70	36.50	43.90	36.70	40.00	38.50
India	3.00	5.60	5.50	770	6.80	4.00	7.70	5.90	8.50	5.20	13.80	16.30	16.50	15.80	13.50
Argentina (4)	2.70	−1.10	4.50	4.20	5.00	1.60	−1.90	3.70	4.40	4.80	35.70	29.40	26.50	17.50	19.50
Brazil(4)	8.60	1.80	2.50	3.60	2.40	9.30	0.30	1.80	3.80	−0.50	27.30	31.00	25.50	17.20	13.20
Chile (4)	2.85	2.90	6.10	4.60	3.70	1.10	2.60	1.90	6.60	2.00	18.60	14.40	19.00	19.70	11.20
Colombia (4)	5.50	3.40	2.70	5.70	3.80	5.80	2.90	1.20	4.60	0.40	17.40	19.70	17.50	15.00	13.00
Mexico(4)	7.00	1.90	3.40	2.30	1.90	7.20	2.10	3.90	0.90	1.30	24.50	18.70	20.00	20.30	17.90
Peru (4)	4.20	−1.20	4.00	5.90	5.60	3.30	−2.00	3.50	4.30	3.20	13.40	11.90	16.70	15.80	14.60
Venezuela (4)	4.00	0.60	1.60	4.60	0.00	5.20	1.90	1.30	2.10	−1.00	24.50	23.40	27.10	19.30	14.30
Global Total	3.80	3.20	2.80	3.20	1.80	4.00	2.20	2.40	5.00	1.70	24.90	21.70	19.50	16.20	15.70

Source (crude data): UN: <stats.un.org/unsd/snaama/dnllist.asp>

(1) Calculations based on VA in US$ at 2005 prices. (2) Calculations based on VA in US$ at current prices. (3) Including mining and public utility services, in 1970/1980, 1980/1990, 1990/2000, and 2000/2007. For the manufacturing industry. Source: 2007/2012= 10.6.
(4) Average rates of 2000/2008 and 2008/2012 for Latin America and Mexico.

The inclusion of China in this table – and I understand that it cannot be included in those categories because it is socialist – shows that it already had a high MVA/VA (36.5%)[9] in 1970, not for having completed the diversification of its industrialization, but mainly because of its high rural population (and employment) and its scarce urbanization and, therefore, reduced services sector. The table shows that that figure grows, standing at approximately 40% over the 1970-2012 period. However, it is worth remembering that the country has already reduced the participation of the rural sector, and the strength of its recent industrialization has transferred more than 300 million people from the countryside to the city, increasing the participation of the services sector, which, from 24.4% in 1970, now reaches 44.6%. For China to also present an eventual normal deindustrialization, such as that of the developed countries, it would need to further expand its urbanization, a hypothesis that would probably only manifest itself in the long run.

However, this apparent deindustrialization must be seen carefully, especially in the post-1990 period. This is because a good part of the developed countries has strongly increased their productive investments in Asia, especially in China, shifting part of their productive capacity to that region and, therefore, creating a deindustrialization that has a much more spatial than effective meaning. These shifts were undoubtedly led by the U.S., EU, and several Asian countries, notably Japan, Taiwan, Hong Kong, and South Korea. Moreover, countries that, in addition to having a mature industry, also have a large agricultural and mineral sector must be considered. These nations greatly benefited from the strong increase in exports of these goods from 2002-2003, notably to China, increasing the annual growth rates of these sectors above those of industry. This is the case in Canada, Australia, and some Latin American countries. However, there is still a third issue: the sharp decrease in the MVA/VA ratio after 2000 may be influenced by the deceleration of growth after 2007, which may or may not be temporary.

9 China's industry in the Mao Era was largely made up of the so-called heavy industry (production goods), which would provide an important basis for further development. In 1970, its industrial VA (mining, manufacturing, and public utilities) in current US$ was about 50% of Japan's equivalent sector, similar to that of France and higher than that of Italy and Canada.

Table 2 – Manufactured exports (xm)

	XM/X TOTAL OF COUNTRY (%)					XM/XM GLOBAL TOTAL (%)				
						Total			Excluding the X from China	
Global Total	1970	1980	1990	2000	2012	1981	1990	2012	1990	2012
U.S.	...	63.00	73.80	82.70	71.30	14.30	12.10	9.60	12.30	11.50
Canada	...	44.60	57.40	63.50	46.30	3.10	3.10	1.80	3.10	2.20
Germany	...	84.00	89.20	87.60	85.20	13.60	15.70	10.40	16.00	12.50
France	...	68.90	74.50	83.30	74.70	6.70	6.70	3.30	6.90	4.60
England	...	61.60	79.20	81.60	71.60	6.20	6.10	3.00	6.30	3.50
Italy	...	81.20	87.00	88.40	79.70	5.80	6.20	3.50	6.30	4.20
Japan	...	94.10	95.70	93.80	88.90	13.40	11.50	6.20	11.70	7.34
South Korea	...	89.70	93.20	89.90	84.40	1.80	2.50	4.00	2.60	4.80
China	...	48.10	71.30	88.20	94.00	0.98	1.90	16.80	-	-
India	...	58.10	69.40	77.60	60.70	0.45	0.52	1.60	1.53	1.90
Argentina	13.90	23.80	28.20	32.30	31.10	0.17	0.15	0.22	0.15	0.26
Brazil	13.40	37.30	51.30	57.50	33.80	0.75	0.67	0.71	0.69	0.86
Chile	4.80	8.50	9.50	14.60	13.30	0.03	0.03	0.09	0.03	0.10
Colombia	9.00	20.50	25.00	32.30	17.30	0.07	0.07	0.09	0.07	0.10
Mexico	33.30	24.40	62.20	83.30	72.70	0.48	1.10	2.30	1.10	2.80
Peru	1.80	15.40	18.20	17.10	11.50	0.04	0.02	0.05	0.04	0.05
Venezuela	1.00	1.60	10.30	8.10	2.00	0.08	0.08	0.02	0.08	0.02
Global Total	...	**53.90**	**68.50**	**72.60**	**62.40**	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**

Source: Crude Data at (US$) current prices – <stat.wto.org/statsticalprogram/ wsdbviewdata.asp.>; Latin America: <estatisticas.cepal.org/cepalstat/web_cepalstat/portada.asp>

Table 2 shows the same countries as the previous table, with their data on manufactured exports. The first part presents the ratio of these goods in the total exports of goods by each country, and in it, there are losers among the developed countries. However, one must consider that between 1990 and 2012, world exports of manufactured goods grew 378% in value (current US$), while inflation in the U.S. (CPI) was approximately 80%. Indeed, these shares grew between 1970 and 1990, remaining high until 2000; they only drop slightly between 1996 and 1998 for Japan and Italy, and almost all of them suffer the largest drops in the 2004-2007 period, affected not only by the crisis but mainly by the enormous increase in the share of China, which grows from 1.9% in 1990 to 6.2% in 2002 and from 12.8% in 2008 to 16.8% in 2012. However, the "trade diversion" that occurred against these countries occurred in a fraction of the growth of these exports, not reducing them, in absolute terms, in any of them. The exception was South Korea, which in the period goes from 2.5% to 4.0%, ranking thereafter as the fourth largest manufacturing exporter[10].

It is even more important to remember that the share of manufactured exports in the total of each of these countries varied in 1980 in the range between 60% and 90% and rose even more until 2000, reaching average levels above 80%, except in the case of Canada (63.5% in 2000), given the high weight of agricultural and mineral goods in its exports. In that country, that share dropped to 46.3% in 2012 due to the same issue pointed out for other countries (excluding South Korea and China), which dropped approximately ten percentage points. There are three reasons for the fall in the 2000-2012 period: first, because in several countries primary product exports grew more than those of manufactures; second, all of them suffered additional export displacements caused by China's trade expansion; third, the post 2007 crisis affected all, notably European countries, which in some of the years from 2007 to 2012 suffered nominal declines in the value of their exports. However, considering the 2000-2012 period, the smallest nominal increase was that of England, with 46%, and over the same period, the U.S. CPI grew by 33%. One should also consider that the period is of great price reduction for electronic content goods.

The second part of the table shows the worldwide share of each country in these exports, including and excluding exports from China. Nominal losses are evident, notably after 1990, when China accelerated its growth and exports. The losses, in this case, are greater because of what they stopped exporting due to China's expansion and the post-2007 crisis. The only net gainers were South Korea and China. Looking at 1990-2012 data, excluding China's exports, losses are smaller, and the only net gainer among them is South Korea, which nearly doubles its share.

China has become the main attraction of foreign investment for Asia as well, especially for Japan and Korea, which channeled part of their industrial production capacity there. With this, the "Asian bloc" expanded and intensified its de facto integration in productive, financial, technological, and commercial terms. Except for Japan – even though it fits one of the two considerations I made above – there are few countries in this bloc that would actually be suffering a deindustrialization, positive or negative.

10 It rises from 2.6% to 4.8% if we exclude China from the global total.

Table 3 – Structure of manufactured exports⁰)

	(1) Machine, equipment, excluding (2)				(2) Automotive products				(3) Electronic equipment and components				(4) Textile and clothing			
									Structure		Global Participation					
	1980	1990	2000	2012	1980	1990	2000	2012	2000	2012	2000	2012	1980	1990	2000	2012
U.S.	49.50	51.70	53.40	44.90	11.00	11.20	10.40	12.00	17.20	12.70	15.90	8.40	3.50	2.60	2.90	1.70
Canada	25.00	26.30	28.90	19.20	30.70	38.70	34.50	29.50	5.10	4.90	2.10	0.60	1.70	1.40	3.90	1.60
Germany	35.60	37.00	39.30	37.10	17.10	18.60	20.90	19.60	9.80	5.50	5.00	3.90	5.70	5.80	3.80	2.70
France	29.20	32.40	44.00	37.40	16.20	16.20	14.40	11.30	12.10	5.20	3.40	1.70	7.00	13.60	4.40	3.50
England	39.00	41.40	46.60	34.20	9.20	9.60	11.00	14.00	21.50	6.20	5.20	1.30	6.50	5.00	3.70	3.30
Italy	29.70	33.90	31.50	34.90	9.10	8.80	8.70	8.00	4.90	2.40	1.10	0.60	13.40	14.40	12.00	8.80
Japan	40.60	49.70	53.70	43.70	21.30	24.10	19.60	23.40	24.00	11.60	11.20	4.90	4.60	2.30	1.70	1.20
South Korea	21.90	38.30	55.00	46.60	0.80	3.80	9.80	15.60	37.90	19.40	6.10	5.40	33.10	22.90	11.40	3.00
China	9.00	23.90	36.80	47.90	0.70	0.60	0.70	2.20	20.00	28.00	4.50	32.30	47.80	38.10	23.70	13.20
India	-	8.80	7.60	16.50	-	1.60	1.80	5.60	1.20	3.00	0.00	0.30	40.00	37.60	35.30	16.20
Argentina	20.80	14.30	14.70	13.10	6.80	5.60	24.70	38.10	1.20	0.30	0.00	0.00	9.50	7.20	3.70	1.40
Brazil	-	23.50	33.90	30.90	19.20	12.60	14.80	15.90	7.30	1.70	0.00	0.02	10.60	6.30	3.70	1.50
Chile	-	9.00	10.40	13.30	-	2.20	7.30	8.90	0.20	2.40	0.00	0.00	1.70	8.60	5.40	5.70
Colombia	-	4.60	7.90	13.30	-	0.30	5.30	5.40	0.30	0.70	0.00	0.00	31.50	34.90	18.60	11.10
Mexico	6.40	46.60	49.00	46.00	8.90	17.40	22.20	28.00	24.50	23.50	3.50	3.80	2.00	5.10	7.40	2.50
Peru	12.00	5.10	5.90	8.00	0.00	0.00	0.10	0.50	2.00	0.70	0.00	0.00	35.80	57.70	54.40	40.00
Venezuela	-	12.50	4.80	7.80	-	4.00	8.20	0.40	0.30	0.20	0.00	0.00	0.60	5.20	1.30	0.20
Total Global	**35.80**	**37.4**	**43.80**	**38.80**	**12.10**	**13.30**	**12.30**	**11.27**	**20.56**	**14.56**	**100**	**100**	**8.75**	**8.89**	**7.52**	**6.16**

Source (raw data): staf.wto.org/statsticalprogram/wsdbviewdata.asp.; calculation at current prices (US$).

(1) Machines, equipment, and components. (2) Passenger, cargo, and auto parts vehicles, excluding railway, aerial, nautical, and motorcycle material, included in (1). (3) IT and telecommunication equipment, including integrated circuits; Mexico's high participation in electronics stems from the implantation of the *maquiladora* industries intensified after its insertion into NAFTA in 1994.

Table 3 shows the evolution of the structural composition of manufactured exports. In the first four columns, the item "machinery, equipment, and components" appears, and from it we excluded "automotive products"; the balance, therefore, has a more appropriate meaning of "capital goods". Despite the high levels presented in 1980, one should note that several countries continue to increase this share, most of them between 45% and 55% in 2000. Canada is an exception, and its lower weight is offset by the high share of automotive products. China, a latecomer, grows very quickly, surpassing all others in 2012. South Korea, a developmental laggard, would come next to China. Certainly, the huge growth in exports of capital goods from China at lower prices must have displaced part of the demand formerly met by developed countries, despite the fall in investment, which surely also exerted a contraction in that demand.

The second group in Table 3 is that of automotive products (passenger and cargo vehicles, including auto parts, not including railway, aerial, nautical, motorcycle vehicles and their parts). In 1980, its participation was between 10% and 15%, and it rose very little over the period. Except for South Korea, which in 2012 already has a high share (15.6%), China was taking its first steps in this sector. Therefore, in this item, one cannot speak of trade displacement caused by China.

The third group includes electronic equipment and its components, which show profound changes in the recent period. Due to unavailability of data, I limited them to the years 2000 and 2012. In 2000, one should note that the share of these goods in total manufactured exports was high, reflecting the global situation of productive restructuring and how restricted the club of countries that produced them was. The developed countries included in this table (excluding South Korea) held 44% of world exports of these products, and in 2012, that figure dropped to just 21%. The share of these goods in total manufactured exports was also sharply reduced.

However, the key issue is that there was a real revolution in the segment's competitive structure, with the sector's partial displacement to Asia, where nine countries now account for 66% of world production, with China holding 32%, South Korea, 5.4%, and Japan, 4.9%. This transformation took place with a sharp drop in prices and changes in production scales. Almost all developed countries not only lost position in this segment but also saw an important part of their trade shift to Asia.

The fourth part of Table 3 refers to textile and clothing exports. As is known, this sector is one of the most traditional in the manufacturing industry. Note that in the case of the developed countries, it decreases its participation as the more complex sectors are consolidated. Some exceptions are found in European countries where high-quality aspects are highlighted in these exports. This is the case, in the table, of France, England, Germany, and Italy, which, although also decreasing, remained expressive in 2000. The case of South Korea is explained by it being a latecomer and still having, in 1980, an expressive weight in the industrial structure in this sector. Nevertheless, in 2012, all of them were virtually aligned at low percentages.

However, this is still a partial view of what happened: world exports between 2000 and 2012 doubled in value, despite the high Chinese presence with its usual low prices. They went from $353 billion to $708 billion. China, alone, went from US$ 52 billion to US$ 255 billion, participating with 57%

of this increase, and Europeans with another 10%. This shows, of course, that developed countries were able to

In summary, if there were losses for the developed ones, they were probably concentrated in the electronics segment.

1.2 Deindustrialization, underdevelopment, and neoliberalism

In the case of underdeveloped countries, UNCTAD called it "***early*** or ***negative*** deindustrialization". This is because their industries, even though they continued to grow, did so at reduced rates, decreasing their share of world production, reducing the investment rate, suffering stagnation, or falling productivity, loss of external and internal competitiveness, and a flagrant drop in the share of exports of manufactured goods. UNCTAD itself shows the few exceptions, such as the Asian NICs that have joined the dynamics of China or Mexico with its ***maquiladora*** industry based on cheap labor. However, Mexico was unable to maintain itself, not resisting the "China effect," even losing part of its exports to the North American market.

For these countries, the crisis also arrived in the 1970s, worsening significantly in the 1980s, a period that was called the "lost decade"[11]. These countries, especially the Latin American ones, had resumed growth production and industrial investment in the second half of the 1970s, growing at high rates and starting a process of diversification of the export basket, with increasing incorporation of manufactured goods. This expansion took place with a strong content of foreign financing, which, at the time, was at flexible rates but very cheap in real terms. However, from 1974-1975, with the first symptoms of the international crisis, credit restrictions began, and the bad news would come with the draconian monetary policy of the U.S., from 1979 onward, excessively raising the real interest rate and with that bankrupting all indebted countries. As ECLAC shows, despite Latin America having suffered a net transfer of resources in the amount of US$ 225 billion in the 1980s, its external debt – which in 1979 was US$ 180 billion – jumped to US$ 453 billion in 1990. All the effort and sacrifices we made were negative, despite of the low growth, technological stagnation, and inflation. The implantation of neoliberal reforms in the underdeveloped world took place slightly later, between the late 1980s and early 1990s[12]. These reforms brought the stabilization policies backed by currency overvaluation and by the heavy fiscal burden resulting from the high interest rates on the external and internal debt

11 About the topic, see Cano (1995 and 1999), especially about the effects of this process on Latin America.

12 Apart from the cases of Chile (1973) and Argentina (1976), imposed by their dictatorial governments, and both failed.

of these countries. Stabilization policies were successful thanks to a high currency overvaluation[13]. A cheap dollar, supported by now abundant external financing and extremely high interest rates, face this competition and survive within it: it is obvious that for this they had to increase their investments and their productivity. Nevertheless, they maintain high deficits in the segment.

Allowed a true flood of imports, stimulating the service sectors (mainly trade and finance) and reactivating growth – which reaches higher bases than in the previous decade. Privatizations, between 1990 and 1997, generated resources equivalent to 1.4% of the GDP of those years, a modest amount compared to the argument stating that "we would pay our debt" with them. The flood of imports cost us deficits in current transactions that totaled, from 1991 to 2000, US$ 493 billion, with which the external debt jumped to US$ 740 billion. The State was transformed into a treasurer of the financial system, "managing" annual public resources for the payment of interests, which reached approximately 8% of the GDP, compressing public spending and, notably, public investment. If the 1980s hampered our industrialization trajectory, the 1990s imposed a perverse cumulative burden. While the developed countries restructured productively, articulating their "business with China" and consolidating the implementation of the technological revolution of the 1980s, we moved even further away from the levels reached by them in terms of international productivity and competitiveness.

Almost all underdeveloped countries were negatively and severely affected by this entire process. Several restrictions were imposed by inflation control policies and currency overvaluation, and the high interest rates tremendously affected public finances and resulted in low (public and private) investment and low growth. The trade opening (which impaired the exercise of a national interest trade policy), a vital part of the anti-inflationary policy, significantly changed foreign accounts, and the high domestic interest became the vital element to attract capital for supporting the depletion of foreign reserves caused in the foreign accounts.

The restrictions imposed on the exchange rate, interest rate, credit, and public finance prevent or cause strong restrictions on the management of the macroeconomic development policy that effectively serves the interests of these countries. It is truly a "straitjacket" that greatly restricts the management of national economic policy. In addition, it is with this perverse heritage that we enter the 21st century. We managed to eliminate the FTAA in 2005, but we had already surrendered our trade policy in 1994, when we accepted the WTO game. The FTAA forced us to do much political and diplomatic work,

13 This appreciation reached around 50% in the decade.

given the difficulties in saying no to the U.S., but this proposal only had the facade of "free trade," as it contained binding clauses on several sensitive issues: services and electronic trade, government procurement, investment and intellectual property agreement. It was so draconian that Joseph Stiglitz himself denounced it[14].

In mitigating our difficult path, the international crisis, although affecting us, at least served to lower the international interest rate. However, instead of Latin America trying to take advantage of it, it continues to exercise high domestic interest rates to attract the insatiable international finance capital to "balance" our balance of payments. Lower interest rates allowed us to breathe slightly more, and the monumental expansion of China reactivated our primary exports, with a substantial increase in their prices.

Only recently, however, has Latin America realized that the highest price we are paying is deindustrialization. I repeat the same method that I took in the analysis of developed countries. The underdeveloped countries included in these tables were also selected. In addition to India, it includes seven of the largest countries in Latin America.

Table 1 shows the depth of the crisis of the 1980s, when we moved beyond the high growth rates of the 1970s. In the 1990s, rates were still low, but one must point out some specificities that explain behaviors as different as Chile's. This country, after the dictatorial regime, virtually abdicated from an industrialization policy, embracing a liberal foreign trade policy, backed by its base of natural resources: mining, especially copper; seasoned fruits and their agro-industrialization; wood and furniture; farmed salmon and shellfish[15]. Nevertheless, history teaches us that relying only on a base of natural resources that are reproducible, but that may not be inexhaustible, involves serious risks. There is already strong concern about the depletion of marine resources, and salmon farming has presented unknown sanitary problems, which has caused the closure of some farms.

Venezuela is one of the largest oil producers, suffering with it the setbacks of an oil economy[16]. In addition, Chaves' victory in 1998 rekindled the country's political struggle, which since 2002 has lived with coup attempts, all of them thus far frustrated. The right-wing coupist is taking advantage of the difficulties of reconciling the country's supply structures with those

14 See the interview from 06/30/2003 *In*: http://www.folha.uol.com.br/fsp/dinheiro/ fi3006200312.htm. For a more detailed critique see Cano (2003).

15 Chile benefits from the off-season period in developed countries. The development of technologies that support these sectors was carried out by the long and intense work of the Chile Foundation, of the State government, which provided this investment.

16 Oil accounts for 25% of GDP, 75% of exports and tax revenue, and just 2% of employment. The movement of international oil prices strongly affects the country's economy, notably the capacity for public spending.

of internal demand and with the recurrent instability of an oil economy that intends to have an active and developmental state. Peru has a productive base backed by mineral resources — notably copper and gold — and has achieved high growth rates over the past 20 years with these exports.

Mexico already had, since the 1960s, legislation that favored the establishment of *maquiladora* industries, a policy that was only successful after the 1980s, by an agreement with the U.S.. This policy allows the import of parts and piecess for the assembly of goods that will be exported. On average, the import content is equivalent to approximately 85% of the exported value, showing the paucity of domestic value addition in such activity, which grew stimulated by low Mexican wages. The activity grew even more from 1994, when Mexico joined NAFTA. The country, which had 2/3 of its exports directed to the U.S., with this decision, which involved many changes n domestic legislation ended up linking its economy to the North American ones, with approximately 85% of exports directed to the U.S. and Canada. In a recent article, Jorge Castañeda (former foreign minister in 2000-2003) balanced the positive and negative effects of this insertion in NAFTA, showing that, if in 1994 *maquiladora* exports comprised 73% of the total, today they comprise 75%, and *maquiladora* industries created only 700 thousand jobs. That is, the internalization effect was minimal. The average growth rate between 1994 and 2014 was only 2.6%, resulting in a low increase in per capita income. In these 20 years, Mexico had only four years of high growth (between 2006 and 2010), two depressive years (1995 and 2009), two years of zero growth (2000 and 2013), and the other 12 years with low growth. If in 1994 there were 6 million Mexicans in the U.S., that number today is 12 million. In addition, it made structural the current account deficits over all these years.[17]

GDP growth in the 2000s is higher, at least in its first eight years, driven by the "China effect," with the exceptional increase in primary exports, little affected by the currency appreciation. In the 2008-2012 period, these economies were affected by the external crisis, lowering, in some cases, their growth rates.

However, the second part of Table 1 shows the most negative side of this process: the growth rates of the manufacturing industry plummeted between 1980 and 2000, gained a boost in 2000-2008 – benefited by the China effect – and fell again before the external crisis.

The third part of Table 1 is more caustic: it shows the violent fall in the share of MVA in the total VA: that of Argentina, which fell from 29.4% in 1980 to 19.5% in 2012; that of Brazil, from 31% to 13.2%; or even that of

17 See Castanheda (2014). On Mexico's weak economic performance and a proposal to revise the NAFTA treaty, restructure its economy and its growth, see Guillén (2008).

Chile, dropping to 11.2%; that of Colombia, to 13%; that of Peru, to 14.6%; and that of Mexico, to 17.9%. These falls were not deeper due to the type of manufactured goods produced, many of which were also stimulated by the China effect. The fact is that both mining and agriculture allow many of their products to be industrially transformed, increasing exports of these types of manufactured goods, such as simple artifacts of metallic products – mainly copper (Chile, Peru, and Mexico); fuels and lubricants (Mexico, Venezuela, Peru, Colombia, Argentina, and Brazil); or processed foods and beverages in most of these countries. The determining factor in this expansion is that these products have their prices first determined by the price evolution of the primary goods that constitute them, and in many cases, it is cheaper to buy them at the origin than to transform them in the destination. This, as in the case of commodities, involves a "monetary" productivity (via prices) that overcomes the obstacle of an overvalued currency.

Argentina, after 15 disastrous years of dictatorship, re-enters neoliberalism, achieving higher growth rates in the 1990s. Nevertheless, the spree of imports – as in the case of Brazil – would also result in a currency disaster and a deep crisis between 1999 and 2002. Since 2001, the new government has taken drastic economic policy measures, including tough "agreements"[18] on the debt and the imposition of additional tariffs on agricultural exports. With this, it supported the exchange rate, and with the resumption of growth in Brazil, it could use Mercosur as the outlet for part of its industrial production. One should also remember that the same government raised the wages of civil servants and the value of pensions and retirement wages, thus increasing household consumption and reactivating the economy.

India was included in these tables, but one must not compare it to Latin America. It does not even make sense to make it part of a supposed group – the BRICS – given their substantial differences. The first is that, in addition to refusing to open the capital account of its balance of payments, it maintained an active state and a industrial policy. However, its structure is very complex: its agriculture still participates with 19% of the GDP, slightly above the manufacturing industry and services, with only 57%. India has used its possibilities – in addition to its cheap labor and the fact that English is its second language. It advanced in industrial production, "where possible," that is, in less complex sectors and, in the more complex ones, in a still contained way. Its high growth rates show that its path, if not the best, was the possible one, even specializing a large part of its foreign trade in the export of services

18 In some cases, the discount reached 80% of face value. The percentage negotiated was high (it appears that it would have been about 93%), but in mid-July 2014, the USA court took a favorable decision for some creditors, and this, at the time (August/2014), caused several protests by Latin American social movements and attitudes of support for Argentina, by various governments in the region.

(computing and telecommunications), equivalent to 40% of total exports and slightly higher than that of manufacturing exports. It was one of the few countries that escaped the straitjacket of neoliberalism.

Table 2 shows, in its first part, the similar trajectory of all these countries in terms of the increase in the share of manufactured exports in the total exports between 1970 and 2012. However, it also shows substantial differences, such as the highest participation from Mexico and the lowest ones from Venezuela, Peru, and Chile, countries that have not embarked on a manufacturing production of greater complexity and scope. The period 2000-2012 exposes the fragility of underdeveloped countries, given the problem of currency appreciation, lack of investment, and relative technological stagnation. We did not resist the "Chinese invasion," which is actually also North American, German, Korean, Japanese... The second part of Table 2 shows the global share of each country in the world export of manufactured goods. India and Mexico sharply increase their shares, and Brazil remains at approximately 0.7%. In the last two columns, I removed China's exports from the world total: those from Mexico and India rise even more; that of Brazil advances to 0.86%; and those of the others, although all rising, show very small values.

Table 3 presents the structure of manufactured exports. The first part shows capital goods of all types, excluding automotive products. The differences between the top of the table and the bottom are now glaring: after removing the automotive products, only Mexico (thanks to the *maquiladoras*) and Brazil managed to increase their share of these goods, with India reaching a modest 16% and Argentina 13%. The data clearly show the fragility of this sector in underdeveloped countries.

The second part, on automotive products, presents another anomaly: Argentina, Brazil, and Mexico – poor and underdeveloped countries – have a participation equal to or greater than that of many developed countries. The assistance generated by international agreements (automotive or free trade, such as Mercosur) and fiscal incentive policies explain part of the issue. India is still groping in this field, which it entered late, currently reaching only 5.6%. Chile and Colombia have modest values (probably of components), while those of Peru and Venezuela are negligible.

The third part shows the most complex and modern segment, that of electronic equipment and components. Due to data limitations, I could only register those from the 2000-2012 period. The first two data refer to the participation of these exports in total manufactured goods; the large numbers are with Mexico: 24.5% and 23.5% of its manufactured exports, or, in billions of dollars, US$ 34 and US$ 63.4, respectively, in 2000 and 2012, and in these same years these imports reached slightly lower values, generating a small surplus.

In the case of Brazil, its exports were equivalent, in the same years, to only US$ 0.5 and US$ 1.4 billion, but its respective imports were US$ 7.6 and US$ 20.1 billion, generating heavy trade deficits. This shows the worst situation in Latin America. Data from other countries are not very expressive in value and relative terms. India expands its participation, but its trade deficit in these goods jumped from $2 to $20 billion, like Brazil. The last two columns show data on the global participation of each country: excluding Mexico (3.5% and 3.8%), the others present insignificant values, and India has a symbolic 0.3%.

The fourth part of Table 3 refers to textile and clothing exports. India has a lagging industrial structure, where this segment still weighs 40% of total exports, only reducing it in 2000-2012. However, this reduction is misleading, since these exports went from $11.6 billion in 2000 to $29.1 billion in 2012. Of the Latin Americans in the table, Colombia still resisted a high percentage until 1990, reducing it thereafter, probably less because it promoted deep changes in the export basket and more because of the weaknesses arising from neoliberalism, which reduced investment and obviously productivity. The only one that maintained a high percentage in this segment is Peru, but its absolute values are negligible and only gain some relevance compared to total exports of manufactured goods, which are also small. The figures for Argentina, Chile, and Venezuela are also small. Those of Brazil are slightly more expressive, at approximately US$ 1.2 billion. The only ones truly with a slightly larger expression are those of Mexico (US$ 11.2 billion in 2000, but dropping to US$ 6.7 billion in 2012). However, import figures show similar flows in 2000 but double in 2012, generating a deficit of US$ 12.5 billion, of which Brazil's was US$ 5.7 billion. Here, the losses are very clear, even in a segment in which we were able to compete internationally and were net exporters. Another painful loss in national and Latin American accounting.

2. Deindustrialization in Brazil

Let us briefly see, in the case of Brazil, the main factors that are causing early and harmful deindustrialization, giving it a economic regressive meaning:

a) One of the main causes has been the prevailing exchange rate policy introduced under the Real Plan. With the liberalizing reforms and the stabilization policy, the excessively appreciated currency plays, until today, the role of price anchor, in which it receives the proper "logistic" support from the practice of absurdly high real interest rates and the fiscal anchor. This results in most of the payment of interest on the public debt[19]. The combined result of this insane trilogy – interest, exchange, and deregulation – was the growing loss of international competitiveness of the national industry compared to other countries.

b) Another reason is the result of the unruly opening that Brazil has gone through and has been going through since 1989, still under the Sarney government, when there was a first attack on the protection we had on imports. This attack was greatly expanded during the Collor government in 1990. The third one carried out during the Fernando Henrique Cardoso government, from 1994, expanded by our entry into the WTO. This deregulation continued and remained so today. The opening of trade with the drop in tariffs and other protectionist mechanisms of the national industry complemented the harmful effect of the appreciated currency, drastically reducing the degree of protection against international competition.

c) Third reason: the country's high interest rate makes the capitalist entrepreneur – both in Marx's and Keynes's view – compare it with the rate of profit, with the expectation of accumulating capital. Except for rare or illicit sectors for which the rate of profit is exorbitant, we can see that, in finance, these gains have been very high, offsetting the tendency for the rate of profit to fall. The rate of profit of the modern industrial economy is relatively contained and, when faced with an interest rate such as the official one (Selic) in Brazil, today, of 11%[20], national entrepreneurs are aware of this phenomenon and only invest as a last resource. Otherwise, they go bankrupt. Under such conditions, investment is strongly inhibited, which leaves the industry vulnerable. An industry that does not invest ages, becomes, in part, obsolete, does not grow, and has enormous difficulties in assimilating technical progress on a daily basis. In short, it loses productivity, new opportunities, and competitiveness, becoming a strong obstacle to the country's economic development. Recent research on the subject shows that between

19 The real exchange rate in recent years has always appreciated. In the 1990s, due to stabilization policies, the average appreciation reached around 50%, according to data from ECLAC. In 2011, between 20% and 28% and, in 2012 (January to June), between 20% and 25%, compared to 2005. Cf. IpeaData, Real effective exchange rate of manufactured exports. Data obtained on 8/15/2012, from http://www.ipeadata.gov.br/. According to Oreiro (2012), between 1/2003 and 2/2012, the appreciation would have been 37.3%. In this text, the author makes an interesting and timely discussion between the dichotomy "internal savings – external savings" and the discussions involved about foreign resources and currency appreciation.

20 Cf. Banco Central do Brasil. It dropped, from 2011 to mid-2012, from 12% to 7.25%, when it rose again strongly, reaching 11% in April 2014.

2002 and 2009, of the 28 industrial sectors surveyed, 23 presented a reduction in average productivity, and only five had positive average annual rates: automobile (4.3%), paints and varnishes (2.2%), cellulose (0.8%), office and computer machines and equipment (0.8%), and textile (0.4%)[21].

d) Fourth reason: foreign direct investment. It is true that this flow has grown in absolute numbers in recent years, a fact celebrated by many economists. They, however, have a serious flaw when they talk about investment because they only think in global terms about the volume and share of GDP. Investment, however, is such an important variable in economics that economists should be more careful. An investment rate needs to be structurally analyzed. First, investment in portfolios, private securities, and public debt, in general, predominantly of a speculative nature, should be deducted from the total flow of foreign capital.

The historical series of FDI in Brazil, compiled by the Central Bank, shows unequivocal data: in the 1980s, the participation of the manufacturing industry in the total FDI was approximately 75%. This figure drops to approximately 60% in the 1990s and fluctuates between 30% and 40% since 2001. At the same time, the participation of services rises, and with them the participation of financial activities. The most serious thing, however, is that the annual average of FDI in the manufacturing industry – which was approximately US$ 17 billion in the 1980s – rose to US$ 25 between 1990 and 1995 but sharply fell thereafter to US$ 8.5 billion between 1996 and 2010. In the period from 2011 to September 2013, it rose to an average of US$ 20 billion.

Regarding domestic investment, similar facts can also be observed, with a predominance of allocation to services, especially in the sectors of finance, construction, real estate, agriculture, and mining, and its current participation in the manufacturing industry is reduced.

This is understandable, as the productivity and competitiveness of Brazilian industry were restrained and, in many cases, fell, and this was well perceived by capital. At the same time, there was a shift of predominantly American and Asian FDI to China in search of cheap labor, undervalued currency, and high competitiveness. For this reason, it largely moved to China to promote cheaper production, abandoning or reducing its presence in former areas where it had had great expression, such as in the northern Mexican border. The harmful internal effects of such a fact were as follows:

21 Cf. Squeff and Nogueira (2012). The survey, carried out in partnership with Ipea and ECLAC, involves 56 industries of the national accounting system (agricultural, industrial, and tertiary sector).

- loss of competitiveness of Brazilian industrial exports (manufactured products) and the replacement of part of them by the product from China in traditional markets such as the U.S.;
- a high increase in imports of these products, both of final consumer or capital goods and even industrial inputs of all kinds, especially chemicals and electronics, affecting many commodity chains of the Brazilian industry in a harmful way;
- The two previous effects profoundly affected the sector's productive investments, making them more specific, opportunistic, and atomized.

e) The fifth reason that economists are even more concerned with is that since 2007, the world economy has slowed down. One can see, especially from the U.S. and European Union economic policy, that we may possibly be going through a long period of crisis in most developed economies, as, in fact, several critical institutions and economists have predicted[22]. Such economies, especially the U.S., plus China – which lost part of the markets it competed for – are developing aggressive policies in the international market for manufactured products, achieving high growth rates in these exports and recovering some of the lost ground.

Some macroeconomic data help us to understand the problem more deeply so that we can better understand the complexity of our situation:

Table 4 – Brazil: average growth rate of effective demand components (%)

	2003-2008	2008-2012	2013
Total GDP	5.0	2.7	2.28
Household consumption	7.0	4.6	2.26
Government consumption	3.6	3.1	1.89
Investment	9.9	2.0	7.53
Exports	16.3	1.2	2.51
Imports	21.3	8.4	8.37

Source: IBGE-CN.

Between 2003 and 2008, after a period of crisis and recession, the GDP growth rate rose due to three specific facts. The first and most important was the growth in household consumption, stimulated by the increase in consumer

22 See, among others, the OECD (2012) and Levy (2012) forecasts.

credit[23], by the sharp rise in the real minimum wage and by other social policies, such as Bolsa Família.

The second, despite the restrictive fiscal policy, were the decisions to expand public financing for (public and private) investment, and the third stems from the great expansion generated by the exports sector, although imports, as of 2005, grew more than exports. It was these factors that allowed a greater advance in income and employment, expanding the demand for consumption, which was more intense than that for investment.

The strong increase in exports was due to the international boom between 2004 and 2008, with a sharp rise in raw material prices and physical demand, mainly generated by the Chinese economy. However, with the greatest global extension of the crisis that started in 2007-2008, the average GDP growth fell, and the average rate of 2008-2012 (2.7%) was close to the critical trajectory of the 1990s, when it was 3%.

The investment rate, heavily depressed since the 1980s, fell further until 2005, recovering a small part of the lost ground, rising in 2008 to 16.9% and to approximately 19% in 2010 and 2011. In 2012, it dropped again to 17.6%, making it more difficult to recover the necessary level reached in the 1970s, on the order of 25% of GDP. Table 5 shows the sectoral growth rates of the Brazilian economy. One can see that the manufacturing industry had the worst results in terms of GDP. As previously indicated, investment is very low, a situation made worse by the effects of the post-2007 crisis.

There is another consequence of this scenario: the loss of the relative position of underdeveloped countries in world industrial production. Whether or not China is included in this list, the data show that Brazil is sharply losing ground on the international scene. Indeed, the Brazilian share in the production of the world manufacturing industry, which was 2.8% in 1980, dropped to 2% in 1990 and reached 1.7% in 2010[24].

Table 5 – Total and Sectorial GDP: average annual growth rates (%)

PERIOD	1989-2002	2002-2008	2008-2013
Total GDP	2.5	3.7	2.6
Agricultural GDP	4.8	4.4	2.3
Industrial GDP	1.6	3.6	1.0
Manufacturing industry GDP	1.6	3.2	0.0
Services GDP	2.8	3.8	2.9

Source: IBGE-CN/IpeaData.

23 Basically, by payroll-deductible loans and supported by deductions from payrolls and retirees.

24 Cf. UN, System of National Accounts, in US$, at 2005 prices. unstats.un.org/unsd/sna- ama/dnllist.asp.

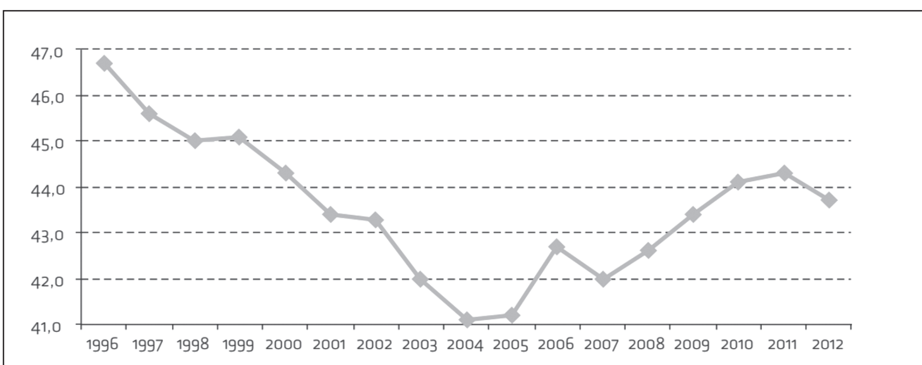
It is also known, regarding the manufacturing industry growth rates, that the capital goods and durable consumer goods sector had been showing sharp growth since 2002, but in fact, it was the durable consumer goods sector that most pulled the demand.

Although the data and facts presented above show this abnormal deindustrialization in our economic process, the acceptance of this fact was not consensual until recently, and many economists, not infrequently, do not believe that these losses have been so accentuated. One of the rare institutions that also denounce deindustrialization is the Institute of Studies for Industrial Development (IEDI), which in its Monthly Letters has warned, denounced, and demonstrated the phenomenon[25]. To reinforce these criticisms, I think it is important to add some other data that expose slightly more the weakness to which the manufacturing industry was subjected.

2.1 The VIT (value of industrial transformation)/ VIP (value of industrial production) ratio

It should be clarified that this ratio was approximately 0.55 in the period of high inflation (between 1988 and 1994), but it could mean, in part, a higher markup as a defense mechanism for companies. With the beginning of the Real Plan, it dropped to 0.52 in 1995. However, due to methodological changes in the source of primary data, it is preferable not to include such data in the following chart, restricting it to the 1996-2011 period.

Graph 1 – VIT/VIP ratio (manufacturing industry)



Source of crude data: IBGE, PIA, several years.

25 Cf. IEDI, several Letters, notably from 2010, all found in www.iedi.org.br/.

The graph shows the sharp drop in the VIT/VIP ratio. Note that it was approximately 0.47 in 1996, falling until 2004 and 2005 (approximately 0.41), showing a small recovery and stability in 2006-2008 (approximately 0.42), and rising slightly in 2009 (0.43) and in 2010 and 2011 (0.44), paradoxically, in a period of crisis. This is very likely due to the following facts: ***i)*** conjunctural change in the productive structure fundamentally caused by the performance of more oligopolized sectors that have a high power to set markups; ***ii)*** intensification of industrial imports in the recent period, lowering prices and costs of imported inputs and capital goods, possibly partly not passed on to buyers of products made with such goods; ***iii)*** this intensification of imports certainly changed commodity chains, replacing more expensive and less profitable products; ***iv)*** strong increase in export prices of several semifinished industrial products after 2003-2004; and ***v)*** reduction of financial and tax costs resulting from the anti-cyclical policies recently practiced.

2.2 The productive structure of the manufacturing industry, according to the criterion of use of goods

As only the manufacturing industry is under analysis here, the data and classification used and published by the Brazilian Institute of Geography and Statistics (IBGE) cannot be used in this item since it includes the mineral extractive industry in its estimates. Thus, we use a methodology that classifies the sectors of the manufacturing industry as ***predominantly producers of i)*** nondurable consumer goods; ***ii)*** intermediate goods; and ***iii)*** durable consumer goods and capital goods, which is the sector with the greatest technological complexity[26].

Sector ***i*** (where important exporting segments are present), as industrialization advanced, sharply reduced its importance between 1939 and 1980, falling from 67.5% to 33.9% of VIT, which reduced its participation, placing it between 35.2% in 2009 and 33.1% in 2011.

Sector ***ii***, with a strong exporting presence, had a significant increase in its participation between 1939 and 1980, from 25.9% to 41%, fluctuating between 43.6% in 2009 and 41% in 2011, also seeming to have lost space in our industrialization.

Sector ***iii*** had the highest growth rates between 1939 and 1980, when it went from meagre 6.6% to 25.1%. Its subsequent trajectory, however, is decreasing, reaching 24% in 1996, 21.6% in 2003, 21.2% in 2009, and 25.9% in 2011, when it seems to return to the 1980 level. This movement

26 For this methodology and for data from the 1970-2003 period, see Cano (2008). Also see Valderrama (1966).

in the structure undoubtedly shows a regressive trend from 1980 to today, with the return of the predominance of nondurable and semi-industrialized export sectors.

This methodology, however, means that a large part of sector ***iii*** contains a greater fraction of durable consumer goods than capital goods, given the methodological and statistical confidentiality problems of IBGE, especially when we operate at more than three digits in the subgroups of activities. A small and partial exercise was carried out with the Industrial Censuses of 1970 and 1980 and the IBGE Annual Industrial Survey for the years 1996, 2003, 2009, and 2011, removing from sector ***iii*** items that are predominantly intended for domestic consumption or production input rather than productive investment. Items removed were passenger vehicles (cars and utility vehicles), auto parts, household appliances, and sound and image devices (from which it is not possible, in three digits, to exclude cell phones).

After deducting the VITs of these four segments, the remaining production from sector ***iii*** is closer to that of capital goods, although it still contains an important residue of durable consumer goods and intermediate goods. The new data would be 15.6% in 1970; 19.9% in 1980; 14.1% in 1996; 10.0% in 2003, 11% in 2009 and in 2011, an expressive rise to 16.2%, but which still leaves the participation of this segment below that of 1980. In fact, what explains more than half of the growth that took place between 2009 and 2011 was the exceptional increase in vehicles and cargo equipment (the rest of the motor vehicle sector), which in 2009 weighed only 0.22% of the total VIT of the manufacturing industry and that, in 2011, thanks to the special incentive policies it received, had a more than tenfold increase in its share, which reached 2.76%. However, although these goods are considered capital goods, they are not machines. Here, industrial regression is even more transparent.

2.3 Problems with the new foreign trade insertion

After the successive trade deficits of the 1990s, only reversed after the 1999 currency crisis, thanks to the expansion of primary exports, we had average surpluses of $42 billion in 2004-2007. The expansion of imports of industrial products, however, reduced that average, in 2008-2011, to approximately US$ 25 billion, falling to US$ 19 billion in 2012 and US$ 2.6 billion in 2013. After the trade opening, the percentage coefficients of exports (Cx) and imports (Cm) of the manufacturing industry, calculated by the Foreign Trade Foundation (Funcex), grew; Cx, for instance, from 12.7 in 1985 to 16.8 in 2004. The Cm, however, jumped from 3.9 to 10.9, reaching higher levels (from 12 to 14) between 1995 and 2000, surpassing the Cx. Some sectors presented huge increases in their Cm between 1985 and 2004, such as electrical equipment (from 8 to 26), electronic equipment (from 12 to 85), pharmacy and perfumery (from 4 to 35)[27].

According to the new Funcex series – from 1996 to 2012 – Cx rises from 12.7 to 21.6 until 2004, falling afterwards until 2012, when it reaches 15.6. For imports, it discloses the Cpm (coefficients of imports)[28], which goes from 14.1, remaining at approximately 15 until 2009, and increasing to 19.3 in 2012, numbers that, since they started in 1996, when imports had already grown vigorously in absolute and relative terms, underestimate part of the changes that occurred during the opening period. Even so, after examining the coefficients of the 23 segments published for the manufacturing industry, it is worth mentioning that the Cpm increases by 18, of which the most notable cases were those of chemical products (19.4 to 27.6), rubber (9 to 15), metallurgy (9.6 to 18.8), machinery and equipment (33.7 to 36.9), electrical machines and appliances (15 to 19.8), computer equipment (36 to 44), other transport equipment (28 to 31), pharmochemicals and pharmaceuticals (17.4 to 27.6), and various industries (21 to 35.7).

The issue becomes more transparent when the net trade result in manufactured goods is analyzed[29]. After the 1999 crisis, it was possible to reverse, as of 2003, the deficit in manufactured goods. From 2003-2006, there was an average annual surplus of US$ 5 billion that turned into successive deficits from 2007 onward (−US$ 9.3 billion), −US$ 38 billion in the 2008-2009 average, −US$ 76.7 billion in 2010, −US$95.8 billion in 2011, −US$94.1 billion in 2012, and −US$105.0 billion in 2013.

However, where is this deficit located? As investment was restrained in tehe manufacturing industry, the high and medium-high technology sectors are heavily represented in this number and constitute more than half of the deficit. Indeed, the structure of exports of industrial products (semi-industrialized plus manufactured) in 2012 shows that high-tech products accounted for only 6.8%; medium-high, for 27.1%; medium-low, 26%; and low, 40.1%. In 2012, of our total imports of these products, 48.5% were high technology goods; 21.5, medium-high; 21.5%, medium-low; and 9%, low technology. Even in the low-tech sector, it is surprising to note that textile and clothing, which are traditionally surplus sectors, have shown deficits of approximately US$ 5 billion, according to WTO data.

27 Coefficients obtained in 2005, at the Funcex website. These calculations were later replaced by a new series, from 1996 until today, which presents the Cx with values slightly different from the previous series and, in place of the Cm, discloses the Cpm.

28 Cpm = M/ (P-X+M), that is, imports over apparent consumption.

29 Total industrial products, excluding semi-manufactured products.

2.4 Business between Brazil and China

The exuberant annual growth of the Chinese economy greatly expanded its foreign demand across the board. The new international division of labor, high productivity, and devalued currency, however, made its trade relations with Latin America take on the classic form of the center-periphery relationship, with the Chinese export basket consisting primarily of manufactured products and its importing basket of primary products, contrary to the commercial structure it practices with the rest of Asia, the EU, and the U.S.

Table 6 shows the structure of Latin American exports from Mexico and Brazil to China. It should be noted that in 1990, the participation of industrial products in the total exports of Brazil (80.5%) and Mexico (98.4%) was high and that of primary products was low. In 2000, that share began to fall, strongly in Brazil (32.1%) and still moderately in Mexico (96%). In 2008, they fell even more, to 22.5% in Brazil and 72.3% in Mexico. Furthermore, Chinese exports to the U.S. displaced a good part of Mexican, Central American, and Brazilian industrial exports, making the international insertion much worse.

Table 6 – Latin America and Caribbean, Mexico, and Brazil: Structure (%) of exports to China

	LATIN AMERICA AND CARIBBEAN	MEXICO			BRAZIL		
Product	2008	1990	2000	2008	1990	2000	2008
Primary	75.0	1.4	3.7	27.5	19.5	67.9	77.5
Industrial:	25.0	98.6	96.3	72.3	80.5	32.5	22.5
-Natural resources	14.6	11.7	11.1	32.7	34.0	13.4	12.2
-Low technology	2.4	6.7	1.9	2.8	17.3	4.5	2.6
-Medium technology	4.6	79.1	24.9	19.6	28.9	9.0	5.5
-High technology	34.3	0.9	58.2	17.0	0.3	5.1	2.1
-Others	0.1	0.2	0.2	0.2	-	0.1	0.1

Source: Cepal/Database.

Due to difficulties in updating this information, I was only able to gather, for recent years, partial data for Brazil: of the total exports to China, 82.9% were basic products, and industrial products accounted for 17.1%, of which 11.3% were semi-industrialized and only 5.8% were manufactured. In the neoliberal order, nevertheless, one cannot complain about this, about "free trade".

The data in Table 3 show that the regression is more severe when the sectors are analyzed by technological intensity: participation in the Brazilian basket falls in all categories. In Mexico, the phenomenon also occurs, but the categories of medium and high technology still maintain significant shares, much higher than the tiny shares in Brazil, making it clear that the results of trade with China show a more regressive situation, even in terms of Latin America.

On the other hand, it is difficult for Brazil to pressure and negotiate with China on this structure and on the "invasion" of Chinese products, given that, from 2009 to 2012, China was responsible, on average, for approximately 30% of our total trade surplus.

2.5 The reprimarization of our export basket

Table 7 shows the structure of the export basket in recent years, according to levels of industrialization: basic, semi-industrialized, and manufactured products. Note what happens with manufactured goods: the weight of exports of products indicated in the Brazilian export balance, from just over 60% in 2000, passes to only approximately 38% in 2011-2013. Even in the semi-industrialized segment, the curve also descends. There are still those who do not accept the idea that a deindustrialization process may be taking place.

Table 7 – Brazil: Structure of exports (%)*

Year	Basic	Semi-industrialized	Manufactured
1964	85.4	8.0	6.2
1980	42.2	11.7	44.8
1985	33.3	10.8	54.9
1990	27.8	16.2	54.2
1995	22.9	20.8	56.2
2000	23.4	15.8	60.7
2006	29.9	14.5	55.6
2007	32.8	13.9	53.5
2008	37.9	13.8	48.1
2009	41.4	13.7	45.0
2010	45.5	14.3	40.2
2011	48.9	14.3	36.8
2012	47.8	13.9	38.3
2013	47.8	12.9	39.3

Source: Ministério do Desenvolvimento, Indústria e Comércio (MDIC) (*) excluding special operations.

The data above are undisputed: they mean a strong regression and reprimarization of the export basket. The phenomenon also affected Latin America, as shown by ECLAC data: between 1980 and 2000, the share of manufactured goods in the region's total rose from 17.6% to 58.2%, falling in 2011 to 39.3%. If the data for Mexico are removed, those figures are, respectively, from 19.3% to 30.6%, falling to 21.6%.

A few words should be added about Mercosur, despite its limitations, since the total exported by Brazil in the last 20 years has remained approximately 12% to 13% of its foreign sales, and its purchases have been only approximately 8% to 9%. A first good reason to support Mercosur is that, from 1990 to 2013, we only had a deficit in nine years. A second and better reason is that our exports are predominantly manufactured goods, accounting for approximately 84% of the total. A third is that Argentina is our third-largest partner in the world – only recently surpassed by China. Considering 2013 data, of the total exported in automobiles, cargo vehicles, and auto parts (US$ 11.1 billion), 71% went to Argentina, 7.3% to other Mercosur countries, and 5.9% to Mexico. For total imports of these same products (US$ 20.7 billion), Argentina contributed 33.3%, with a zero balance; Mexico contributed 9.2%, causing us a debt balance of US$1.2 billion; and the bulk of the deficit in this segment came from the U.S. and some European and Asian countries.

In other words, even if Mercosur does not solve our trade problems today, it must be strengthened. I agree with the concerns expressed by ambassador Samuel P. Guimarães, who, in a recent article, warns that if the Mercosur-EU Agreement is approved, it would, in fact, mean the end of Mercosur, since the advantages of companies based in Mercosur would disappear, favoring the European ones. By indirect relationship, via the Trans-Pacific Partnership and the US-EU Trade Agreement, such advantages would be extended to member countries of these agreements, representing, in fact, a probable extinction of Mercosur, without obtaining the advantages promised by both treaties. We would be repeating the mistakes made in the Uruguay Round and in joining the WTO[30].

By the way, speaking of the Trans-Pacific Partnership, it is good to remember the recent warnings made by Stiglitz to the US government about the harm that this agreement will cause to the U.S. in terms of unemployment, calling attention in particular to the deregulation of norms and the increase of international rights to companies, trampling on the national law of all member countries of these agreements[31].

2.6 The structure of the import basket

Table 8 indicates the structure of total imports in terms of capital goods, durable consumer goods, nondurable consumer goods, and intermediate goods (excluding fuels and lubricants). While total imports grew 5.1 times between

30 Cf. Guimarães (2014).
31 Cf. Stiglitz (2014).

2002 and 2013, those of capital goods and intermediate goods grew slightly less (4.4 and 4.6 times, respectively), but those of nondurable consumer goods multiplied by 5.5 and consumer durable goods grew 8.9 times.

The real "avalanche" of imports, especially regarding durable consumer goods, was due to the cheap dollar and poorly negotiated trade opening. This increase in imports has, in part, broken or weakened links in various commodity chains, thus eliminating companies and the production lines of several companies. At the same time, the phenomenon highly inhibits normal investment, typical innovator investment, or even the one that complements production chains.

One must understand that eliminating a company is relatively easy under such circumstances. Destroying a national industrial leadership, a dynamic industrial entrepreneur, as occurred to many, is also easy. The difficult thing is to create or try to recreate such companies and their respective leadership. Creating and recreating expressive and large national companies such as the Mindlin group (Metal Leve, in the auto parts sector) or others, such as Kasinski, which previously produced parts and exported them to the North American and European markets, then became simple assemblers of motorcycles in the Free Trade Zone of Manaus and, finally, sold the new companies to foreign capital. In addition, which is also very serious, large national textile companies, such as Hering, which used to have industrial production as their main activity and, now, have regressed to a predominantly commercial activity.

Table 8 – Brazil: Imports (in US$ billions)

YEAR	TOTAL	Capital goods	Intermediate goods	Durable consumer goods	Non-Durable Consumer Goods
2002	47.2	11.6	23.4	2.5	3.4
2003	48.3	10.4	25.8	2.4	3.1
2004	62.8	12.1	33.5	3.2	3.7
2005	73.6	15.4	37.8	3.9	4.6
2006	91.4	18.9	45.3	6.1	5.9
2007	120.6	25.1	59.4	8.3	7.8
2008	173.2	35.9	83.1	12.7	9.8
2009	127.6	29.7	59.7	11.6	9.9
2010	181.6	41.0	83.9	18.6	12.8
2011	226.2	47.9	100.1	24.1	16.0
2012	223.1	48.6	99.8	22.2	17.2
2013	239.5	51.6	106.5	22.2	18.7

Source: MDIC.

(*) Excluding fuels and lubricants.

2.7 Macroeconomic policy and the balance of payments

Table 9 summarizes, for some of the foreign accounts, the direct and indirect effects of this perverse macroeconomic policy, which are not limited to imports and exports, since the cheap dollar encourages spending on various types of services. Net spending on services (tourism, film rental, engineering services, international transport services, financial services, etc.) jumped from −US$8.3 billion in 2005 to −US$47.5 billion in 2013.

Table 9 – Balance of payments (in US$ billions)

Year	Trade	Services	Income	Current account
2005	44.7	−8.3	−26.0	14.0
2006	46.1	−9.6	−27.4	13.6
2007	40.0	−13.2	−29.4	1.6
2008	24.8	−16.7	−40.6	−28.2
2009	25.3	−19.2	−33.7	−24.3
2010	20.2	−30.8	−39.6	−47.4
2011	29.8	−37.9	−47.3	−52.6
2012	19.4	−41.0	−35.4	−54.2
2013	2.6	−47.5	−39.8	−81.4

Source: Banco Central do Brasil.

The cheap dollar and the low investment opportunity generate even worse effects on the income account of the Balance if Payments, causing them to reduce reinvestment and increase remittances of profits and dividends. The numbers are also frightening: its deficit, which in 2005 totaled −US$26 billion, jumps in 2010 and 2011, respectively, to −US$39.6 billion and −US$47.3 billion, falling slightly to −US$ 35.4 billion in 2013, certainly due to the crisis and reduction of profits, as well as the temporary reduction in interest rates. Thus, services and income totaled, between January 2010 and December 2013, the fantastic figure of −US$ 319 billion. As is well known, the algebraic sum of the balance of services and the balance of income with the balance of trade indicates (approximately)[32] the current account balance, which reached −US$ 81.4 billion in 2013.

To settle this deficit, macroeconomic policy keeps the economy unregulated and real interest rates at a surprisingly high level, with the obvious objective of attracting foreign capital, which, with the voluptuousness of high interest rates, enters in greater amounts than needed. Thus, the origin of the accumulation of foreign reserves is more financial than commercial.

32 The balance is not accurate, due to Errors and Omissions and other unverified data.

Having covered the deficits over all these years, after 1999, there was no more currency crisis, and there was still an accumulation of US$359 billion in international reserves. Several analysts look at these numbers and claim that the country's foreign vulnerability is over. The US$ 359 billion in international reserves, however, are very expensive, as they are basically invested in US government bonds whose interest rate is close to zero. The government, nevertheless, to accumulate these reserves, has to issue public debt bonds, which pay interest that today amounts to approximately 11% annually and are equivalent to approximately 5% of the GDP, in a large drain on public revenue and expenditure.

The disincentive to internal investment and the cheap dollar strongly encourage the outflow of Brazilian capital. Until 2001, the total invested abroad was US$ 68.6 billion – this amount would rapidly grow, reaching US$ 275 billion in 2010, of which 25.5% were invested in notorious tax havens[33]. In 2012, that figure jumped to US$ 356 billion, and of this total stock, FDI amounted to US$ 268 billion. Its investment structure revealed strong similarity with that of national capital investment in Brazil: 25% in agriculture and mining; only 18% in the manufacturing industry; and 57% in services, of which 65% in financial services. Altogether, Brazilian capital would have created approximately 200 thousand jobs abroad.

The most paradoxical thing, however, is that, for this, a large part of these investments have been financed by public resources (generally subsidized), mainly from the National Bank for Economic and Social Development (BNDES). Investments abroad are being financed when it should be in Brazil that jobs must be created, the industry modernized, illiteracy and hunger eradicated, road holes covered, housing policies promoted for the poor, and barbaric rural endemics ended. Table 10 shows our total foreign debt, our net foreign liabilities, and foreign reserves. The data show that if we discount foreign reserves from foreign liabilities, net liabilities increase from US$ 298 billion in 2004 to US$ 826 billion in 2012, falling to US$ 764 billion in 2013. Furthermore, one must consider that a large part of foreign investment today consists of portfolio investments that are more easily mobilized and, therefore, liable to a quicker capital flight.

33 As the data for these investments are per countries, among which only a few of them are identified as tax havens, the figure estimated in the text is certainly strongly underestimated. Several surveys over the past ten years point to figures that range between 50% and 70%. For official data see: Banco Central do Brasil; Capitais Brasileiros no Exterior: www. bcb.gov.br/rex/cbe/port; data obtained in 03/24/2012.

Table 10 – Foreign debt and net foreign liabilities

Year	Gross foreign debt	Net foreign liabilities	Total reserves
2004	220.2	298	52.9
2005	188.0	317	54.0
2006	199.4	369	85.8
2007	240.5	550	180.3
2008	262.9	283	193.8
2010	351.9	887	288.6
2011	404.1	764	352.0
2012	440.6	826	373.1
2013	482.8	764	358.8

Source: Banco Central do Brasil.

(*) In 2008, the Central Bank started to disclose the International Investment Position data, which is lower than the data from the old PEL calculation. The large reduction between 2007 and 2008 refers to the strong outflow of portfolio investments.

As the liabilities exceed reserves, the vulnerability remains. Of course, foreign reserves are important and strategic but are not enough to avoid or protect from an international crisis that could cause a major capital flight.

Would it be possible to reverse this picture of deindustrialization? Past crises have shown that there is no way to be liberal in a depression. If the "safe" is empty, without money, how can one be liberal? In contrast, in such circumstances, it is necessary to intervene publicly, and there is no less bitter remedy.

The consolidation of the national company is an expensive and very important investment, whose greatest examples, before China, come from Germany, Japan, and South Korea. In such cases, international circumstances were different, as the threat of socialism was very strong, positively conditioning part of the American reactions to state intervention policies that strongly benefited the economy of these countries.

There was a drastic intervention in German, Japanese, and South Korean society and economy. The largest and most radical were the agrarian reform and the capital reform. When Japan "opened up", restructured its industry and recovered from the defeat of the war, and when South Korea was supported by the U.S., both "open up" markets. Such countries not only had extremely favorable international circumstances for their companies to become stronger and more aggressive and to be victorious in the international scenario but also had state policies aimed at this, that is, protectionist ones, directed toward industrialization and those financing industrial activity. South Korea even banned the domestic consumption of color television, directing its production to export. There was the practice of macroeconomic policies and industrial policies which allowed their large companies to grow and achieve extraordinary performance in the international scenario, under favorable international circumstances. There was, above all, a National State and, not infrequently, a statesman who knew how to conduct this process.

Would it be possible, today, to reverse this picture of deindustrialization in Brazil? For this, the formulation of a new industrial policy, although necessary, would not be enough. In my understanding, no specific policy (sectoral, regional, industrial, agricultural, foreign trade, or otherwise) will be successful if the macroeconomic policy does not provide the necessary political and economic support, that is, the industrial policy must be in line with the macroeconomic policy. Otherwise, with the current interest rate, the current exchange rate policy, the level of openness of the economy, and the noncontrol of the financial account of the balance of payments, there is no industrial policy that can reverse the situation analyzed above. It is a true "straitjacket".

Tax exemptions, for example, on payroll and IPI used recently for some sectors (clothing, footwear, furniture and apparel, civil construction, vehicles, and software production) had positive effects on demand in times of economic slowdown. Currently, they are being renewed and extended to various industrial sectors. Nevertheless, they incentivize only demand and not investment, except in the case of residential construction. In 2012, the administration launched a timely, necessary, and commendable private and public investment plan for transport logistics, with important resources in terms of the sector, but very limited in general terms, equivalent to approximately 0.4% of the GDP per year over the next five years. This plan also expands the investment capacity of states of the federation, whose investments, however, are proportionally very small in the total fixed capital formation in the country[34].

For businesspeople in these segments the tax exemptions and the investment plan are good measures because reduce costs and increase profits. However, they are insufficient before the country's not only cyclical but also structural needs. With the prolongation of the international crisis, exports have slowed down, which further reinforces the warning that growth cannot be maintained via household consumption, which, incidentally, also seems to have slowed down.

One should not forget the productivity differentials with similar products from China and the U.S. and the currency overvaluation, which until recently was approximately 30%. Thus, one must do much more than what is

34 It is the logistics package announced to the press on 8/15/2012, with total investments of R$ 133 billion; R$ 80 billion for the next five years and the remainder for the following 25 years. Their weight as an annual proportion of the GDP would be 0.4% in the first and only 0.05% in the following ones.

being done and proposed so that these businesspeople face competition and restructure the industry. Public subsidies and investments, however, are always limited, not only by the "obligation" of restricted fiscal behavior but also by the fact that the country signed the Uruguay Round (GATT) and joined the World Trade Organization (WTO) since 1995. Therefore, the government is always "hands tied". The WTO even admits some temporary measures, but these subsidies may become unacceptable to it.

One must remember that, at this moment, we are going through not just another crisis, but the continuation of a very long crisis that has been going on since the end of the 1970s. It is a disastrous cumulative process that not only destroyed our development institutions but also weakened the State itself, in addition to distorting the path of productive and progressive businesspeople.

This is the central issue of the Brazilian crisis, but it is not touched upon. None of the administrations in this long period tried anything deeper as necessary. For such a fact, one must face serious internal and external political and economic adversities. Brazil entered the so-called globalization, signed treaties, and assumed international commitments that it should not have. China declared itself a market economy but did not open the capital account. India did the same thing, as did Russia. Not opening the capital account means maintaining control over international and national capital inflows and outflows, profit remittances, and investment flows. Moreover, it means having an advanced degree of sovereignty in managing one's own exchange rate, fiscal, and monetary policy, which we do not have.

In Brazil, there is an industrial policy. There are important actions taken by several public agencies, such as the BNDES. There are, however, many misunderstandings. There are successes in the attempts to merge and solve structural problems of large national companies, even to try to strengthen them in the future in terms of international presence. At the same time, there is no macroeconomic and industrial strategy to make it sustainable and feasible to face deindustrialization, as pointed out by Cano and Gonçalves (2010).

Economists must learn that economics goes beyond the theoretical premises that neoclassical authors are so fond of. Economics is politics! Economics as a science is very limited. Economics is the result of social decisions made by people who have power. Whether entrepreneurs make decisions to invest or not, to buy or sell, or the State to adopt and try to enforce certain economic goals and objectives. This decision-making is always conflicting. Is always faced with diverse or even contradictory interests and, above all, with the uncertainty of their future success.

It is no use thinking about economics only from a technical point of view, of formulating a certain technical recipe, when the problem is political. If governments, after 1990, "sold their souls to the devil," that is, to the financial system, we need to break this covenant. This is, however, a very complicated attitude, because when you make a deal with the devil, he will demand your soul, after taking your liver and pancreas. In any case, current international political horizons are at least imprecise and unpredictable. There is, therefore, in my opinion, an open window for reflection on the future.

The US administration is Democrat, but the economic policy, in a way, is still controlled by the Republicans. In Europe, the picture is exactly the same. The most reactionary right is in charge of managing these problems and the crisis. There is a good interview by Professor Maria da Conceição Tavares on the website Carta Maior[35], in which she draws attention to the differences in relation to the 1929 Crisis. At that time, the winner was Roosevelt, and, through the New Deal, it was possible, in addition to taking measures for the economy, to look slightly more toward the poor and, from then on, Welfare State policies were developed in the western world. Attention must be paid to the crucial difference between the power structures before and after the 1929 Crisis and the current conservative and reactionary, and even deflationary, power structures. That is, judging by the performed attitudes and declared intentions thus far, they tend to deepen the crisis.

In Brazil, managing the 1929 Crisis and its subsequent period required a revolution, the 1930 Revolution. Here, a statesman, Vargas, anticipated those measures. Mexico had Cárdenas, and both knew, intelligently, how to lead their countries.

Brazil can and must face the structural crisis, referring, to a large extent, to the domestic market. There are almost 200 million inhabitants, a large territory, and a good endowment of natural resources. It is not the case to focus exclusively on the domestic market. It should be complemented by a National Development Program that has, in addition to this vector, a specific strategy for exports, technological introjection, and a sectorial and regionalized prioritization of infrastructure and high technology[36]. On the other hand, such a path cannot be aimed only at growth and productivity purposes but should include, as a priority, the sectors that meet the basic needs of the population and the country, such as popular housing, basic sanitation, public education and health, which, undoubtedly, should top the planning agenda.

35 Available from: http:// www.cartamaior.com.br/ templates/materiaMostrar. cfm?materia_id=17556. Access on: 12/21/2011. Interview granted on 03/17/2011.

36 The author recently published a proposal in this regard, in which the program is relatively detailed. See Cano (2010).

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CHAPTER 20

LABOUR IN THE LULA GOVERNMENT: reflections on recent Brazilian experience[1]

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Introduction

The objective of this paper is to analyze the set of changes in the Brazilian labour market, especially during the period 2004-2008. This is a period characterized by a significant increase in the pace of the economic growth (around 5% per year). It contrasts with the previous period, marked by the introduction of neoliberal economic policies in Brazil, when low annual average rates of economic growth (slightly above 2% per year), together with the impacts of the resulting abrupt structural changes, led to a strong deterioration in several aspects of the Brazilian labour market. Therefore, the higher growth rate was one of the most relevant aspects for the improvement of the national labour market observed during the period prior to the recent international financial crisis. For this reason, Section 1 of this study is devoted to an analysis of Brazilian macroeconomic dynamics, focusing on a discussion of the main determinants and the consequences of greater dynamism in the Brazilian economy.

The increase in the pace of economic growth had a positive impact on the Brazilian labour market in several respects: job creation, decreased unemployment, improvements to occupational structures, a rise in the proportion of occupations covered by labour legislation and a reduction in the enormous earnings inequalities within the country. The main characteristics of this process and its relations with the broader dynamics, as well as an assessment of

1 Translated by Camila Gripp and Steven Toff.

other aspects that are important for understanding the recent evolution of the Brazilian labour market, are themes covered throughout Section 2.

In addition to economic growth, the Brazilian labour market has benefited from a policy of revaluing the minimum wage, greater monitoring of compliance with labour legislation, and the results of trade union negotiations and pressure, as well as a set of important changes that were not immediate consequences of economic growth, but stemmed from the political relations established between workers, employers and government in various institutional bodies, as expressed in various relevant policies and actions. Thus, for example, the major expansion of income transfer programmes – either directly through the new "Bolsa-Família" programmes or through improvements in the wage floor and the coverage of the pensions system (old-age and other continuous benefits guaranteed by the Federal Constitution of 1988) – should not be regarded as a policy targeted at, and impacting directly on, the labour market. However, we do need to be aware that, together with the minimum wage policy, these improvements were indirectly very important for the expansion of employment, including formalized jobs in the small towns of the poorest regions and municipalities in the country. They galvanized demand, thus stimulating local commerce and production activities. These issues are examined in Section 3.

Section 4, devoted to final remarks, aims to highlight the more general outcomes and the significance of the changes, both macroeconomically and in Brazilian working life, while considering the enormous challenges for the future in a country still marked by a major set of social and economic problems.

Brazilian macroeconomic dynamics in the 2000s decade

Important elements of continuity can be identified in Brazilian macroeconomic policy between the second government of FHC (Fernando Henrique Cardoso) in 2006 and the first Lula government, but also important differences, such as the loss of momentum in the process of privatizing State companies and the strengthening of the National Economic and Social Development Bank (Banco Nacional de Desenvolvimento Econômico e Social - BNDES). As important elements of continuity, we may point to the policies of inflation targeting and flexible exchange rates – adopted by the Central Bank after the devaluation of the Real in January 1999 – and the primary surplus policy implemented by the Ministry of Finance.

Furthermore, this devaluation significantly changed the functioning of the Brazilian economy and its relationship with the labour market (Baltar, Leone,

& Borghi, 2009). One noteworthy aspect of this change was the effect of the rising value of the dollar. This caused a strong increase in the public debt, as a substantial portion of that debt was pegged to the exchange rate and was being used as a protection for investment capital portfolios built throughout the 1990s with resources borrowed from international financial market.

The devaluation of the Real, besides increasing the public debt in relation to GDP, brought back the inflation problem. The increase in the value of the dollar, resulting from the flight of capital, dramatically increased domestic production costs, as the opening up of trade had expanded the range of marketable products with prices set at the international level. Additionally, the privatization of public services entailed linking their prices (in national currency) to the general price index, which is very sensitive to international commodity prices (Carneiro, 2006). Thus, inflation would increase as a result of a broad rise in costs, which could become a new and widespread price-wage spiral, if workers – in order not to lose purchasing power – managed to get nominal wages readjusted in line with the price increases, and if companies were in a position to pass the increased costs on in their prices.

The IMF's support paved the way for the re-election of President Fernando Henrique Cardoso in 1998. This helped to set a policy which, while avoiding accelerated inflation, set out to maintain the recent opening up of trade and finance. So a macroeconomic policy was adopted that combined inflation targets, primary surplus in the government's budget and a floating exchange rate. The policy of a floating exchange rate represented continuity in exchange rate policy: the country continued to refrain from using the exchange rate as an instrument for guiding development, exporting more manufactured goods and depending less on imports of these products.

To attenuate the flight of capital, the interest rate had been set very high before the devaluation of the Real. After the devaluation, given the inflation target policy, interest rates were maintained at a very high level. The devaluation of the Real tended to have a positive impact on Brazilian economic activity, enabling greater exports and creating better conditions for domestic producers to compete with imported products. Nevertheless, the containment of public spending and the high interest rates were specifically aimed at maintaining a low level of economic activity, as a way of preventing a speed-up in inflation.

Due to the high interest rates, the trend was for the public debt to grow faster than GDP. The primary surplus on the public accounts was aimed at avoiding a disproportionate increase in the debt. To make this possible, there was a dramatic increase in taxes, especially social contributions. This increase in the tax burden had been occurring throughout the 1990s, as a result of the implementation of a social contribution scheme, provided for in the Brazilian Federal Constitution of 1988, which created a comprehensive social security system in the country. The total amount of taxes and social contributions increased from 25% to 35% of GDP. In addition, through measures adopted by the National Congress, the Brazilian Federal Government detached a significant part of its revenue (20%) from specific expenditures, and implemented the Fiscal Responsibility Law, facilitating action by the Treasury to contain expenditure (and even investment) and gain the capacity to pay a portion of the interest on the debt. The Brazilian government also used public funds and public banks to absorb a portion of the public debt, and the restrictive monetary policy meant continued use of the banking system to keep rolling over the huge debt, to the detriment of the loans needed to finance the economy.

From 1999 to 2003, the macroeconomic policy adopted only managed, at best, to contain inflation, leading to modest growth in GDP achieved primarily through the positive impacts of international trade. The currency was kept devalued over these five years and the performance of the international economy worsened in 2001, but it was possible to make up for the poor performance of the domestic market with an increase in exports and a reduction in imports, so that there was a reversal of the trade balance deficit of the 1990s, reaching an impressive surplus in 2002. In any case, beginning in 2003, the world economic situation improved for emerging countries. So the continuity of the basic lines of the macroeconomic policy implemented from 1999 onwards led to lower inflation rates and stronger GDP growth, from 2004 until the international crisis in September 2008 (Baltar, Santos, Garrido, & Proni, 2009).

The resumption of GDP growth began with exports and was later consolidated by the increase in consumption and investment, in a context where there was also a major increase in imports. The Brazilian economy benefited from the favourable international market, since it is a major exporter of commodities together with manufactured products, mainly to commodity-exporting countries and the USA (Hiratuka, Baltar, & Almeida, 2007).

However, this recent experience of abrupt devaluation of the Real prompted the repayment of a not inconsiderable part of the foreign debt (public and private), and external loans were focused on financing exporters. The expansion of the domestic financial market, fostered by the inflow of foreign capital and the increase in international loans, opened up space for big companies to place debt securities and property titles, with financing in national currency, as an alternative to taking resources from the international financial market in foreign currency.

Capital inflow (direct investments, financial market applications and external loans) compensated for the decline in the current account balance, and it was therefore possible to maintain the accumulation of international reserves. The increase in the international reserves, however, did not prevent the process of appreciation of the Real that intensified in 2004 and was only interrupted by the effects of the recent international crisis. With the appreciation of the Real, inflation finally decreased and GDP growth was accelerated, bringing positive impacts in terms both of increased consumption and of increased investment.

This growth was boosted by a substantial increase in jobs, formal employment, labour earnings, income transfers and the real minimum wage, which together resulted in a significant increase in family income, particularly for those in the intermediate and lower strata of family income. This process of increasing consumption and investment was also favoured by a combination of family income increases and the expansion of consumer credit - driven by longer repayment periods, falling nominal interest rates and institutional changes that began to allow the direct deduction of repayments from wages (check-off loans). As a percentage of GDP, loans by the banking system – which decreased steadily from 33.7% in 1995 to 24.2% in 2002 - have been increasing since then and reached 41.8% of GDP in 2008. In a scenario characterized by higher GDP growth, lower inflation, significant availability of international reserves and lower external debt stock (public and private), companies and banks expected continued growth in sales, production, employment and income. In fact, before the international crisis hit the country, GDP growth had accelerated, reaching an annual rate of 6.5% in mid-2008, through a process in which the volume of investment had been rising at significantly higher rates (Baltar, Leone, & Borghi, 2009). With that came an expansion in consumption of consumer durables, companies increased their investments in production capacity expansion, and the state resumed investment in infrastructure. Thus, even though the actions of the Central Bank of Brazil, aimed at containing inflation, had hampered the provision of loans in national currency and maintained a high level of interest rates (with negative impacts on the pace of economic growth), the average growth rate of the Brazilian economy rose significantly.

At the heart of the difficulties the country currently faces if it is to return to a more intense and continuous pace of GDP growth is the challenge of restoring the engine of growth, in other words, boosting the expansion of the process industries. Throughout the industrialization process, the country built a diversified and integrated industrial sector, mainly geared to domestic demand. Since 1980, industrial output has grown very little, with its share of GDP decreasing from 34% to 16% in the context of nearly a quarter century (1980- 2005) of semi-stagnation in the Brazilian economy, during which per capita output has barely increased. This loss of momentum in the industrial sector is related to the decline of investment in the country, with gross fixed capital formation currently ranging between 14% and 18% of GDP, while in the previous period of industrialization and sustainable growth (the late 1960s and the 1970s) it had reached much higher levels (between 20% and 25%).

The opening up of trade and finance during the 1990s did not substantially alter this picture of low industrial dynamism and GDP growth - with average rates of growth even lower than those of the 1980s. The coefficients of exports and imports in the industrial sector increased, and this sector certainly became more efficient, but there was also a significant loss of density in manufacturing production chains, which reduced the possibilities of increasing aggregate value and therefore the power to carry other sectors of activity.

The firmer and continued resumption of growth in industry, and also in the GDP, currently requires expansion of investment rates with infrastructure creation and a restructuring (densification) of production chains for manufactured goods. This would increase industry's capacity to create aggregate value in industry and its power to stimulate other activities, besides helping to increase the share of industrial exports and reduce the country's dependence on imported manufactured goods. Increasing the investment rate, however, entails going beyond the amount of investment induced by sales growth. It requires a more active government role in its relationship with the private sector and in the expansion of economic and social infrastructure.

From the second government of President Lula onward, following his re-election in 2006, the government has clearly taken a different position on economic growth, despite the continuity in the macroeconomic policy based on inflation targets, primary surplus in the government's budget and the policy of floating exchange rates (Barbosa & Pereira de Souza, 2010). One symptom of this change was the refusal to deepen out fiscal adjustment, which was a refusal to implement a policy suggested by (some) economists and conservative segments in Brazilian society. The implementation of a more restrictive fiscal policy, which aimed at a higher nominal primary surplus in the public accounts, was suggested as a way of taking advantage of the possibility of increasing the primary surplus brought by the higher rates of GDP growth and tax collection. From this perspective, the nominal surplus would help to cover the full payment of interest on the public debt, accelerating the decline of this debt in relation to GDP - an absolute priority for those interested in developing a more sophisticated financial sector, even though this could hinder more robust development of manufacturing in the country.

Thus, the government opted to launch the Growth Acceleration Plan (Plano de Aceleração do Crescimento - PAC), in order to restore public service staffing and pay levels, both of which had been sacrificed significantly during the earlier effort to contain public spending; maintain the pace of increase of the legal minimum wage and take on the increasing cost of social security, whose minimum benefit levels are linked to the minimum wage; and restore public investment, especially in infrastructure. Another symptom of this change in the government's position was the funding by the National Treasury of the BNDES (National Bank for Economic and Social Development), and the intensification of its activities such as forming national business groups and supporting investment by public enterprises.

Finally, the government's response to the international crisis at the end of 2008 also expressed this change of position. Although it acted late, due to fear of an increase in inflation caused by the devaluation of the Real, the Central Bank lowered the basic interest rate in Brazil (the Selic); loosened bank reserve requirements; used the international reserves to guarantee export financing; temporarily reduced the tax (IPI) on consumer durables (cars, domestic appliances, building materials, furniture and other products); launched a programme to build affordable housing (My House, My Life); reduced income tax for the middle class; used the public banks to ensure that demand for credit was met and to incorporate financial institutions weakened by the crisis; and ensured bank lending to the micro and small enterprise sectors.

These changes, which reflected the new attitude of the Brazilian government to the conduct of economic policy and to managing the impacts of the international crisis, along with new oil discoveries in the pre-salt layer along the Brazilian coast, have set a new context marked by optimism - or at least hope - that the country can achieve a sustained process of economic development, on which can be built the material foundations for a progressive improvement in the welfare of the population as a whole. The new posture of the Brazilian government - especially its reaction to the threats posed by the international crisis, but also the way in which it conducted the debate on the institutional construction necessary for the country to benefit more from the new oil extraction opportunities - has led to a rapprochement between the state and private enterprise. This has contributed to more concrete thinking on the possibilities for reconstructing the instruments of government action, necessary for strategic investment projects that are fundamental to a substantive development of the Brazilian economy.

Improvements in the Brazilian labour market during the period 2004-2008

In this period characterized by an increase in the average rate of growth of the Brazilian economy, the labour market showed significant changes which, all in all, have led to significant improvements: a decrease in average unemployment rates, an increase in formal[2] waged jobs (covered by Brazilian labour laws and the social security system), employment growth in the most organized sectors of the economy (including large companies and the public sector), a reduction in the proportion of unprotected waged jobs and self-employment on the labour market, a substantive increase in the real value of the minimum wage, the recovery of the real value of wages negotiated in collective bargaining agreements and conventions, a large decrease in unpaid work, the intensification of the fight against forced labour and a substantial reduction in child labour[3]. However, before examining the main changes observed in occupational and income structures over this period, it is important to point out the major changes observed in the evolution of the economically active population (EAP) and the recent changes in its gender and age composition.

In Brazil, the economic participation rate for young people aged 15-19 decreased during the 1990s, but it is still very high compared with countries at similar levels of development, such as Chile, Argentina and Mexico. The differences between these countries are significant. For example, in 2005 the activity rate for young people (15 to 19 years old) was 52% in Brazil, 36% in Mexico, 25% in Argentina and 17% in Chile (ILO, 2007 in Welters, 2009). Currently in Brazil, half of the teenagers are looking for work, whereas 20 years ago this proportion had reached 75%. At that time, the first attempts to enter the labour market occurred before 15 years of age, so young people aged 15-19 had already been fully inserted into the labour market. This fact was, amongst others, one of the symptoms of the disintegration of the Brazilian labour market, and it has been changing in the meantime, but even today half of the population in this age group participates fully in economic activity, although increasingly, this population also attends school[4].

The changes observed for those older than 15, according to age groups, reflect modifications that have been occurring in birth and mortality rates as well as in the pattern of Brazilian population growth since the late 1960s:

2 To be considered as a formal worker, one needs the Carteira de Trabalho e Previdência Social (CTPS, Work and Social Security Card) which records a worker's employment history, qualifications and social security entitlements. The card is, in theory, required for any provision of work by one person to another. Throughout the English version of this paper, the phrase "emprego sem carteira de trabalho" has been translated as "informal employment" or "unprotected employment" – Editor's note.

3 Despite the effort to eradicate child labour (for children under 16 years of age), the Survey "Pesquisa Nacional por Amostra de Domicílios" (PNAD/IBGE), conducted annually, shows that 1.5 million adolescents aged between 10 and 14 years participated in some economic activity in 2008, accounting for 8.4% of all people in that age group. Furthermore, 10.5% of the economically active minors had not performed any work activity during the reference week of the survey, but had taken initiatives to find a job. Among those minors who had had an occupation during the reference week, two-thirds were working without payment, in most cases for a family member, and almost all the rest were unprotected employees.

4 In this analysis of the economically active Brazilian population, we will concentrate on the population aged 15 years old and above, divided into three major age groups: 15 to 24 (youth), 25 to 54 (adults) and 55 and above (seniors).

the number of people in the 15-24 age group was less in 2008 than it was in 2004; for older age groups, it can be observed that the number of people aged between 25 and 54 and those aged 55 years and over grew at annual rates of 2.3% and 4.7% respectively (Table 1). The strong increase in the population aged 15 and older is a result of the rise in the adult and senior population. The growth of the adult population, between 2004 and 2008, reflects the significant growth of the Brazilian population in the 1970s, while the increase in the senior population reflects not only the more intense growth in the Brazilian population before the 1970s, but also the increase in life expectancy that has been occurring in Brazil since then, which has led both to an increase in the number of people who reach old age and to a lengthening of this stage of people's lives.

Thus, over the period 2004-2008, there was an increase in the participation rate within the working age group, mainly explained by an increased participation rate among adult women[5].

Table 1 – Total working age population and economically active population (EAP) Brazil: 2004 and 2008

Age Groups	Total working age population (15 years old and over)			EAP		
	2004	2008	Annual Growth Rate	2004	2008	Annual Growth Rate
15 to 24	26.3	23.4	-0.9	24.5	21.6	-1.2
25 to 54	55.3	56.1	2.3	65.1	66.5	2.5
55 and over	18.4	20.5	4.7	10.4	11.9	5.4
15 and over	100.0	100.0	1.9	100.0	100.0	1.9

Source: IBGE-PNAD, 2004 and 2008.

Despite the resumption of economic growth, unemployment reached 7.1% in 2008. Moreover, of the total economically active population, 31.2% were still occupied as self-employed workers, employers or non-remunerated workers or engaged in subsistence farming or building their own homes. Thus, wage employment did not cover more than 61.7% of the economically active population, of whom 33.7% were informally employed (a form of illegal use of the wage labour force in Brazil) and 10.9% were employed in paid domestic work. Therefore, when assessing the impact of Brazilian economic growth on the absorption of the economically active population, it is very important to differentiate the wage labour market (formal and informal commercial

5 The participation rate for men fell from 81.2% to 80.5% and for women increased from 57% to 57.6%. For people aged between 15 and 24 years old there was a decrease in the participation rate of men, while the participation rate of women remained constant. For adults (25 to 54 years) and seniors (55 and over) the participation rate remained constant for men and increased for women. For the whole group of 15 years and older, the participation rate remained constant (68% in 2004 and 2008).

establishment employees and formal and informal paid domestic workers) from the rest of the occupational positions (self-employed, employers, subsistence farmers and unpaid home construction and other unpaid workers). Also, the boundaries between paid work and unpaid work in Brazil are difficult to establish because the flexibility of wage labour has led to an increase in self-employed work that is just a disguised form of wage labour. That is, an important part of what is recorded in the statistics as self-employed work is actually disguised wage labour, and this leads to an underestimation of the part played by the wage labour market in absorbing the economically active population (Leone & Baltar, 2008).

In Brazil, there are important differences in the labour market participation rate according to age and gender. The higher the age, the lower the participation rate as employees (formal and informal commercial establishment employees and formal and informal paid domestic workers). So the adult and especially the senior population account for a larger percentage of the self-employed and the employers (usually in small businesses)[6].

Despite the substantial fall in the economically active proportion of those aged 15 to 24, the considerable reduction in unemployment during the period 2004-2008[7] failed to significantly alter the unemployment situation among young people - who were mainly seeking wage employment – as in 2008, this group was still marked by a very high unemployment rate (Table 2). In contrast, among adults and especially among the elderly population, besides the unemployment reduction, the situation in 2008 reflected the fact that not only unemployment rates were lower, but also a more substantial number defined themselves as self employed or employers – that is, they were not seeking an occupation as a waged employee[8]. Unemployment amongst women has remained much higher than amongst men, especially in the youth and adult groups. Women also continued to have a greater presence in the most precarious types of occupation: informal wage labour, unpaid work, unpaid domestic work and subsistence agriculture (Table 3).

6 Within the youth group, the proportion of unemployed, employed and paid domestic workers reached 79% of economically active young people in 2004, rising to 88% in 2008.

7 Still for the youth group, the major improvements in the Brazilian labour market during this period were the decrease in unemployment and increase in formal employment. Moreover, the proportion of domestic work absorption of young workers has decreased and so has the proportion of unpaid labour.

8 In the case of self-employment, small businesses were taken together with disguised wage labour. On the other hand, the great prevalence of the employers' category in absorbing the active adult and senior population reflects the narrowing of the labour market caused by 25 years of economic stagnation, along with the relative importance of small businesses run by the adult and senior population, in a country where the regulation of economic activity is very weak. The decrease in self-employment for adults and seniors in the absorption of the EAP was also very important.

Table 2 – EAP absorption according to age groups. Brazil: 2004 and 2008

Occupational status	15 to 24		25 to 54		55 and over		15 and over	
	2004	2008	2004	2008	2004	2008	2004	2008
Unemployment	18.0	15.5	6.4	5.2	2.7	2.1	8.9	7.1
Formal employment	29.1	35.2	39.0	43.7	17.1	20.2	34.3	39.1
Informal employment	25.6	26.6	14.3	13.5	10.7	10.3	16.7	15.9
Formal domestic work	0.8	0.6	2.3	2.3	1.1	1.4	1.8	1.8
Informal domestic work	5.4	4.3	5.3	5.2	3.6	4.3	5.2	4.9
Employer	0.6	0.7	4.5	4.8	7.0	7.1	3.8	4.2
Self-employed	7.9	7.4	22.1	19.7	38.7	36.2	20.3	19.0
Unpaid	10.4	7.1	3.6	2.9	4.8	4.3	5.4	4.0
Subsistence farming	2.1	2.5	2.4	2.6	14.0	13.8	3.5	3.9
Own home construction	0.1	0.1	0.1	0.1	0.3	0.3	0.1	0.1
EAP	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: IBGE-PNAD, 2004 and 2008.

The increase in the average growth rate of GDP over the period 2004-2008 resulted in significant positive impacts on the Brazilian labour market. Not only did the labour market absorption of working age people increase and unemployment go down, there were also improvements and important qualitative changes in the occupational structure: the relative importance of informal employment, self-employment and unpaid work within the occupational structure declined[9]. Thus, changes in the composition of occupations by sector, reflecting the resumption of economic growth and its positive impacts on the expansion of formal employment, reduced the weight, within total employment, of sectors that attract workers who are generally seeking survival strategies and have no alternatives at times of high unemployment. That is, sectors marked by precarious employment and non-wage labour, not covered by the labour legislation and associated with very low work income were reduced. Thus, there was a reduction in the rate of increase of non-wage labour (self-employed workers or employers) and unprotected employees. These figures rose much less than those for formal employment. From 2007 on, there was even a reduction in the absolute number of workers in these two occupational groupings, coupled with higher growth of GDP and of formal employment (Baltar et al., 2009). The share of informal employment in the occupational structure was reduced from 27% in 2004 to 25.4% in 2007, while that of non-wage workers fell from 29% to 27.6% in the same period.

9 Nevertheless, agriculture, domestic work and other services still accounted for 24% of total employment in 2007.

Table 3 – EAP absorption according to age group and gender. Brazil: 2008

Occupational Status	15 to 24		25 to 54		55 and over		15 and over	
	Men	Women		Men Women	Men	Women	Men	Women
Unemployment	11.9	20.5	3.5	7.4	1.9	2.4	5.2	9.6
Formal employment	37.0	32.6	47.8	38.7	21.5	18.1	42.1	35.2
Informal employment	30.9	20.8	15.6	10.8	13.0	6.1	18.7	12.4
Formal domestic work	0.1	1.2	0.4	4.6	0.3	2.9	0.3	3.7
Informal domestic work	0.4	9.6	0.4	11.0	0.9	9.6	0.4	10.6
Employer	0.9	0.4	6.3	3.1	9.2	3.9	5.4	2.7
Self-employed	8.3	6.3	23.6	14.9	42.0	27.4	22.5	14.4
Unpaid	8.1	5.7	1.0	5.2	1.3	9.0	2.6	5.7
Subsistence	2.2	2.9	1.3	4.3	9.5	20.5	2.6	5.7
Own home construction	0.2	0.0	0.1	0.0	0.4	0.1	0.2	0.0
EAP	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: IBGE-PNAD, 2008.

On the other hand, it may be noted that just over half of the working population in Brazil are still non-wage workers and/or in situations that do not comply with the country's labour legislation. Together with the reduction in informal employment and self-employment in the occupational structure, there was a significant rate of increase of formal wage employment and of the weight of this category within the occupational structure. This significant expansion of formal employment - which began after the devaluation of the Brazilian currency and was intensified by the increased pace of economic growth in the period 2004-2008 – was a result of two different effects: on the one hand, a tendency towards formalization of businesses and labour contracts; on the other, an increase in the number of formal jobs generated by every percentage point of GDP growth. Thus, the process of increase in formal employment was very strong, due to modifications and expansion of the Brazilian productive structure, but also due to the formalization of contracts through the supervision conducted by the Ministry of Labour and Employment.

The good jobs associated with higher income (managers, graduated professionals, and technicians) increased at a particularly significant pace. The worst occupations, usually present to a greater extent in agricultural activities and the provision of services, also showed progressive formalization of contracts, which was accompanied by other qualitative improvements with respect to the occupational positions, and by an increase in average income and a decrease in inequality of earnings. Furthermore, the segment characterized by the worst occupations expanded at a lower growth rate than that observed for the segment with the best occupations (Baltar et al., 2009). So overall, this process meant a significant reversal of several negative trends, ongoing since the early 1990s and which had advanced along with the implementation of neoliberal economic policies and related measures that aimed to make the labour market even more flexible.

Determined by the higher rate and the characteristics of economic growth, in a context of high employment elasticity in relation to the economic product (average of 0.4, similar to the elasticity observed in the 1970s), the growth in the number of employees hired in accordance with the labour regulations (CLT) or the Statute for Civil Servants - the so-called “formal wage employment” - grew from 44% in 2004 to 47% in 2007 of the total working population with an income (Baltar et al. 2009). Moreover, as may be seen from Table 2, the proportion of formal employment in the whole economically active population aged 15 and above (a universe that also includes the unemployed) increased from 36.1% in 2004 to 40.9% in 2008.

This increase in formal employment occurred in all age groups, but there was an especially significant increase in the formalization of youth jobs[10]. This expansion of formal employment was also widespread in all sectors of economic activity, with annual growth rates of over 3%, except in some services and public administration, where the formal employment growth was slightly less than 2% per year[11].

The increase in formal employment also occurred in almost all occupational groups, particularly in management positions, sales occupations, highly skilled professions and technical posts. However, even in manual occupations in agriculture, for example, formal employment grew at a rate of 3.5% per year (Baltar et al., 2009). While formal employment in all the five types of occupation with a relatively high average income (managers, graduate professionals, technicians, administrative support services and armed forces personnel) increased their share of the total employed population, the occupations with lower average incomes continued to show lower participation, but the four types of occupation with the lowest average income (services, sales, agricultural and non-agricultural manual labour) reduced their share of total formal employment. Moreover, during this period, formal employment also

10 Still, the highest rate of formal wage labour is for those between 25 and 54 years of age (71.1% in 2008 compared to 53.7% for young people and 59.7% for seniors).

11 The degree of formalization continued to vary widely across the sectors and types of occupation. In five sectors with low average incomes (agriculture, construction, hotel services and food, domestic and personal services), the proportion of formal employment in the generation of new occupational opportunities was very low. In trade and repair and transport and communication, the average income is not so low, but the proportion of formal employment in total job creation was also relatively low.

showed high growth rates in large firms - particularly significant in view of the reduction it had suffered during the 1990s (Santos, 2006).

This overall increase (by age, industry, type of occupation, size of company) in the relative importance of formal employment occurred from 2004 on, simultaneously with an increase in the total employed population with an income, significant recovery of the average labour income, a strong increase in the total labour income, and a slight recovery of the share of the national income appropriated by the workers. The average work income in Brazil had been reduced during the 1997-2003 period, hampered by rising inflation and decreasing economic activity, especially after the exchange rate devaluation of 1999. Since 2004, the fall in inflation, together with the reactivation of the economy, has given rise to a recovery in the purchasing power of the workers' average income, a trend that has been strengthened by increases in the minimum wage and the wages of the better organized occupational categories. At the end of the period, however, the average income of workers was at a level very close to that of 1998. The resumption of economic growth from 2004 on has just begun to change this picture, enabling the average work income and the workers' share of the total national income to recover losses suffered since the devaluation of the Real in 1999.

Total labour income (between 2004 and 2007) benefited more from the recovery of the average income than from the growth of occupations. Furthermore, the increase in the recovery of the average income was generally higher in industry sectors where the average work income is lower than in the overall economy, reflecting the importance of the minimum wage increase policy for the recovery of the average work income. By contrast, as regards the increase in the total mass of labour income in the formal sector, the growth of formal employment was more significant than that of average income.

Thus, as the resumption of economic growth during 2004-2008 occurred in the midst of greater monetary stability and a reduced level of inflation, one of the more notable consequences was that economic growth not only contributed to a process marked by significant formalization of labour contracts, but also helped to create the momentum for an increase in the real value of the minimum wage and a rise in real wages, through the gains made by the more organized workers and their unions in the course of wage bargaining. All this led to a significant improvement in average labour income, indicating a trend towards decreasing inequality of labour earnings.

Despite the increase in the proportion of occupations with higher income, the average labour income increase showed even more significant impacts in the worst occupations, helping to reduce income inequalities. Moreover, the increasing proportion of formal jobs in the occupational structure was decisive for the changes in the composition of the total labour income, by occupational status, further reflecting the positive development of employment rather than average income. And in that sense, the greater relative increase in the average income from informal jobs and non-wage labour only prevented a further decline in their share of the total mass of labour income (Baltar et al., 2009)[12]. The reduction in the income differences of employed people was also expressed in the reduction of differences in average income by occupational status, which occurred for both formal employment and the total occupational positions. However, income differences in the total employment picture remained very high by industry sector and, especially, by type of occupation. The effects of the policy of increasing the value of the minimum wage, thus providing for stronger increases in low wages in the lower income sectors, were not enough to decrease the disparities in average sectoral incomes - not even in formal employment. Sectors and types of occupation with lower incomes are also those that have lower proportions of formal employment within the total occupation rate. This greatly exacerbates the differences in the socioeconomic situation of the workers, since compliance with labour laws entails guaranteeing various advantages to formally employed workers, such as paid weekly rest, holidays (with one-third of the wage as an extra payment), coverage by the severance payment fund (FGTS), assistance with transportation and food, and social security, among other labour rights.

However, the increase in wage employment, the formalization of labour contracts, the rise in incomes (particularly the lower ones, impacted by the raising of the purchasing power of the minimum wage), the trade unions' struggles and their collective bargaining achievements, resulting in real wage increases and falling unemployment, have all contributed to the increase in family income, especially for the lower income groups. Those categories that are better organized and have a higher average income also showed an increase in incomes, but greater significance should be attributed to the policy of progressive increases in the real value of the minimum wage, within a context of economic growth and increasing public revenue and work income. This has particularly benefited the workforce segments on lower incomes, helping to reduce the high existing inequalities not only in the labour earnings structure but also in the family income structure (Baltar et al., 2009).

Thus, the positive employment developments and the already cited recovery in labour income affected family income and - along with the credit

12 Even in 2007, formal jobs accounted for only 47% of the total number of paid jobs and 53.5% of the total weight of earned income. Informal employees represented 25.4% of paid jobs and accounted for 13.5% of labour income, while self-employment accounted for 27.6% of paid jobs and 33% of labour income.

expansion – they had positive effects on the level and structure of household consumption, contributing to the significant expansion of Grade C (intermediate consumption pattern), or the lower middle class, which became increasingly important as the basis of the enormous prestige and popularity of President Lula's second government.

However, we must contextualize this process of significant advances in the occupational and income structure from a historical-structural perspective of the economy and the labour market in Brazil. Thus, it is very important to note that even in a particularly favourable world economic situation, Brazilian economic growth over this relatively short period has not been extraordinary, and its positive impacts on the labour market may be seen as the beginning of a more extensive and time-consuming process, required in order to (i) reverse the negative changes in the labour market and income structures caused by the neoliberal economic and labour policies implemented since the early 1990s, and the resulting production restructuring, low economic dynamism and precarization of the labour market and labour relations, (ii) reduce the adverse effects that 25 years of stagnation in GDP have had on the labour market of an underdeveloped country, (iii) reduce the problems resulting from an occupational structure historically and structurally marked by informality, precarity and low wages.

Social regulation and public policies

As explained, the positive evolution of some of the Brazilian labour market indicators (in particular, the increase in the formalization of employment relationships and the rise in the average income of those at the bottom of the remuneration structure) is fundamentally related to the economic dynamics and the change of political environment. However, it is also necessary to highlight the contribution of public policy, the social regulation of labour, the role of public institutions and trade union action. Economic growth certainly has contributed to the virtuous character presented by these institutional factors, in the sense of a greater structuring of the labour market. In parallel, the need to respond to social demands related to employment and income, in a context of strong political tension, has led the government to adopt policies that would indicate concern for the poorest sectors of the population. That is, the explanation for the recovery of formal employment and wages over the decade must also include the importance of the legal framework, government policies and the trade union movement, as will be discussed below.

Labour regulation and the advancement of job formalization

In Brazil, “formal (or protected) employment” is the term used to describe jobs validated by a work card[13]. An employee with a formal contract has access to the social security system and the labour rights included in the legal framework. Unregistered employment is illegal, but is very widespread in the Brazilian labour market. Therefore, the growth of formalization means that a larger number of workers are theoretically protected, being assured access to the social security system which offers old-age pensions and protection in case of sickness, workplace accident or unemployment. Moreover, a great number of the labour rights recognized by Brazilian legislation - amongst which we may mention the “thirteenth salary” (year-end bonus), paid holidays, maternity and paternity leave, paid weekly rest and the minimum wage – are guaranteed only to those who are formally hired.

A further element to be considered is the curbing of the work flexibilization process. Brazil has followed the employment relations flexibilization agenda, albeit in a tardy and idiosyncratic way. In comparison with the main developed countries, flexibilization was late in coming, but it put in a strong appearance in the 1990s, in the context of an economic crisis, trade and financial liberalization with exchange rate appreciation and redefinition of the state’s role in the economy. It is idiosyncratic because the specificities of capitalism in Brazil are such that the country has always had a flexible labour market, especially after the military dictatorship, allowing the employer to adjust the quantity and price of labour to different economic scenarios. Therefore, unlike in the main developed countries, the social regulation of labour in Brazil has not achieved the same degree of protection.

Despite the chronic weakness of the social regulation of labour, the flexibilization agenda grew in Brazil during the 1990s, providing a set of ad hoc measures that increased the degree of flexibility, especially in the forms of labour recruitment, conditions of use and payment. Among the reforms, in this paper we highlight those introduced under the justification of incentivizing the maintenance or creation of jobs and reducing informality. The main changes introduced were: temporary work contracts, part-time contracts[14], suspension of contracts for periods of up to 5 months[15], adjustments to annual

13 See note 2 above.

14 These permit a working week of up to 25 hours. Labour rights are in accordance with the weekly hours worked.

15 The main measures that accompany the suspension of the employment contract are: a) the employee is to receive a “training allowance”, which follows practically the same rules as the unemployment insurance during the period of suspension of the contract, b) the employer may give a monthly allowance, not considered salary, during the period of suspension of the contract, c) the company is committed to offering a qualification course to the worker during this period, d) the employee will continue to receive food stamps through the Worker

work time, first jobs and temporary contracts in the public sector[16]. In addition to these recently created forms of contract, there are other forms of contract, including temporary forms, for the most vulnerable workers in the Brazilian legal framework.

Compared with the experience of developed countries[17], the modalities of atypical employment contracts are negligible in Brazil, as the prevalent arrangement in the formal labour market is the open-ended employment contract. As may be seen from Table 4, it is noteworthy that formal employment was stagnant during the 1990s and has grown strongly in the first decade of the 21st century. In the private sector, in 1999, the number of workers with open ended contracts was lower than in 1989. In the public sector, during this period, employment under the statutory regime increased, due to the effectiveness of the social policies laid down in the 1988 Constitution. Between 1999 and 2008, protected employment grew by 57.8%, jumping from 25 million to 39.4 million people employed under contract. Employment growth took place mainly through open-ended contracts, but temporary employment has grown by 60% in the last 10 years.

Table 4 – Evolution of employment relationships, Brazil: 1989-2008

	1989	1995	1999	2003	2008
Open-ended contract	20,729,491	18,284,300	19,182,600	22,361,112	30,547,223
Statutory	2,638,781	4,545,992	4,537,091	5,439,922	6,818,849
Non-effective statutory	-	446,226	719,761	1,124,094	1,146,023
Independent	109,577	90,549	124,636	115,731	90,767
Temporary/fixed-term	84,656	307,198	409,307	461,050	684,177
Minor apprentice	-	-	7,429	27,643	133,973
Other/unknown	924,063	81,471	12,441	15,375	20,554
Total protected jobs	24,486,568	23,755,736	24,993,265	29,544,927	39,441,566

Source: MTE-RAIS

Although the forms of employment that can be verified through the RAIS (Annual Social Information Report) increased from 1 in 1989, to 9 in 2008, temporary contracts have a low incidence, representing only 1.4% of total employment in the private sector. In the public sector, especially at the

Food Programme (Programa de Alimentação do Trabalhador), e) if the employee is dismissed after the end of the suspension of the contract, he/she is entitled to receive severance pay plus one month's salary, f) in case of dismissal, the employee can apply to the unemployment insurance and receive at least one month's benefit, g) the employee must receive retraining during the period of suspension, but upon returning to work, he/she comes back to the same position with the same pay.

16 There is no available statistical information for all the new modalities introduced.

17 Freyssinet (2006) shows that, in 2004, 13.6% of the contracts in the European Union had temporary status. In his data, the part-time contracts are excluded. See also CESIT/MTE (2006).

municipal level, there was an increase in temporary contracts, particularly between 1995 and 2003. However after 2003, in relative terms, there was a decrease in hiring of temporary and dismissible staff, especially at the federal level, due to the Terms of Adjustment of Conduct between the Ministry of Labour and the Central Government for the replacement of these workers (including outsourced workers) by workers hired through public competitions.

Except in the public sector, there was no increase in atypical contracting in Brazil. In a context of better economic performance, public institutions and trade unions contributed to fraud prevention and pushed companies to hire according to the law. However, despite the increasing formalization, it is important to emphasize that the labour market still features some characteristics that are very unfavourable to the employees, such as the structural manpower surplus, informality, self-employment and subsistence work. Alongside the expansion of open-ended contracts with social security coverage, the employer still has the freedom to break the employment contract without justification.

For example, in 2009, in the midst of the crisis, 995,000 formal jobs were created (15.2 million dismissals and 16.2 million new hires) among a total of 33 million employees registered by the RAIS. So the turnover of dismissals and contracts remained very high throughout the period under consideration. This freedom of the employer to break the contract unilaterally and unjustifiably was reaffirmed by the denunciation of ILO Convention No. 158, which was in effect in Brazil for only 10 months in 1996. It is currently being examined by the Federal Supreme Court, which is reviewing the constitutionality of the denunciation. The lack of growth of temporary contracts has not eliminated the possibility of expanding other forms of contracting that are not captured by the RAIS: outsourcing, hiring of independent contractors, internships and labour cooperatives.

The fundamental issue is that the recent evolution of employment has been overwhelmingly characterized by the expansion of open-ended contracts, encompassing 95% of all formally employed workers.

Besides the explanation based on economic dynamics, as discussed above, other important factors need to be taken into account in order to understand the recent process of the significant expansion of protected (formal) jobs. Among them, the following should be highlighted: a) the need to improve the state's revenue collection in order to tackle the growing public debt (as explained, to produce a fiscal surplus as a way of guaranteeing the conditions for honouring debt repayments), b) the role of public institutions, especially those responsible for monitoring and ensuring compliance with the social and labour regulations, c) the formalization of micro and small enterprises (where much of the unprotected labour is concentrated) allowing access to credit and tax incentive programmes, and d) union activity, channelling a social aspiration to access the social security system.

The role of public institutions

The public institutions in the field of labour protection have taken on the task of resisting a flexibilization process based on disregard for labour laws. Three of these institutions deserve to be singled out: the public system of inspection and monitoring which includes the Ministry of Labour and Employment (in the exercise of its supervisory powers), the Public Ministry of Labour (in the management of public civil actions in defence of collective interests) and Labour Justice, which is a body that guarantees labour rights.

The labour inspectorate has the role of verifying compliance with legal provisions on working conditions and the protection of workers while they are engaged in their activities. The Constitution of 1988 enshrines a federal competence for organizing, maintaining and carrying out labour inspections. These inspections are performed by the Ministry of Labour and Employment (MTE) through Labour Inspection Auditors (Nobre, Jr., Krein and Biavaschi, 2008).

In the 1990s, the tendency was to strengthen the direct negotiation mechanisms and foster the private settlement of labour disputes. In this spirit, an ordinance was enacted discouraging the official monitoring of collective agreements, the declared aim being to add value to direct negotiations. In parallel, the labour monitoring system fell into neglect.

But from 1999, with the need to improve the state's revenue collection, new ways to enhance the surveillance system, especially through monetary incentives tied to the payment of dues and the collection of FGTS fees[18], began to be implemented, and monitoring teams have gradually been reassembled, although they are still inadequate in terms both of numbers and of working conditions. But some progress was achieved from the point of view of reaffirming the ILO's principles on labour inspection, including increased independence for inspectors in the exercise of their public duties.

The contribution of the inspection system can be seen in the significant increase in formal jobs each year, rising from 250,000 in 1999 to 746,000 in 2007. Considering the size of the labour market, those numbers are not so high, but the exemplary effect should also be taken into account - when there

18 The FGTS (Employment Duration Guarantee Fund) provides for the payment of 8% of the monthly salary to compensate the employee in case of unjustified dismissal. This fund finances housing and basic sanitation construction projects.

are signs of increased surveillance, companies preemptively adjust to the law in order to avoid being fined.

In addition, two other factors need to be highlighted: 1) the creation of "Super Receita" (Super Revenue), unifying the social security and tax revenue auditing systems, providing the possibility of sharing information and thus improving the whole system of supervision, from 2004 onwards; and 2) the creation of mobile inspection groups to facilitate the Child Labour Eradication Programme (PETI) and the National Plan for Slave Labour Eradication[19] in partnership with the ILO as part of the National Agenda for Decent Work.

To sum up, after 1999 there was an improvement, though an insufficient one, in the monitoring system, which helps to explain the expansion of protected employment, the fight against child labour and slave labour, and the increase in companies' payment of payroll-linked social contributions (Nobre Jr, Krein, & Biavaschi, 2008).

The second public institution that must be mentioned is the Public Ministry of Labour (MPT), which can be regarded as a relatively recent institution, as its powers were redefined in the Federal Constitution of 1988 and its structuring process started during the early 1990s. This institution is vital to the judicial role of the state. With its permanent, autonomous and independent character and its task of preserving the legal order, the democratic regime and basic collective and individual interests, the MPT has become a key agent for the defence of social interests. As it is not subordinated to any other power or institution in the country, it has great autonomy in its role of monitoring compliance with laws. At the same time, it has full powers of action and intervention, imbued as it is with the role of defending society and of protecting the various collective and homogeneous individual interests. Moreover, it can act as an arbitrator or mediator in the resolution of collective labour disputes (Nobre Jr, Biavaschi, & Krein, 2008).

The MPT's action focuses primarily on collective labour issues that have impacts on social relations (such as the eradication of child labour and forced labour, the fight against all forms of discrimination, monitoring of fraudulent cooperatives and assurance of fundamental labour rights, notably formalization of employment). Its members (the MPT's prosecutors) are entitled to take the initiative in launching investigations into denunciations and to refer to the legal system any issue involving disregard for the social legislation affecting a collective of workers or society in general.

19 These are two programmes that have had a high level of activity, contributing to social awareness of two great ills still plaguing the Brazilian labour market. The programmes have been successful in reducing the number of working children and freeing people who were working in conditions akin to slavery.

The work of many labour prosecutors (often coordinated with the judiciary and trade unions) has shown positive results in reining in fraudulent practices. For example, in the state of São Paulo, the action of the Public Ministry of Labour was crucial to the fight against fraudulent labour cooperatives. It required that fake cooperative members be hired directly – i.e. with work card registration.

In short, the MPT plays an important role in monitoring compliance with the social legislation, helping to fight fraud and build respect for labour law across the regions.

The third public institution is Labour Justice - a specialized branch of the judiciary composed of over three thousand judges - which is structured and present throughout the national territory. Each year, it receives more than two million labour complaints. When examining the dossiers, its role is to ensure compliance with acquired rights through application of the labour legislation. Labour Justice verdicts contribute to the understanding of certain issues related to labour law. And its case law also has a standard-setting role.

Its contribution to the growth of formal employment can be identified particularly in two movements that have been consolidated during recent years, influenced by the current debates in society and the dynamics of the labour market. First, the recognition of the employee status (protected employment relationship) of "informal" workers, "trainees", "cooperators", "juridical persons" and "autonomous workers" when all the characteristics of a employment relationship are present: the existence of human work that is personal, on behalf of others, non-casual, dependent and paid. Therefore, the predominant jurisprudence has become one of condemning any evidence of fraud in the employment relationship. Thus, through individual actions of the Public Ministry or the unions, a vision of repairing people's rights within a disguised employment relationship has come to prevail. Although it is not possible to measure its effects, this approach has stimulated formal employment growth, since condemnation of fraud has prevailed (Nobre Jr, Krein, & Biavaschi, 2008).

Second, companies that outsource services have been held accountable when the contractor does not comply with labour laws. The recognition of accountability, or at least subsidiary accountability, induced many companies to adopt preventive measures in order to avoid the accumulation of future labour liabilities. That is, contractor firms became subject to monitoring by the outsourcing company. For example, formalization in sectors with highly outsourced services, such as private security, cleaning and maintenance, rose above the average level of formalization of the labour market.

The two abovementioned trends were more visible in the current decade, as the concepts of flexibility and deregulation of rights were on the wane in Brazil. Therefore, although insufficient to meet demands, the strengthening of the labour judiciary's capacity to act has helped to make possible the growth of protected labour contracts, in a context of continual improvements in labour market indicators and the recovery of trade union power.

Company regularization and State actions

Not only has employment undergone formalization, the same is true of companies. Some initiatives in this direction have contributed to the advancement of formal labour contracts, although it is not possible to measure their effects with precision. They are basically of two types: 1) legislation to give tax incentives for the formalization of small businesses (in particular the "Super Simples", which has reduced taxation and simplified bureaucratic procedures), 2) the requirement that companies regularize their tax and social security situation as a condition of access to credit and of participation in bids for public contracts.

As in the recent period there has been a strong expansion of credit offers and of public spending, an additional stimulus was created for the regularization of micro and small companies, which had already received tax incentives. Certainly, this has also contributed to the formalization of employees contracted by small businesses.

Secondly, although very fragmented and scattered, the trade union movement has sought the application of the rights enshrined in law, thus helping to bring a greater of proportion of workers within the scope of social protection.

The trade unions have legal advice services, tasked with advising on collective bargaining and, mainly, bringing labour complaints before Labour Justice. Most of the unions, given their low representativity and their weakness, opt to go to court in order to resolve workplace disputes, especially those related to compliance with the labour legislation. It must also be said that in unfavourable times (as happened in the 1990s) many unions, in the name of allegedly maintaining employment, took a somewhat lax approach to the application of rights, and this implied less social protection for their members.

Although union fragmentation has increased recently[20], it may be surmised that many unions, in a more favourable economic context, will help to

20 Organizing rates are fairly low, but trade unionism did manage to maintain its representativity in a context of the deep fragmentation of the working class and changes in its composition. According to the most recent census, taken in 2001, there were about 16,000 trade unions in Brazil. In the meantime, that number is likely to have increased.

press the public institutions and the companies for greater formalization of employment contracts.

Under the Lula government, a certain strengthening of many union bodies may be noted, particularly due to two phenomena: 1) there have been improvements in collective bargaining outcomes (as will be discussed below); and 2) unionization rates have increased, but only slightly, rising from 16.7% of all those employed in 2001 to 18.2% in 2008. For formal employees alone, the rate reached 26% in 2008, according to the PNAD (National Continuous Household Sampling Research Programme). Within this new context, worker pressure for access to basic social protection also grew, a pressure that was considerably reinforced by the trade union position of seeking support within the public institutions for the fight against fraud.

Finally, it is important to remember that the type of employment created in the public sector plays an important role in the dissemination of an employment pattern that serves as a reference point for the economy as a whole.

Despite the growth of public employment in the 1990s (due to the implementation of provisions in the 1988 Constitution, which has significantly expanded social policies), a downsizing trend in Federal Government and privatization of public enterprises prevailed during this period. On the other hand, public employment increased at the municipal level (e.g. in public schools and municipal health centres), but the jobs created in these spheres were of a pattern inferior to the one predominating at the Federal Government level.

In recent years, there has been a shift in the Federal Government's strategy, moving toward the reshaping of some civil service career structures through the holding of public competitions. In this sense, despite inadequacies and persisting problems of efficiency and quality, there has been an increase in public hiring. According to the RAIS, the civil service establishment (the actual complement of public servants) grew by 25% between 2003 and 2008, i.e. the public administration, at the three levels of the federal structure, was responsible for the hiring of 1.4 million people.

Public policies and income distribution improvements

A key aspect, when examining the nature of the policies adopted by a government, is related to the changes they cause in the distribution of income. In recent years, parallel to a better structuring of the national labour market, income inequality showed a small decrease, as measured by the Gini index (from 0.58 in 2003 to 0.55 in 2008). Certainly, income inequality in Brazilian society is still very high, but there is a clear trend towards improvement, which can also be measured by the ratio between the income of the richest 10% and the poorest 40% (Table 5). The improvement in the labour market configuration, which was more pronounced, had a very positive impact on the reduction of the numbers living in poverty: from 61.4 million people in 2003 to 41.5 million in 2008 (in relative terms, from 34.3% to 21.9% of the total population) and on the decrease in absolute poverty: from 26.1 million people in 2003 to 13.9 million in 2008 (from 14.6% to 7.3% of the total population).

Table 5 – Income inequality and poverty indicators. Brazil: 1999-2008

Year	Income inequality: Gini Index	Income ratio between the wealthiest 10% and the poorest 40%	People living in absolutely poor households (thousands)	People living in poor households (thousands)	Household income per capita (R$ 2008)
1999	0.59	22.95	23,955	56,183	540.21
2001	0.60	23.34	25,406	58,489	547.70
2003	0.58	21.42	26,069	61,386	515.97
2004	0.57	19.91	23,326	59,542	528.08
2008	0.55	17.13	13,889	41,461	661.11

Source: IBGE-PNAD. Indicators elaborated by IPEADATA.

The improvement in income distribution, the reduction of poverty and the increase in the average family income were all made possible by the resumption of economic dynamism and its impact on raising the level of wage employment, as explained above. But if the employment increase was important to bringing a greater number of workers into paid occupations - which meant, in many cases, achieving the income needed to get the family out of absolute poverty conditions (or even to reach Grade C) - the effects of other public policies cannot be disregarded. Thus, it is necessary to highlight the importance of the minimum wage revaluation policy, the social security policies, the conditional income transfer policies and labour market policies.

Minimum wage revaluation policy

The adoption of a policy to ensure real increases in the minimum wage is central to an understanding of the reduction of income inequality among waged workers in recent years. The legal minimum wage, since the implementation of the Real Plan in 1994, had been recovering its purchasing power. However, the real recovery gained momentum from 2005 on, when the Federal Government made an explicit commitment to promoting the growth of the real value of the minimum wage. The value increase that took place between 2003 and 2008 exceeded the inflation rate, providing workers at the base of the income pyramid with real significant gains (38.3%). The government established a policy of annual adjustment that takes account of past inflation and adds up the average GDP growth of the two previous years, so ensuring that the minimum wage is increased as the economy keeps growing.

It is important to note that in the period prior to 2004, GDP stagnation and rising inflation caused a severe decline (estimated at 17%) in the average work income level, between 1998 and 2003 (Lopes, 2009; Brito, 2008). The minimum wage in 2003 was 9.7% higher than in 1998, but the average income of 50% of workers with lower incomes fell by 8.5% between these two years. The protection of the purchasing power of the lower labour incomes through increases in the minimum wage, higher than the inflation rate, did not prevent total labour income from decreasing after the devaluation of the Real, despite the observed increase in employment elasticity of GDP growth and the tendency to formalize labour contracts.

Graph 1

Source: IPEADATA.

This scenario has changed significantly since 2005. It should be noted that in parallel to the more pronounced increase in the minimum wage, there was a significant increase in the median wage[21]. Inflation eased after 2003 and the GDP growth and job creation helped the professional categories, from 2004 onwards, to obtain wage increases higher than inflation. However, the minimum wage increased more than the median wage, shifting the relationship between them from 0.50 in 2004 to 0.55 in 2008. The purchasing power of the minimum wage increased by 31.4% and that of the median wage by 23.5%, but the median value was very low in 2004, so the increase between these

21 Wages of employees of a commercial establishment, excluding domestic workers and considering only the job contracts formalized in accordance with the law.

two years only made the purchasing power of the median formal wage return to its 1998 level. Furthermore, the increases in average income, occupation rates and total wages have meant that labour's share of national income has begun to recover in recent years.

It should be stressed that in orthodox economic literature, it is commonly argued that increasing the minimum wage always leads to some job losses and some inflationary pressure (Neumark et al., 2006; Firpo & Reis, 2006). Moreover, in the aforementioned study, Neumark affirms that the effects of raising the minimum wage are adverse to the poorest families. Undoubtedly, the recent Brazilian experience contradicts this assumption and indicates a very different path, emphasizing the importance of public regulation of the national labour market[22].

The importance of the minimum wage in the Brazilian case is due to the large proportion of workers earning wages close to this level. Employees who are formally hired cannot receive less than the established legal value. Moreover, most of the employees hired informally - unregistered - and some of the self employed workers have the minimum wage as a reference point for their remuneration. Thus, the minimum wage is an important legal instrument that allows the state to contribute to a better structuring of the Brazilian labour market.

The positive impact of the policy of increasing the minimum wage is probably higher for the group of workers whose union organization is weak or rather inactive. In the worker categories for which the wage floor is equal or close to the minimum wage, raising the benchmark meant an increase that would not have been reached through collective bargaining. Therefore it contributed to the reduction of wage dispersion, or at least to reducing the pay differential amongst employees. As the minimum wage functions as a beacon or a benchmark for labour market remuneration, the increase in the real value had a positive influence on wage negotiations, especially on setting normative floors for some occupational categories (Dieese, 2008).

As mentioned, in addition to increasing the average income of the lower-paid employed workers, thus helping to improve income distribution, this policy contributed to reducing poverty and expanding household consumption. The minimum wage increase also had an indirect effect on the living conditions of poor families, especially those composed of seniors and children, due to the existence of welfare policies and income transfer programmes whose benefits are linked to the value of the minimum wage.

22 As well as the increase in the minimum wage in a context of economic growth, the increase in the median wage also had the effect of boosting the decrease in income inequality. Previous studies (Soares et al., 2007) showed that the money transfer programmes (Bolsa Família and others) also helped to decrease inequality, but the effect of the income increase was greater.

Social security

The Federal Constitution (FC), enacted in 1988, established a national system of social security based on income redistribution mechanisms. In particular, the FC settled a historic debt, equalizing the rights of urban and rural workers. The latter had an inferior status upon retirement. So a non-contributory scheme was brought in for rural workers. Also, a welfare benefit was provided for people aged over 64 who were in households with a per capita income of less than one quarter of the minimum wage, whose occupational activity had been concentrated in the informal market and who were unable to prove how long they had worked. For these workers and for impoverished people with disabilities that prevent them from living independently, the Continuous Money Benefit (BPC – Benefício de Prestação Continuada) was created. In both cases, the benefit cannot be below the value of the minimum wage (in line with the general Social Security guidelines for retirement or survival benefits).

The explicit policy of revaluing the minimum wage, as implemented since 2005, did not worsen the deficit of the social security system (most pensioners receive the minimum benefit), as the good economic performance and the expansion of formal jobs have boosted the system's revenues, pushing down the current deficit. On the other hand, the increased purchasing power of the rural pensioners and other poor beneficiaries, besides improving the living conditions of these families, has resulted in increased disposable income in smaller communities, especially in the North-East region of Brazil, boosting commercial activities and making the economies of these locations more dynamic.

Additionally, the greater effectiveness of the social security system has contributed, even though indirectly, to improving the labour market, insofar as a guaranteed income for seniors enables them to stop seeking work. In some cases, it also allows minors (dependents) to avoid premature entry into the labour market.

Income transfer policies

Policies of conditional income transfer were another important factor in improving the living conditions of the poor population as a whole. Implemented during the 1990s under the responsibility of various ministries, in Lula's government they were expanded and grouped in a single programme, the "Bolsa Família" (Family Grant Programme or PBF), coordinated by the Ministry of Social Development and the Fight Against Hunger, which incorporated the whole area of social assistance that previously was under the responsibility of the social security system. Although the institutional rearrangement and the new management were relevant to the implementation of the programme, the most important impact came from the expansion of coverage, which now extends to more than 11 million families.

The programme transfers a monetary supplement to families with an insufficient income per capita to avoid situations of extreme deprivation. In return, the families agree to maintain their children's and teenagers' school attendance, seek medical care for expectant mothers and newborn babies and withdraw their children from child labour.

It should be noted that the intention of this policy is for the benefit to work as a temporary support - that is, it should allow the family members some time to seek better insertion into the labour market and, once the financial difficulties have passed, the family is supposed to leave the programme. Some measures have been tried out aimed at creating the conditions for families to become independent of the programme, through an increase in household income. For example, if the heads of households are unemployed, they are individually referred to the Public Employment Service in order to be assisted and reinserted into a paid occupation. In cases when the work income is insufficient to maintain the family, those of working age are encouraged to join the labour market, even in self-employed occupations. Yet, even in the favourable circumstances of economic growth and employment expansion in the period 2004-2008, the vast majority of the families were unable to meet the conditions for leaving the programme.

Besides being an assistance programme to mitigate conditions of deprivation for the poorest families, the programme has contributed to reducing absolute poverty and has functioned as a mechanism for income redistribution. By removing children and adolescents from child labour and requiring their school attendance, it can help to prepare a better future for this generation of young people, and a better-qualified vocational insertion. However, this would require the Brazilian economy to remain impressively dynamic during the next decade, and the labour market to continue being restructured on new bases.

Labour market policies

Policies aimed at improving the functioning of the Brazilian labour market – particularly unemployment insurance, manpower services and vocational training – have always had little impact on income distribution and the occupational structure. Although a more dynamic economy combined with formal employment expansion could open up opportunities for a more important role to be played by these policies as instruments of labour market structuring and the promotion of decent work, few advances have been made on this in recent years.

Here, we will focus on the unemployment insurance programme, as it is a mechanism of income transfer. In the period 2004-2008, despite the economic dynamism and employment expansion, the number of beneficiaries of the unemployment insurance grew, contrary to what can be observed in other countries. This occurred because the greater formalization of jobs was not accompanied by a reduction in employee turnover rates (a result of the great flexibility that companies have to hire and fire, adjusting the quantity of work to their production or sales, which explains the high rate of hires and lay-offs over the years).

Thus, with the large number of jobs created in recent years, there was also an increase in the number of workers who met the minimum requirements for receiving the unemployment insurance benefit upon dismissal. The result was an expansion of the programme's coverage and increased spending on these benefits. The increased expenditure on unemployment insurance pay-outs stemmed partly from the larger number of workers in benefit and partly from the real increase in the minimum wage. This is because the minimum benefit is equal to the statutory minimum wage.

Unemployment insurance played an important role during the worst period of the economic crisis, between the end of 2008 and the beginning of 2009, providing income to workers who lost their jobs due to the sharp downturn in industrial production and the slowing of commercial activity. It should also be noted that the duration of the unemployment insurance benefit was extended to 7 weeks for workers in the sectors most affected by the crisis, thus avoiding a further worsening of the living conditions of a significant portion of the population.

Finally, it should be mentioned that the unemployment insurance has also been contributing to the promotion of decent work in Brazil. This is because workers rescued from slavelike labour are entitled to the benefit, guaranteeing them an income during the time it takes to reinsert them into the labour market. In this respect, the unemployment insurance plays a role that goes beyond what was originally conceived.

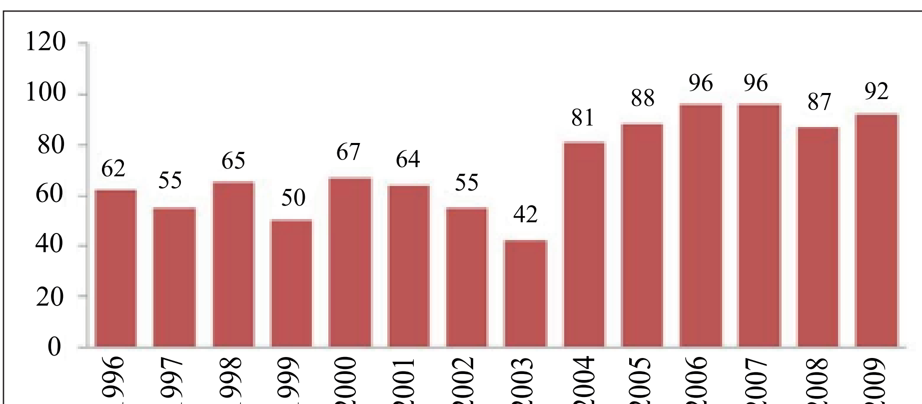
The role of trade unions and collective bargaining

Despite the existence of seven recognized trade union centres, the Brazilian trade union movement has been demonstrating unity in action in recent years. However, there are also countervailing pressures. On the one hand, its ability to mobilize the workers around the great issues on the national agenda does have limits. On the other, the growing strength of this player is apparent in the collective bargaining outcomes and in its capacity to dialogue with the Federal Government.

Despite some tensions, the relationship with the government has moved forward, especially since 2005, towards meeting various labour demands, prominent among which are: the minimum wage revaluation policy, recognition of the trade union centres and adoption of measures to tackle the recent crisis in 2008-2009. So the trade union movement, through the trade union centres, is an important interlocutor for the Federal Government, and is given the space to take part in the formulation of public policies. This relationship has been facilitated by the social origins of the President of the Republic and the institutional channels created by the 1988 Constitution, which broadened the participation of the social actors in the elaboration and implementation of public policies.

From 2004, as Graph 2 shows, collective bargaining outcomes improved, contributing to the recovery of purchasing power. Even during the crisis of 2008- 2009, a large proportion of the occupational categories managed to regain the purchasing power of their wages. What happened was that the negotiating climate changed, reversing the trend that had prevailed up to 2003. Rights are no longer being bargained away in exchange for the maintenance of employment.

Graph 2 – Per cent of wage increases greater than or equal to National Consumer Prices Index-IBGE growth rate, 1996-2009



Source: DIEESE data.

So the trend towards a better-organized labour market was strengthened. And, even though this trend was predicated on economic growth, it may be seen that the Brazilian judicial and institutional framework contributed to the fight against the most destructive forms of labour exploitation and in favour of more formalization of employment.

The times the country has gone through recently, with the relaunch of the development agenda, have increasingly shifted the trade union movement's focus from the simply defending jobs to winning back lost rights and broadening out its demands. Among the main issues around which the unions and the trade union centres are currently mobilizing are: i) reducing weekly working hours to 40; ii) regulation of subcontracting; iii) the minimum wage revaluation policy; and iv) defending a development model that distributes income and valorizes work.

One distinctive feature of the past few years had been the adoption of a joint agenda by the main Brazilian trade union organizations. In 2010, apart from the issues outlined above, the main action point will be to discuss a sustainable development model for the country, including income distribution and the valorization of work, and one of the events envisaged is the holding of a unity conference. So the union centres aim to take an active part in the national debate and influence the guidelines to be drawn up for the development model that the country will adopt. It should be emphasized that many of the issues cited have more to do with the trade union movement's relations with the present government than with the capacity to mobilize workers and society. The crucial point is that the prospects exist for putting a new, much more constructive, agenda up for discussion, deriving to a great extent from the recent changes in the Brazilian socio-political and economic context.

Final remarks

Workers' conditions in Brazil have undergone systematic improvement, notably since 2004. This is reflected in the increase in protected work, mainly on open ended contracts, the raising of the minimum wage, the recovery of the average wage, a drop in open unemployment and curbs on unprotected subcontracting. Families have seen a rise in average income, and a considerable reduction of poverty and need. The minimum wage revaluation policy, social security, income transfers and improved wage bargaining have contributed to a reduction in inequality. All of these elements point to a better incorporation of workers into the objectives of Decent Work (ILO, 2009). Despite these improvements, a number of structural problems remain, such as high labour turnover, informal employment, structural unemployment and the strongly heterogeneous nature of the occupational structures.

The reasons for the shift in labour market indicators have to do with the economic dynamics, public policy on the raising of incomes, and a legal and institutional framework in which the public institutions and the trade unions play a prominent role.

Currently, as discussed, opportunities exist for sustained development in the coming years. After 25 years of stagnating GDP and 15 years of commercial and financial opening, the most recent feature of the Brazilian economy has been its interrelatedness with the labour market. The country now has the possibility of moving towards a form of development which, if properly utilized, could possibly enable a better structuring of the economy and the labour market, increasing the well-being of the population as a whole. The characteristics of this development should include a policy of economic growth, an active industrial policy, coordination of efforts to solve the infrastructural problems, respect for the environment, expansion of the public services, linking up of production chains, investment in science and technology, and restructuring of the State.

Providing that employment can be generated, there is also the possibility of extending public labour regulation and social protection. So to guarantee a development that distributes incomes and valorizes work, there is a need to: strengthen public institutions as a way of fighting labour market fraud; introduce ILO Convention 158 in order to counter unjustified exemption mechanisms; implement a trade union reform so as to increase the representativeness of the class-based organizations and ensure trade union organizing rights in the workplace. It is also crucial that there should be continuity in the policy of revaluing wages, particularly the legal minimum wage.

Thus, the structuring of the labour market combines the creation of jobs, especially high-quality ones, with policies for the social regulation of work. In other words, a continuing improvement in the absorption of the economically active population requires economic growth and efforts to achieve better regulation of economic activity and wage employment.

In a society whose labour market is notoriously heterogeneous in structure, emphasizing the role of the State is essential. But that fact obviously does not detract from the need for a society in which workers have their say and for a truly representative trade unionism, with the strength to attain higher standards of social regulation of work. This is certainly one of the great political tasks of our time, implying as it does the creation of a development model that distributes income and dignifies citizens.

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CHAPTER 21

NAVIGATING AGAINST THE WIND: a prologue on the developmentalist experiment of the Dilma Rousseff administration

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Introduction

In order to analyze the failure of the developmentalist experiment of the Dilma Rousseff administration, we assume that the economic policy and its implementation are contingent on a broader context in which, in addition to class relations, there are structural and cyclical aspects in the economic sphere shaping the backdrop against which decisions are made. Thus, our thesis is that the Brazilian economy's trajectory during the 2011–2016 period can only be explained on the basis of the interaction between these three elements: the structural, cyclical and economic policy elements. From a substantive point of view, this chapter rejects two families of interpretations about the period: those of heterodox inspiration, for which the main reason for the failure was the contraction of aggregate demand, particularly that of public spending; and those of orthodox inspiration, for which excessive wage growth and the squeeze of corporate profit margins would have been the determinants of the investment contraction and subsequent crisis.

The slowdown of the 2003–2010 cycle imposed the need to seek a new growth model to overcome the limits of the previous pattern. To that end, the chosen course was to diversify the productive structure, so as to reverse the regressive specialization, and to expand the infrastructure, partly overused, partly dilapidated due to years of low investment. In this case, the main driving force would be autonomous, private and public investment, directly supported by State actions.

The distinction between autonomous and induced investment is crucial to understanding the character of the new growth model that should replace the previous one, in which the stimulus from exports and consumption had driven growth. The exhaustion of dynamism required a shift to a new investment pattern for which there was a set of obstacles. From the industry's point of view, the pre-existing demand did not fully justify it, due to the high production scales. And the technologies, in turn, were not immediately available.

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In terms of infrastructure, the risks were of diverse natures: of construction, environmental and its illiquidity were the main encumbrances to be tackled.

What kind of political arrangement would this new model demand? Certainly not that of the broad reconciliation of classes observed in the Lula administrations, during which, due to particular circumstances, it was possible to accommodate many interests. Making choices and clearly defining the segments that would integrate an interclass alliance was crucial. According to Singer (2015), one of the main problems of the Dilma administrations was broadening the spectrum of disputes, while not clearly defining the profile of the alliances and not deepening the support of the popular classes. The thesis highlights important points, but it needs to be qualified.

The fact that the proposed alliances were not successful does not allow us to think that there was no proposal for them or for how to strengthen them. From the perspective of the dominant groups, the model excluded financial capital and its cosmopolitan ramifications, but intended to rely on industrialists and large construction companies, as its point was, after all, reindustrializing the country and expanding its infrastructure. On the other hand, the new middle classes and workers were emphasized, broadening the spectrum of social policies and giving less importance to the traditional middle classes. A more leading role was also defined for the State and its bureaucracies, through its public banks, especially the BNDES, and also through Petrobras, the main instrument of the new industrial policy. Considering these attributes, two polar interpretations of the failure arise: either the implementation of the economic policy was in fact very poor or the project had little support in the social classes and groups of interest. This work is founded on the hypothesis that both factors played a role in explaining the failure of the developmentalist experiment.

Major structural changes: an outline view

The main structural conditioning factor for the period's performance was the rapid integration of the Brazilian economy into the globalized economy, starting in the 1990s. This vector was decisively affected by the financial crisis of 2007/2008, initiating, then, a peculiar period of the global economy, which coincides with the Dilma administrations. In the financial dimension of the integration, there is a permanent and growing instability, which is visible in the increased sensitivity of the domestic economy to the global liquidity cycle. The latter intensifies after 2009, as a result of unconventional monetary policies to tackle the crisis in central countries. Thus, the operation of the macroeconomic policy in peripheral countries is increasingly constrained by the nature and direction of these policies.

The productive sector is marked by the third industrial revolution, dominated by microelectronics, information technology and the constitution of global value chains, with the emergence of its main protagonist, China. Brazil remains relatively on the fringe of the process, having undergone a regressive specialization in the industry whose main characteristic was the increase in the participation of sectors intensive in natural resources and the loss of importance of the more technologically intensive segments. In terms of production, the crisis and the resulting slowdown in growth lead – on a global scale, but especially in Asia – to an excess of productive capacity spread across almost all sectors.

In summary, as discussed by Belluzzo and Galípolo (2017), in addition to a financialized economy in the developed countries, characterized by recurrent liquidity cycles and a major crisis in 2008, there was the adoption – in order to deal with this crisis – of an economic policy profile based almost exclusively on unconventional monetary policy (quantitative easing), which exacerbates liquidity cycles. In turn, the constitution of global value chains, with the fragmentation of production stages, concentrated in Asia and particularly in China, imposed an exacerbation of competition based on price reductions and intensified, after the crisis, by the widespread of idle capacity.

The financial dimension

Since the end of the 1980s, Brazil carried out a broad movement of financial integration into the globalized economy. According to data from the Central Bank (Bacen), Brazil's International Investment Position increased after a decade of opening, from US$ 480 billion (assets + liabilities) in December 2001 (approximately 85% of GDP) to US$ 2 trillion in December 2015 (around 110% of GDP). This figure is an important indicator of how financial integration influences the Brazilian economy's trajectory through its main transmission channel: the external liquidity cycle.

This quantitative change was followed after the crisis by the growth of external liabilities in more volatile forms, reflecting important changes in the international situation. According to Lane and Milesi-Ferretti (2017), after the crisis there were important changes in the intensity of the global financial integration, with a decrease in the participation of financial flows *vis-à-vis* GDP, expressing the deceleration of globalization among developed countries.[2] In addition, according to these authors, capital flows to peripheral countries

2 Other important characteristics of the capital flows were the shrinking of the balances of bank, hit hard by the crisis, with corresponding reduction in cross-border loans; partial offset of this movement by the growth of the bond market; an increase in FDI, but with a different profile, originated in the financial centers, reflecting the shift of corporate finance to these markets and, finally, an increase in the weight of public flows very associated with the European crisis.

exhibited the following profile in that period: during the crisis, in 2008/2009, a reversal based on flight to quality; between 2010 and mid-2013, a significant recovery; and, after this last date, marked volatility.

Considering another period, the work of economists Ahmed and Zlate (2014) and the work of Biancarelli et al. (2017) show that the intense post-crisis recovery occurs from mid-2009 and lasts until mid-2011, occurring from then a deceleration of capital flows towards the periphery, but above all an increase in their volatility. The peak observed in the first two quarters of 2011 has not been reached again since then. Values are very volatile for Asia, especially for China, and more stable for Latin America, but for both the drop is significant after mid-2013.

An important aspect highlighted by Ahmed and Zlate (2014) is that, of the three main determinants of capital flows to the periphery – the growth differential, the interest rate differential and risk aversion, measured by the VIX –, the second becomes more prominent, that is, portfolio flows start to show more sensitivity to this differential and less to the drop in risk aversion measured by the VIX. This, is the result of the unconventional monetary policy applied in the central countries, including zero-bound interest rates, quantitative easing (QE) and, more recently, negative interest rates. The consequence was the expansion of the so-called carry trade operations, which take different forms, seeking precisely to exploit interest rate differentials. This is one of the main reasons why flows to Latin America remain substantial, while those to developing Asia and China decline.

The unconventional monetary policy, in particular QE, has important effects on financial wealth and the formation of bubbles, including at the global level, as pointed out by the work of VOX/CEPR (2016), but its impacts on economic growth are uncertain. QE differs from conventional monetary policy not only because of its scale, but also due to its targets, long-term government bonds and corresponding interest rates.[3] Its main consequences, in addition to the long-term interest rates, are those on private portfolios, as their composition changes, increasing the weight of the currency and short-term bonds to the detriment of long-term bonds.

The assumption behind QE was that, by reducing long-term interest rates and increasing the liquidity of the agents' balances as a whole, it would favor financing, bank credit and private spending. This effect was limited as, in the banking sphere, the increase in liquidity was neutralized by an increase in preference for liquidity, leading to an increase in the purchase of short-term assets, but not in credit. In turn, increasing the liquidity of the portfolios of households and companies did not necessarily influence their propensities

3 At the beginning of QE, in the US, the Fed even bought substantial volumes of poor-quality corporate bonds that were in the portfolios of large banks, under the pretext of injecting liquidity into a system that was stuck.

to spending. Companies, mainly, but also households, chose to pay debts. Thus, the credit and spending circuit was less affected. In other words, the wealth circuit was greatly affected, but not that of income. The first led to the construction of positions in existing assets, such as stocks and bonds in developed countries and exchange rates, interest rates and commodities in peripheral countries, originating successive bubbles.

In the case of Brazil, it was not observed an adjustment in the level of capital flows after 2013. The explanation for why this has not occurred is linked to various types of carry trade operations, from intercompany ones to those of derivatives, aiming at exploiting the interest rate differential. The preservation of capital flows occurs at the expense of their quality, especially with the expansion of the more volatile forms. In summary, as suggested by Biancarelli et al. (2017), although there was no drought, the quality of flows deteriorates, responding more to short-term macroeconomic variables.

Productive aspects

The prevalent form of industrialization in the capitalist periphery, at least since the 1990s, was that which took place through the so-called Global Value Chains (GVCs), which correspond to the fragmentation of the production chains of discrete production processes. With the specialization in the core business, companies from central countries exported on a large scale, to the periphery of the system, the most wage-intensive production segments. This mainly benefited countries where the wage cost was lower, such as those in developing Asia, and benefited less middle-income countries, such as Brazil. Certainly, infrastructure, especially logistics, and other tax incentives were relevant, but the wage cost was decisive, as pointed out by Baldwin (2013).

As demonstrated in the work of UNCTAD (2013), Brazil was practically out of this pattern of development. The decomposition of the value of exports, into domestic added value and imported added value, shows the relevance of the chains for foreign trade. In the case of Brazil, and South America in general, the share of domestic added value in exports is very high, reflecting the export of raw materials and the weight of natural resources. In Asia – even in China, a continental country –, there is a distinct pattern, with the relevance of the imported added value, that is, of the chains, in the value of exports. It should also be noted that the constitution and operation of value chains does not have solely a technological significance. As analyzed by Vitali, Glatterfeld and Battiston (2011), the chains constitute a centralization of capital on a global scale and, therefore, a concentration of decision-making power concerning strategic variables such as investment, R&D, etc. in the countries of origin of companies or holding companies. Furthermore, as pointed out by Nolan, Zhang and Liu (2007), global oligopolies were also reinforced in the intermediary links of the chains and not just in their core.

This process of a global nature, in which Brazil participates asymmetrically, has as its characteristics a regressive specialization until 2010 and, after then, deindustrialization. The regressive specialization, with increased share of natural resource-intensive sectors in the industrial added value, had an exception: the expansion of transport material industry. Moreover, it also meant the rarefaction of production chains with the deactivation of domestic production of intermediate inputs with higher technological content, increasing the imported coefficient without the counterpart of the increase in the exported coefficient, with the exception of the transport material industry – for example, planes.

As pointed out by Sarti and Hiratuka (2017) and Diegues and Rossi (2017), despite the regressive specialization, deindustrialization – at least in its particular meaning of reducing the share of the industry in the GDP – cannot unequivocally be stated to until 2010. Between 2004 and 2010, both industrial product and investment showed good performance, including with the latter growing above GDP, as a result of the cycle's acceleration stage. Starting in 2011, deindustrialization accelerates as a result of the intensification of global competition, the drop in industrial prices and, in the Brazilian case, the disproportionate rise in imports.

The facts that compounded these trends are the 2008 global crisis and the Chinese response, through the countercyclical policy. As shown by Conti and Blisktad (2017), the increase in the rate of investment in the Chinese economy is not able to boost the GDP, whose growth decelerates progressively. The most important consequence of this fact is the emergence of widespread idle capacity in manufacturing in China and developing Asia. The data in Table 1 are significant with regard to continuous production sectors. However, this occurs in a widespread manner in China, as shown by the surveys of CKGSB (2016), implying an intensification of competition in several markets, including those in which Brazil had a significant presence, such as the US, South America and in the domestic market itself.

Table 1

China: Capacity utilization rate in selected sectors in 2008 and 2014 (%)

Steel		Aluminum		Cement		Oil Refining		Flat glass		Paper/Cardboard	
2008	2014	2008	2014	2008	2014	2008	2014	2008	2014	2008	2014
80	71	79	76	76	73	80	65	88	78	90	84

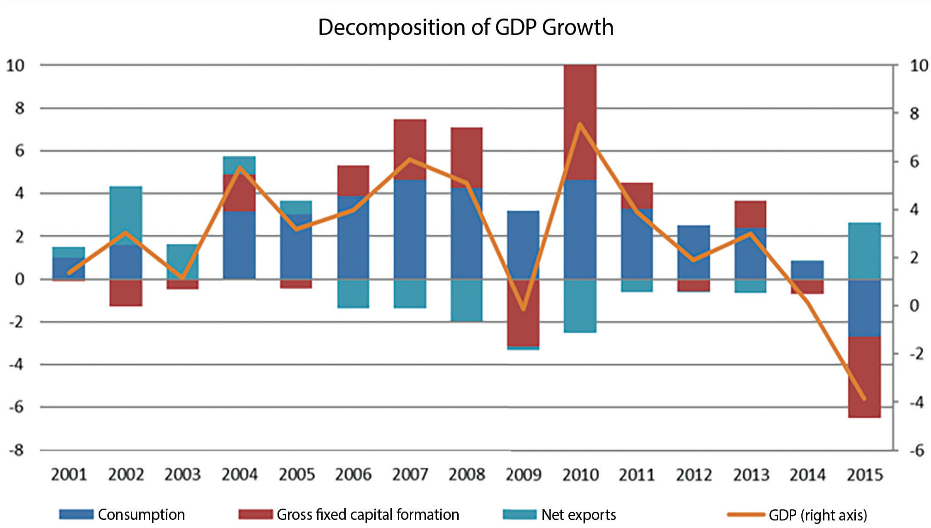
Source: European Union Chamber of Commerce in China. Overcapacity in China: An Impediment to the Party's Reform Agenda (2016).

Growth with social inclusion

Nationally, in the 2003–2010 period, the Brazilian economy saw an acceleration of growth. This growth, initially driven by commodity prices and net exports, gained momentum with the rapid growth in consumption and, later, with the expansion of investment induced by both. Net exports lose prominence very quickly, due to growing deficits in the balance of manufactured goods and services. Consumption, on the other hand, accelerates due to improvements in income distribution and to the credit cycle, leading to increased investment (see Graph 1).

This cycle progressively lost dynamism. On the one hand, due to the loss of speed in the improvement of income distribution, based on wage mechanisms, but mainly due to the limits on household indebtedness.[4] Moreover, public income transfer programs, very relevant to explain the improvement in distribution, reached an expressive level, indicating the impossibility of their substantial expansion in the prevailing fiscal framework. Induced investment, in turn, had its dynamism reduced by the leakage abroad of part of the demand for machinery and equipment and intermediate inputs.

Graph 1



Source: IBGE.

4 Based on the Keynesian/Kaleckian theoretical framework, it is possible to postulate that this cycle, for which the leading role of consumption was crucial, had in credit its main stimulus as a generator of autonomous effective demand. The improvement in income distribution played an important – but complementary – role due to its relevance in increasing the income multiplier.

Consumption played a more relevant role here than in other cycles, as it was the product of two simultaneous forces: the increase in household credit and the improvement in income distribution. Thus, explaining why it slows down implies considering how its determinants found their limits. To that end, it is essential to analyze the obstacles to further improvement in income distribution, both from the point of view of the labor market and of social policy, as well as the obstacles to the growth of household credit.

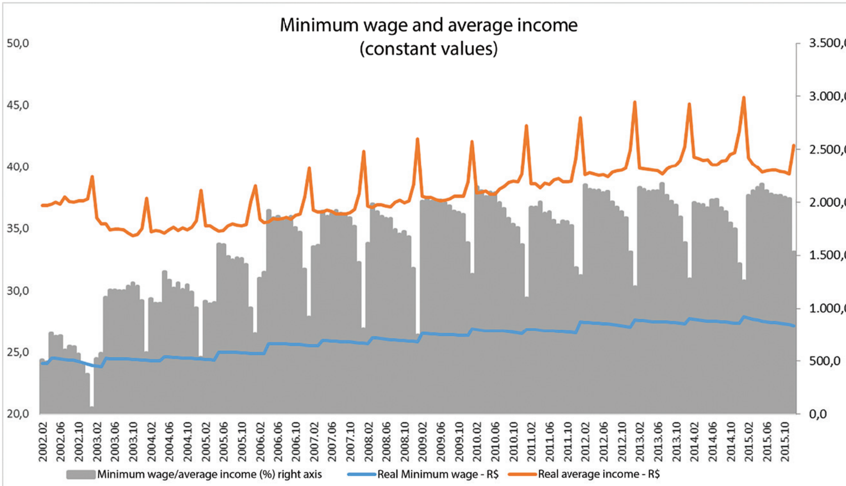
A first aspect to note is that the increase in wages, especially in sectors with lower purchasing power, heavily influenced by the minimum wage, as pointed out by Baltar, Souen and Campos (2017), was greatly helped by the appreciation of the real and the consequent downward pressure that it imposed on inflation. The costs, in terms of jobs – not in their quantity, but in their quality –, as a result of the non-development of more sophisticated links in the manufacturing industry, were expressive. This mechanism to enable faster growth in real wages, partly due to currency appreciation, could not be maintained, either because the downturn in the commodity price cycle, associated with the reversal of the liquidity cycle, would imply their devaluation, or because the reindustrialization endeavor would require a more competitive exchange rate, as in fact occurred during the Dilma administration after 2011.[5]

According to Baltar, Souen and Campos (2017), between 2003 and 2008, the structure of occupations did not change significantly, but wage dispersion decreased remarkably, characterizing an improvement in the distribution of wage earners' income, without significant structural transformation. This same pattern intensifies between 2008 and 2013, as the higher productivity sectors, such as the industry, have their weight in employment reduced while dispersion continues to fall, albeit at a slower pace.

The indications are, therefore, that the reduction in inequalities by shrinking the salary range ran into limits of the productive structure itself, that is, to reduce inequality in this manner, when the sectors that expand more rapidly are those with lower productivity, can lead to an escalation of the distributive conflict, especially in the face of the slowdown in the economy and productivity after 2010. In turn, even if growth had been preserved, the distributive impacts of the minimum wage would have been attenuated due to the high ratio between minimum wage and average wage then reached, which rose from around 25% in 2002 to 38% after 2010.

5 The exchange rate between the real and the dollar shows an appreciation of our currency, measured in real terms, of around 50%, when compared to the averages of 2002 and 2011. It is partially explained by the 35% gain in terms of trade in the same period and, in part, by arbitrage with interest rate differential.

Graph 2



Source: Brazilian Institute of Geography and Statistics, Monthly Employment Survey (IBGE/PME).

Social spending was undoubtedly an important factor in reducing inequalities. In fact, in advanced countries, enhancements in income distribution usually occurred more through the Welfare State, with increased progressiveness in taxation, than through changes in the labor market. In the case of Brazil, transfers, in the strict sense, and social spending, in the broad sense, played a crucial role in improving the distribution of labor income. As noted by Dweck and Teixeira (2017), despite the regressive tax burden, social spending more than compensates for this disadvantage and promotes improved distribution. This spending rose from 12.4% of GDP in 2003 to 15.3% of GDP in 2014 and is almost exclusively concentrated on cash transfers to households (welfare + social security).

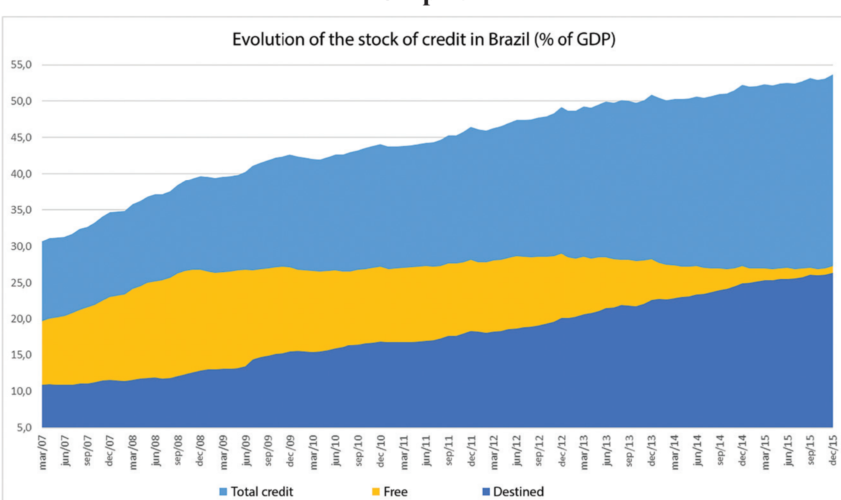
Thus, the crucial issue is the financing of increasing and progressive spending, by an increasing and regressive tax burden. According to Ribeiro, Luchiezi and Mendonça (2011), the taxation framework changed little in the 2000s. The incidence of the tax burden is higher the lower the income. In other words, as the rich pay proportionally less taxes, the financing of social spending comes disproportionately from the middle and popular classes. From this point of view, improving the distribution of income in this way has obvious limits, in addition to intensifying the distributive conflict, as the belief that distributive policies are carried out to their expenses developed in portions of the middle classes.

In the essential role played by consumption in the 2003–2010 growth cycle, credit was the predominant factor. That said, it is worth considering the limits of its expansion from the perspective of both demand (growth of available income, level of interest rates and household indebtedness) and supply (banks' exposure to risk). In the first case, the high level of interest rates very clearly has a dampening effect on the expansion, as, for relatively low levels of indebtedness, the portion of income allocated to pay for its service is proportionally high. According to data from the Central Bank, household indebtedness, as a percentage of income accumulated in twelve months, rises from 15% at the beginning of 2004 to 45% at the beginning of 2014, when it stabilizes. The most substantial increase occurs between early 2004 and early 2011, when it reaches 40%. In this same period, the portion of income allocated to debt service grew from 12.5% to 20%.

As for the supply of credit, it was necessary to rely on a decisive role of public banks to provide greater elasticity to the credit cycle, due to the downturn of the private system. Graph 3 shows that total credit decelerates after 2009, driven by the stabilization of free credit while earmarked credit plays an anticyclical role. At yearend 2010, the expansion of credit with free resources had already been substantially reduced, with a crucial role being played thereafter by earmarked credit and the public system. The downturn of the private banking system occurs for reasons related to risk assessment based on the already high household indebtedness. Thus, the public system is called upon to play a prominent countercyclical role.

Once restrictions were imposed on the improvement of income distribution – from the perspective of both the labor market and social spending – and credit expansion was limited, the cycle would inevitably lose dynamism. It is true that, in the Brazilian case, some peculiarities, such as the tax framework and the level of interest rates, added significant restrictive elements to a growth model whose greatest source of dynamism was consumption; nevertheless, as we will see, this model also ran into limits associated to investment.

Graph 3



Source: Bacen (time series).

The proposition relative to investment is a specification of the argument of demand leakage abroad, especially in the acceleration phase of the cycle. That is, given the productive structure of the Brazilian economy and its more specialized nature, the linking effects of this investment were reduced. Its difference relative to the leakage of consumption demand refers to its amplitude. The work of Fevereiro (2016) shows imported coefficients of household consumption around 10% and stable throughout the various phases of the cycle. In investment, this coefficient is doubled, around 20%, and rises in the acceleration phase.

As pointed out by Sarti and Hiratuka (2017), evidence of leakage is, in general, indisputable, such as the significant increase in imported content in the industry and in manufacturing. Data on the coefficient of penetration of exports show stability, around 15% between 2003 and 2009, and an explosion, thereafter, reaching 22% in 2015. However, the most important indicator to characterize the leakage is the coefficient of imported industrial inputs. This number has risen continuously since 2004, from a value close to 20%, that year, to 28% in 2015.

The general conditioning factors of the economic policy

Although the failure of the Dilma administration materialized from 2015, as a consequence, to a large extent, of the macroeconomic policy shifting toward orthodoxy, with its deleterious effects on employment and income and the growing contamination of the economy by the political crisis, the tragedy was foreshadowed in 2013. There are economic, social and political facts that already attest to the model's difficulties and its difficult survival.

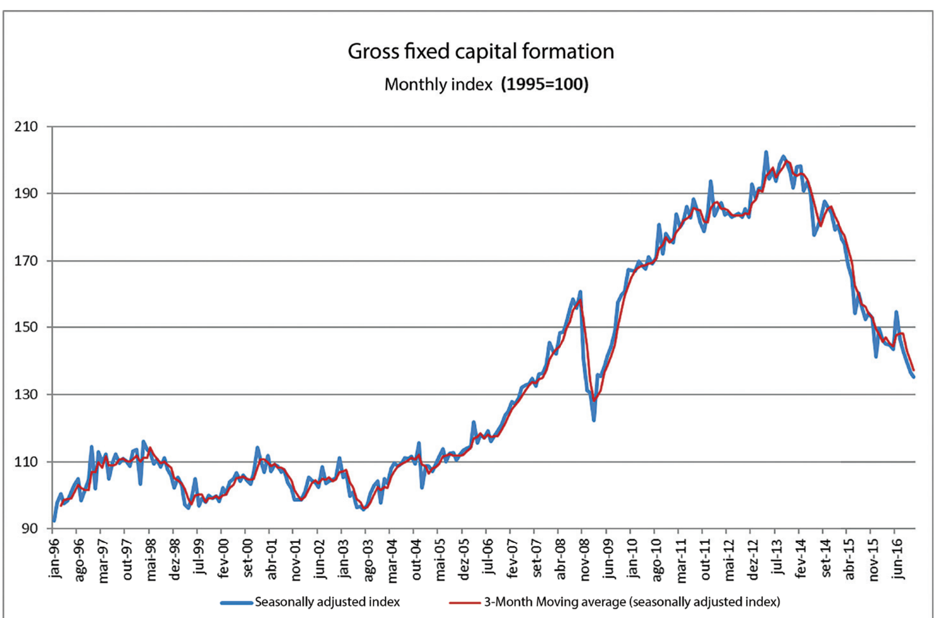
In economic terms, the most representative indicator of difficulties is the investment trajectory (Graph 4). In mid-2013, investment initiates a continuous decline for more than three years, which represents an almost unparalleled performance in the history of the Brazilian economy. This declining behavior of investment attests to the failure of the developmentalist experiment and the inability of the economic policies put in place since then to revert it.[6] The background for the model's failure was the structural and cyclical transformations, but it is necessary to recognize – as we will detail below – the unsatisfactory response of the economy to the set of economic policies implemented throughout the first Dilma administration.

6 It is noted that, contrary to what some authors postulate, such as Serrano and Suma (2015), the downfall of the model only occurs from mid-2013, and not in 2011, as they want. Despite the fiscal consolidation promoted in the first year of Dilma's administration having led to a slowdown in investment, it already recovers in late 2012.

In order to understand the deterioration of the broader context in which the economic policy operates, it is important to highlight, in the external sphere, the change in the context with the beginning of the reversal of the expansionist monetary policy in the USA (tapering), announced in June 2013, which, although later discontinued, caused serious disorders in the global currency, exchange and asset markets and deteriorated expectations. Domestically, it is also possible to observe the manifestation of a growing social and political dissatisfaction with the administration, whose landmark are the demonstrations in June 2013.

According to political analysts, such as Alonso (2016), the demonstrations involved, in their initial stage, quite different groups and agendas, which ranged from the demand for better public services to the fight against corruption, encompassing various segments of the middle classes. Over time, the conservative agenda gained preeminence, resulting in contesting the government and supporting its deposition. Beyond the movements' subjective political motivations, it is worth noting that they respond to a fundamental determinant, namely, the loss of growth dynamism, expressed in the reduction of social mobility.

Graph 4



Source: IBGE (Quarterly National Accounts, prepared by IPEA).

The data in Table 2, extracted from Quadros (2015), are noteworthy. They attest to the enormous social mobility that took place in Brazil between 2002 and 2012 and its decline from 2013 onwards. In the first period, 40 million Brazilians ascend from the lower strata and are absorbed mainly into the lower middle class. However, it is important to point out that both the middle and the upper middle class expand in absolute terms. This is no longer maintained in the fateful year of 2013. Downward mobility affects several groups, but mainly those with medium and high incomes, who are predominantly absorbed into the lower middle class. A variety of factors account for this movement, but for those at the bottom it was possible to mitigate it due to improved social policies. Those at the top increasingly begin to criticize these policies, the role of the State, in a clear movement of social polarization. The subsequently updated data of Quadros (2017) confirms the observations in the previous work: the year of 2012 can be considered as the peak of social mobility, and 2013 as the beginning of the decline.

Table 2

Evolution of the social stratification of the Brazilian population (1,000 people)

"Standards of living"	"2002"	"2012"	2002/2012	"2012"	"2013"	2012/2013
Upper Middle Class	13,183	17,719	4,536	17,719	17,097	-622
Intermediate Middle Class	20,653	31,182	10,529	31,182	28,857	-2,325
Lower Middle Class	54,941	85,893	30,952	85,893	89,043	3,150
Working Mass	53,769	50,101	-3,668	50,101	50,218	117
Poor	45,305	14,794	-30,511	14,794	16,253	1,459
Total	187,851	199,689	11,838	199,689	201,468	1,779

Source: PNAD - IBGE, apud Quadros (2015).

The developmentalist experiment's failure to ensure growth and the abandonment of the project by the alleged allies – industrialists and construction companies –, added to the mistrust on the part of the middle class and an extreme opposition on the other side, left few alternatives. The expansionist fiscal contraction chosen as an option turned the deceleration, already converted into stagnation in 2014, into an open recession. It is true that the objectives pursued in the previous period, such as reindustrialization and the investment program at Petrobras and to invest in infrastructure, could hardly be reaffirmed, both because of a moderate, but widespread, deterioration of economic indicators and also because of Operation Car Wash. The combination of the orthodox option, which led to recession, with the intensification of the political struggle led to the growing dominance of this sphere, causing one of the worst crises ever seen in the country.

The developmentalist experiment

The conclusion of the previous analysis is clear: although successful in achieving growth with social inclusion, the 2003–2010 cycle progressively lost dynamism. Reorienting the model was, therefore, essential. The elements present in this reorientation were significant, and several characteristics of a developmental growth model could be identified, such as: reconfiguration of macroeconomic relative prices (interest rates, exchange rates, energy prices and wage costs) to induce private investment, combined with high-impact sectorial instruments and incentives, such as investment by Petrobrás, which synthesized the industrial policy, the expansion of infrastructure and the support of public banks, in particular the BNDES. The general objectives were clear: reorienting growth by prioritizing industrial diversification and the expansion of infrastructure, with autonomous, private, and public investment as a key instrument.

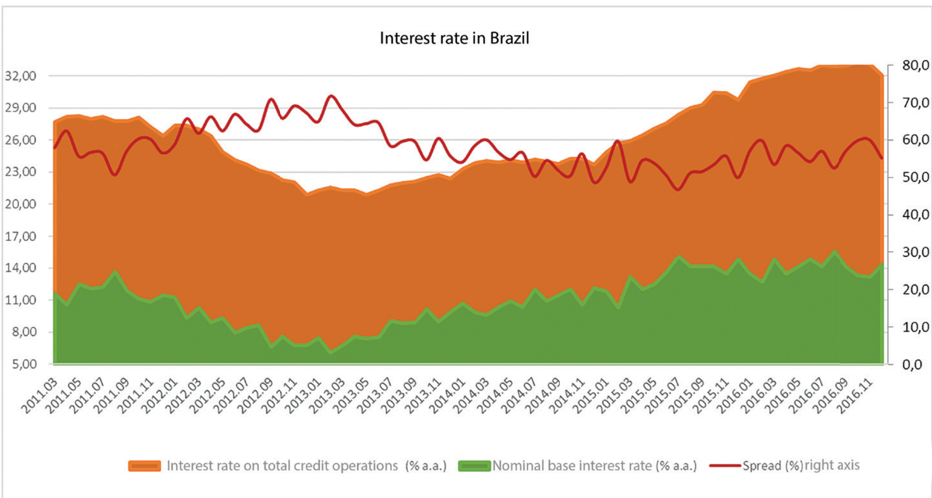
The change in relative prices

Data on the trajectory of interest rates are also unequivocal. From mid-2011 to Q1 2013, the economy's nominal interest rates, expressed in the Selic rate, fell and were the lowest since 1994 and even since 2002. According to Bacen (2017), despite the increases in the nominal rate that occurred from mid-2013, the real Selic remained well below the contemporary floor, only surpassing the level of 4% in Q1 2015, making a period of about four years with real rates at historic lows. Two succeeding factors explain the nominal increase in the Selic rate after almost two years of decline: the increase in country risk (EMBIbr), which occurs already in 2013, recurring until 2015, despite some pauses, and the subsequent increase in the inflation, which intensifies from 2014 onwards.

Interest rates on credit granted by the banking system dropped substantially. The attempt to reduce the banking system's margins, known as the spread battle, involved a variety of instruments – including the expansion of credit in the public system – to force the private system not to increase spreads considering the fall in basic interest rates. As observed in Graph 5, the success of the measures was only relative, showing the strength of the private banking oligopoly. Thus, during the Selic drop, spreads increased. They only decreased again after mid-2013 due to the replacement of credit from private banks with credit from public banks, which has been occurring in an absolute manner since then.

One of the most widespread criticisms of the interest rate policy adopted by Bacen during the Dilma administration originates in the orthodox sectors, which claim that rates were kept artificially low, without respecting the fundamentals. According to data calculated by the Center for Capital Market Studies (Cemec, 2017), it is observed that, throughout the period considered, the setting of the Selic target respected the limit given by the uncovered interest rate parity equation. Thus, the real interest rate in national currency was never below the dollar-equivalent real interest rate of Brazilian sovereign bonds. As might be expected, the first was always about two percentage points higher to compensate for the exchange rate volatility typical of inconvertible currencies.

Graph 5



Source: Bacen (time series).

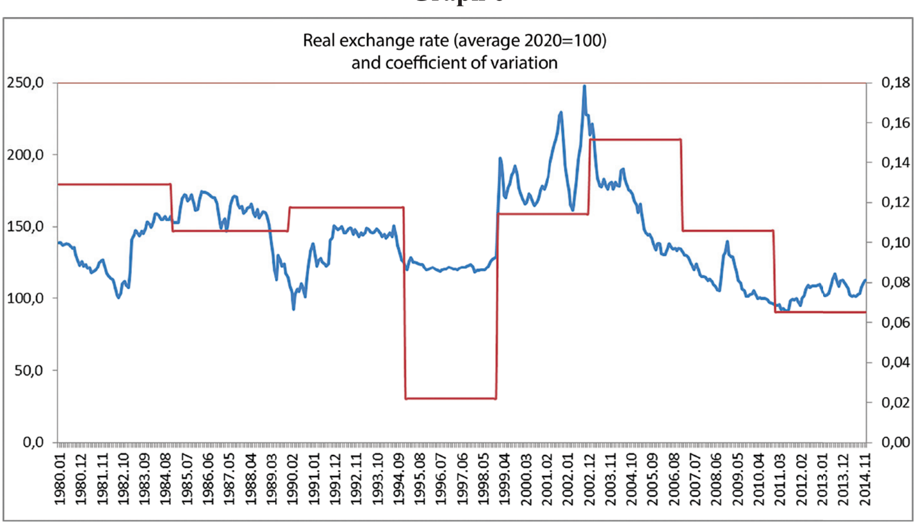
In evaluating the interest rate and financial policy of the Dilma administration, it is possible to discard more simplistic and extreme views that either deny its relevant character or claim that the fundamentals were disregarded. In fact, both the interest rate policy and the spread policy "poked the bears," going against the interests of various rentiers – from large investors to well-off middle-class members – and also of large private banks. On the other hand, it benefited large segments of households and small and medium-sized enterprises (SMEs) in the productive sectors, generating the necessary support to sustain them, at a time of economic and productivity slowdown.

Another crucial dimension of the economic policy implemented during President Dilma Rousseff's tenure was the administration of the exchange rate. We saw above that the growing financial openness of the Brazilian economy, associated with the worsening quality of external liabilities after the 2008 crisis, led to greater potential volatility in the exchange rate. The policy of regulating capital flows, analyzed by Carneiro and Rossi (2014), carried out in 2011 and 2012 and later relaxed, was successful in containing, and even reducing, this volatility, and it did so in a very significant way, even under strong criticism from the financial establishment and banks.

According to data in Graph 6, the exchange rate volatility during Dilma's administration was only not lower than that of the first FHC administration, during which the nominal exchange rate was, during almost the entire period, frozen. Furthermore, associated with the reduction in volatility, there was a reversal of the long period of currency appreciation observed during the two Lula administrations, with a moderate but significant depreciation of the real. The neo-developmentalist theses suggest that the devaluation was not enough nor lasted long enough to more forcefully redefine the vector of relative prices, encouraging export and the import substitution. However, an effective real devaluation of 20% on average is not insignificant and, therefore, there are other factors in explaining this performance.

Long periods of currency appreciation, such as those observed between 1991 and 1998 and between 2002 and 2010, produced a hysteresis in certain economic processes. In the Brazilian case, as shown by Sarti and Hiratuka (2017) and Diegues and Rossi (2017), the appreciation motivated a substantial increase in the imported coefficient in manufacturing, both of final goods and inputs. This process reached its paroxysm in the case of the machinery and equipment industry, which practically became an assembly industry. Therefore, the devaluation of the real leads – at least in the short term – to a deterioration in profitability, due to the increase in costs.

Graph 6



Source: Bacen (prepared by Ipea).

The interests that opposed the devaluation of the real during Dilma's tenure were varied and can be classified into general and specific. The first group comprises the productive sector, with a high import coefficient. Consumers, in general, also had reasons to oppose devaluation. In this case, in addition to the widespread opposition to rising inflation, we can identify groups, especially in the middle class, the largest consumer of imported goods and services – including international travel – whose interests were more opposed. Finally, banks and foreign investors, who lost, with the reduction in volatility, an important source of profits arising from speculative operations with the exchange rate in their various markets.

As for the policies to change relative prices, that for reducing the cost of electricity occupies an important place. This decrease materialized through Provisional Measure (MP) 579, later Law 12,783, whose objective was to reduce tariffs by 20.2% on average. This would be achieved through three measures: tax relief on part of the charges, including social charges; annual contributions from the Treasury to the Energy Development Account, including to offset part of the tax relief; anticipation of the extension of concessions in generation, transmission and distribution maturing, in exchange for the reduction of tariffs. The latter was, by far, the main measure.

The proposal to anticipate, by thirty years, the renewal of concessions maturing within five years was based on the observation that part of the assets involved in the production of hydroelectric energy, especially in large electric power generation companies, was partially or fully amortized. For this reason, the renegotiation, aiming to exclude the remuneration of the assets already amortized, would allow the tariff to be proportionally reduced, excluding the cost of capital from its calculation and considering only the operating and maintenance costs. For cases in which the assets were not fully amortized, indemnity of the remaining amount would be carried out.

Although the proposal of the Dilma government had legal support and the tariff reduction was a legitimate choice among the objectives of the granting authority, problems accumulated. The main one encompassed the conflict over the criteria for indemnification of non-depreciated investments. As there was no agreement on this point, the measure reached only about 50% of the initially planned generation capacity. This point is extremely relevant, as, from then on, two distinct groups of electric power generation companies were formed. Those that accepted the renegotiation – which were practically restricted to the Eletrobras group – had energy quotas established to be re-contracted, that is, sold in long-term contracts to distributors. The other electric power generation companies that did not join the negotiation progressively reduced their quotas to be negotiated through long-term contracts with the distributors.

The previous point is crucial: the unsuccess of the measures diverted the formation of electricity prices, to a large extent, to the short-term market. Without part of the contracted energy, distributors shifted their demand to the free market. The hydrological crisis, in turn, implied the activation of thermoelectric plants, with much higher marginal costs, increasing the sale price, the "price of settlement of differences". It is important to note that, despite the existence of several power generation companies with uncontracted energy, as they did not accept the terms of the measure – part of them owned by the public sector, that is, the state governments commanded by the PSDB, an opposition party –, they refused to participate in the auctions for contraction, adopting a short-term and speculative attitude.

Table 3

Brazil: Mean electricity tariffs by region (R$/MWh)*							
Years	2012	2013	2014	2015	2016	Δ% (2016/2015)	Δ% (2016/2012)
Brazil Mean	292.85	254.45	276.97	395.00	419.09	6.1	143.1
North	321.17	276.68	303.53	372.93	419.75	12.6	130.7
Northeast	297.09	250.52	269.05	340.00	367.64	8.1	123.7
Southeast	294.78	260.24	282.22	413.04	441.65	6.9	149.8
South	277.22	235.15	264.27	409.28	415.10	1.4	149.7
Central-West	290.41	257.74	273.63	398.07	419.38	5.4	144.4

Source: National Electric Energy Agency (ANEEL): Decision Support System (DSS) - * no taxes

The result of the set of factors mentioned above is that tariffs actually decreased in the first year of the measures' effectiveness, but later followed an explosive trajectory (see Table 3). The distributors either raised their prices according to these price increases or, when they did not, they were compensated by the government, which thusly increased the subsidy to the tariffs.

Another pillar of the economic policy, with its objective of changing relative prices, aiming a reduction in wage costs, was the fiscal waiver. Thus, the partial payroll tax relief mechanism was adopted from 2011 onwards. It was configured in a tax policy that exempted companies from paying the employer's contribution to the INSS related to their workers. According to the Ministry of Finance (2015), at the beginning, the idea was to increase the competitiveness by reducing the total wage cost of some industrial sectors and of the information technology sector. However, over time, the exemptions were extended to several sectors, including producers of non-tradeable goods.

Thus, the waiver gradually became widespread. Starting with 10,000 contributors in 2012, it reached 80,000 in 2014. Monthly values increased substantially from R$ 200 million in 2012 to an average of R$ 1.5 billion in 2014, reaching 0.5% of GDP that year.[7] This was the result of both the generalization and loss of criteria in its granting and of the fact that, at the aggregate level, tax neutrality was not achieved, that is, the replacement with another tax or increase in rates that would offset the exemptions granted.

The document from the Ministry of Finance (2015) summarizes the assessment of the results of the tax relief policy carried out by a tripartite commission, composed of government, employers, and workers. The conclusion points out the ineffectiveness of the policy, both for the results and for its costs. In summary, the tax relief policy served to reduce wage costs and increase the profitability of companies, but with small aggregate effects on the employment trajectory. Considering the maintenance of almost full employment during Dilma Rousseff's administration, the conclusion is debatable. The tax reliefs most likely had a compensatory effect by preventing falls in employment and, also, in investment.

The structural programs

In addition to the economic policy to encourage industrial diversification, based on the change in relative prices, the Dilma government had other important strategic objectives: reindustrialization, expansion of infrastructure and development of the oil and gas sector. The main financing instrument for these programs was the BNDES. Thus, for going beyond the macro policy, the economic policy had developmentalist characteristics, involved in a broader State action, although without the intensity of the experiences of the 1950–1980 period, mainly due to the lower weight of public investment.

The infrastructure and energy program, for example, were significant. For the 2012–2014 period, it provided investments of around 10% of GDP, distributed in: logistics (5.2% of GDP); electricity (3.2% of GDP); and oil and gas (1.6% of GDP). The option regarding infrastructure was implement the program through concessions, that is, through the private sector, partially abandoning the alternative of conventional public investment. The central

7 The work of Dweck and Teixeira (2017) found slightly higher numbers: 0.6% of GDP in 2014 and 0.7% of GDP in 2015.

argument was that the State did not have the operating conditions to carry out such program, although the private sector needed decisive support from the State to execute it, mainly through financing.

Despite efforts to increase investment and the supply of infrastructure services, the results were only reasonable when considering the four main segments: transport, energy, telecommunications, and water and sanitation. According to the Ministry of Finance (2015b), taking as a basis for comparison the immediately previous period, 2006–2010, investments in the area increase by only 0.5% of GDP. However, these aggregate results hide very different sectoral performances.

According to data presented by Frischtak and Davies (2014), the transport sector is the one that showed the best performance, evolving from an average share of 0.6% of GDP in the previous decade to 1.2% of GDP in 2014. Despite repeated criticisms of excessive governmental intervention in concession processes, including through the attempt to set the projects' internal rate of return (IRR), it was in this segment that private share made the most significant progress. In fact, data calculated by Galípolo (2016) show that there was a replacement of the public sector with the private sector in investments in the sector. The success of concession auctions in various segments – mainly in airports and, to a lesser extent, in highways – underlies this change.

In the energy segments, the level of investments remained relatively constant, at around 0.8% of GDP, as a result of the completion of a cycle of investments that primarily focused on expanding the generation capacity through large hydroelectric plants. As pointed out in several studies, this new capacity ensured not only universal access but also the growth of supply ahead of demand. The most important criticism of how the system expanded concerns the constraint imposed by environmental restrictions. Limiting the size of the reservoirs made the system more vulnerable to droughts, more dependent on thermoelectric complementation, and made prices more volatile. The so-called crisis of the electricity system, observed in the 2013–2015 period, was, in part, a reflection of this configuration, as discussed above.

In telecommunications, there was a drop in investments as a percentage of GDP, reflecting the stage reached by the sector. Once the universalization of fixed and mobile telephony was completed, the expansion front that remains today is the expansion of broadband Internet access. Regulatory deficiencies prevented the access program from reaching sufficient scale. Finally, in the water and sanitation segment, investments remained stable as a proportion of GDP, despite huge deficiencies. The crucial problem in this case concerns the constitutional responsibility of municipalities for providing services, resulting, in many cases, in a lack of planning and/or of the required scale of operation.

Public and private investment in infrastructure played an important role in preserving growth at a positive range, albeit insufficient to prevent a slowdown. Aside from the episodic decline in 2011, *lato sensu* public investment grew in line with GDP (see Graph 7). Given the *crowding-in* effect that the latter has on private investment and on long-term expectations, it seems evident that its trajectory did not contribute to making the new growth model viable. Here, a fundamental discussion is clearly suggested as to whether the contemporary Brazilian State has the instruments – public companies and planning and execution capacity in direct administration – necessary to command an increase in the economy's investment rate. This subject will be readdressed below.

Despite the effort, and some evident successes, the results of the infrastructure program of the Rousseff administration could have been more satisfactory. From the outset, the public administration could have made a more significant investment. Another reason for the moderate performance is in the sphere of government relations with the private sector. As shown in the work of the Ministry of Finance (2015b), the option for concessions succeeded in involving private investors in the sector, and the level of investment under their responsibility evolved from US$ 25 billion in 2010 to an average of US$ 50 billion between 2011 and 2014. Considering the importance given to these players, the relationship should have prioritized broader and more extensive negotiation processes. The excess of provisional measures and unilateral decisions worsened the investment environment.

The exploitation of pre-salt resources was the main motivation of the oil and gas program. It was conceived considering four aspects: the definition of the sharing regime to replace the royalty model, considered more adequate to the low risk of exploration; the minimum 30% participation of Petrobras in all fields to be explored, to control the extraction pace and allow the execution of the local content policy; the constitution of the sovereign fund to prevent the appreciation of the real and manage resources in hard currency; the allocation of the results obtained in the sovereign fund to the social area.

According to Azevedo (2017), the production of oil in the pre-salt layer generated important technological challenges, such as the production of specialized and sophisticated equipment, such as rigs, vessels, floating production systems and submersion systems. Given the scale of production to be faced and the underdeveloped character of this industry in Brazil, the challenge was huge. In other words, adapting the timing of exploration to the capacity of the nascent equipment industry in Brazil was a huge obstacle. In fact, as the government had also decided to expand the country's refining capacity, the challenge was twofold: high and simultaneous investments both in exploration and in production and refining. This dual investment front significantly pressured the capacity of the heavy construction industry in Brazil, delaying projects and making them more expensive in the short term.

The indicators relating to the productive-technological aspects of Petrobras are quite positive, as can be observed in Table 4 below. Investments in exploration and production nearly quadrupled between 2006 and 2013, when they reached their historical peak. Proven oil and gas reserves grew about 20% between 2006 and 2014, when they started to decline due to the reduction in investments. In the same period, production grew 15% and continued to increase in 2015 and 2016. The highlight in this case is for offshore production. In the Campos basin, it expanded by 19% and, in new areas, it almost increased tenfold.

The most important aspect of this performance, however, is that related to extraction costs, showing a significant increase in productivity. It grows in the early years of deep-water and pre-salt exploration, but starts to see a notable decline after 2014, to an average of US$ 10.20 per barrel. Furthermore, these costs are even lower in the case of the pre-salt layer, where they reach a value below US$ 8.00. According to the World Energy Investment Outlook (2014), the operating costs of oil production in the various productive areas in the world ranged from US$ 7.00 to US$ 35.00, showing that exploration in the pre-salt layer is close to the cost of the most productive areas in the Middle East.

The fall in the cost of production indicates substantial technological progress in deep-water oil exploration, led by Petrobras. In light of these data, criticisms regarding the local content policy, which are based on evidence that the pieces of equipment were produced at more expensive prices than similar ones abroad, lose consistency. The controversy over higher prices is old, but its critics make a static argument. The information compiled by Foster et al. (2013) shows an expressive convergence between the prices of local and international equipment, attesting to the international experience with the nascent industry.

Table 4

	Petrobras: Production Area Indicators										
	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006
National Historical Proved Reserves											
Oil (millions of bbl)	10,336.4	10,670.4	13,636.3	13,458.2	13,219.3	13,154.2	12,841.3	11,985.7	11,899.6	11,722.5	11,591.5
Natural Gas (Millions of boe)	1,925.0	2,186.5	2,496.5	2,461.2	2,445.2	2,487.8	2,373.6	2,112.5	2,123.6	2,117.9	2,082.2
Extraction Cost (US$/ Barrel) - Brazil	10.2	10.6	14.2	14.3	13.8	12.5	10.3	9.5	8.2	8.6	7.2
Nominal E&P Investment (US$ MM)	n.a.	19,131.0	25,500.0	27,566.0	21,959.0	20,405.0	18,600.0	15,928.0	14,279.0	10,684.0	7,041.0
Oil and LNG production (Mbpd)											
Total	2,144.3	2,128.3	2,034.4	1,931.4	1,980.1	2,021.7	2,003.9	1,970.8	1,854.7	1,792.1	1,777.7
Offshore	1,969.0	1,939.6	1,836.9	1,727.6	1,768.4	1,808.5	1,790.2	1,754.8	1,633.3	1,563.1	1,545.7
Campos Basin	1,358.5	1,487.9	1,525.8	1,531.0	1,618.3	1,677.0	1,676.8	1,693.6	1,546.8	1,475.3	1,468.3
Others	610.5	451.7	311.2	196.5	150.0	131.6	113.4	61.3	86.5	87.7	77.4
Land	175.3	188.6	197.4	203.8	211.7	213.2	213.8	216.0	221.3	229.0	232.0

Source: Petrobras, http://www.investidorpetrobras.com.br/pt

With regard to the company's financial performance, Petrobras' profitability, in addition to factors associated with its operating efficiency, depends on two fundamental determinants: the exchange rate between the real and the dollar and the international price of oil. As a general rule, domestic prices of oil derivatives have to follow these two parameters, varying inversely with the real-dollar exchange rate and directly with the international price. As the sale of oil derivatives in the domestic market is Petrobras' main source of revenue, its pricing policy is the main determinant of its profitability and depends on the amount of prices subsidies to domestic consumption.

During Dilma Rousseff's tenure, a policy to control the prices of oil derivatives for the domestic market was adopted. Predictably, this had a major impact on the company's financial situation. The effect was enhanced because, since 2006, domestic consumption had grown at high rates. Furthermore, as domestic production was insufficient due to the low installed refining capacity, it was necessary to resort to growing imports, exacerbating the problem. The combination of lost revenue and major investment effort significantly deteriorated the company's financial situation, reducing, on the one hand, its cash flow in absolute terms from 2011 onwards and, on the other hand, increasing indebtedness, which increases from US$ 32 billion in 2010 to US$ 132 billion in 2014. The great improvement in the capital structure – debt/equity ratio – that had been obtained, such as the giant IPO of 2010, a necessary condition for the great expansion program, progressively deteriorated.

Since the end of 2014, a series of facts, such as allegations of corruption, reduction of international prices, and delays and cancellation of investment projects, created a very negative environment at Petrobras, which was compounded by a set of wrong decisions. These latter were expanded during the Temer administration and consisted in abandoning a long-term vision and adopting a business strategy similar to that of private companies. Measures such as rapid reduction of leverage, sale of assets, focus on the core business – i.e. exploration and production –, loss of exclusivity of participation in the exploration of areas and mitigation of the national content policy progressively turned Petrobras into a conventional company, focused on obtaining short-term results, to meet the primacy of shareholders.

The financing of the programs, for Industrial diversification, infrastructure and part of that relating to oil and gas, was the responsibility of the public banking system and in particular of the BNDES. The public system also played other roles, such as inducing reduced spreads in short-term lines, but it was in long-term financing that its action was characteristic, resuming a tradition in the country at times of great transformation of the productive structure. The fact that the BNDES came to directly control, through its financing, about ¼ of the Gross Fixed Capital Formation (GFCF), having received funds from the Treasury in the order of R$ 525 billion, between 2009 and 2013, approximately 10% of GDP, which came to represent 57% of the bank's funding in 2014, made them the main financier of the process.

The available data[8] show that despite the great negative publicity around the BNDES' huge operation in the Dilma administration, there is a discontinuity in its trajectory. The level of financing remains constant as a percentage of GDP, around 3.4% on average, in the 2007–2010 and 2011–2014 periods, but with a downward trajectory from 2010 onwards. Another important aspect, which also denies the conventional thesis of picking the winners, as stated by De Bolle (2015), is the deconcentration of funding, visible in several indicators:

a. The more than proportional increase in indirect operations, smaller and based on transfers through retail banking institutions, whose share grew from 27% of total disbursements in 2009 – the year that the BNDES PSI was initiated – to 44% in 2014. The highlight in this case were the operations of the Agency for Industrial Financing (Finame) in the scope of the Investment Support Program (ISP – or BNDES PSI in Portuguese).
b. Disbursement to micro, small and medium-sized enterprises (MSMEs) grew from R$ 35.6 billion (2015 prices) to an annual average of R$ 70 billion in 2013/2014, doubling its value in real terms.
c. The number of companies supported by the BNDES increased from 108,000 in 2009 (4% of the total) to 277,300 in 2014 (9% of the total).
d. Between 2009 and 2014, the percentage of companies, by size, supported by the BNDES evolved as follows: large companies, from 22.4% to 28.8% of the total; medium companies, from 16.7% to 26.0% of the total; small companies, from 9% to 17.5% of the total; micro companies, from 2.7% to 6.3% of the total.

Given these indicators, the concern with the BNDES' operation should be related not to the concentration of resources, but to their dispersion. Strictly speaking, the latter shows the persistence of countercyclical programs inherited from the previous administration, the main one being the Investment Support Program (BNDES PSI), with heavily subsidized interest rates. Thus, if on the one hand it is undeniable that the BNDES' operation in the 2009–2014 period influenced the sustainability of the investment rate and the expansion

8 The data used in this characterization of the BNDES' operation were extracted from: BNDES (2016), BNDES (2017) and http://www.bndes.gov.br/wps/portal/site/home/conhecimento/pesquisaedados/

of capacity in a wide range of sectors, the dispersion of its resources, on the other hand, translates the difficulties of this expansion in those sectors that were the axes of the developmentalist program.

Despite this relative dispersion, the BNDES' operation was of great relevance in some strategic segments. Although there is also deconcentration of resources in the various sectors of activity financed, some priority segments maintain an expressive share in disbursements. Thus, for example, infrastructure and industry remain practically constant in real terms, despite still leading in absolute terms.

a. In infrastructure, it is worth highlighting the crucial role of BNDES financing for its expansion, with decisive participation in all sectors, such as electricity (64% in generation and 56% in distribution), logistics (airports, 82%; ports, 71%, highways, 91%); sanitation (sewage treatment, 58%). The negative aspect is the more than proportional growth of auxiliary transport activities (storage and delivery activity).
b. In industry, the commodities segment, especially pulp and paper and extractive industries, led disbursements, and the automotive sector continued to be important in absolute terms. Strictly, there was no change in the pattern of financing to the sector during Dilma Rousseff's tenure.
c. In operating areas, the highlights were the increased participation of urban and social infrastructure, low-income agriculture and the Amazon fund, the latter with very little absolute weight.

This relative loss of focus by the BNDES resulted from external factors, such as the slowness of the Logistics Investment Program (PIL), or the intensification of international competition with the domestic industry, both implying a reduction in the demand for financing. It is uncertain whether the BNDES would have the autonomy, in isolation, to advance the two strategic axes. Perhaps for this reason, its performance partially lost its strategic sense.

Considering this great endeavor toward structural transformation contained in the economic policies of the Dilma administration, the question "Why didn't it work?" is decisive. There are elements of conception and management of the policies themselves that appear as negative factors, even before the orthodox macroeconomic policy implemented in 2015, such as: the inconstancy of this policy, analyzed by Mello and Rossi (2017), the loss of selectivity by the BNDES, the damming of Petrobras' prices, the slowness of the logistics program, the excessive tax reliefs, in a broader context of low capacity to negotiate with the various economic agents. However, in order to understand the failure of the developmentalist experiment, the economic policy mistakes should be considered in conjunction with deeper changes that had been underway in the global economy, which accelerated after the 2008 crisis, as well as the moment of deceleration in the domestic cycle.

Critics of the Rousseff administration's economic policy, such as Serrano and Suma (2015), deny its developmentalist character. They defend the thesis that incentives to private investment were made to the detriment of public investment, that is, the government's central proposal would have been the replacement of public investment with private investment as a dynamic element of growth. The major problem with this postulation is that it works with the idea that the State had the size and the necessary instruments to command investment, without synergy and complementarity with private investment.

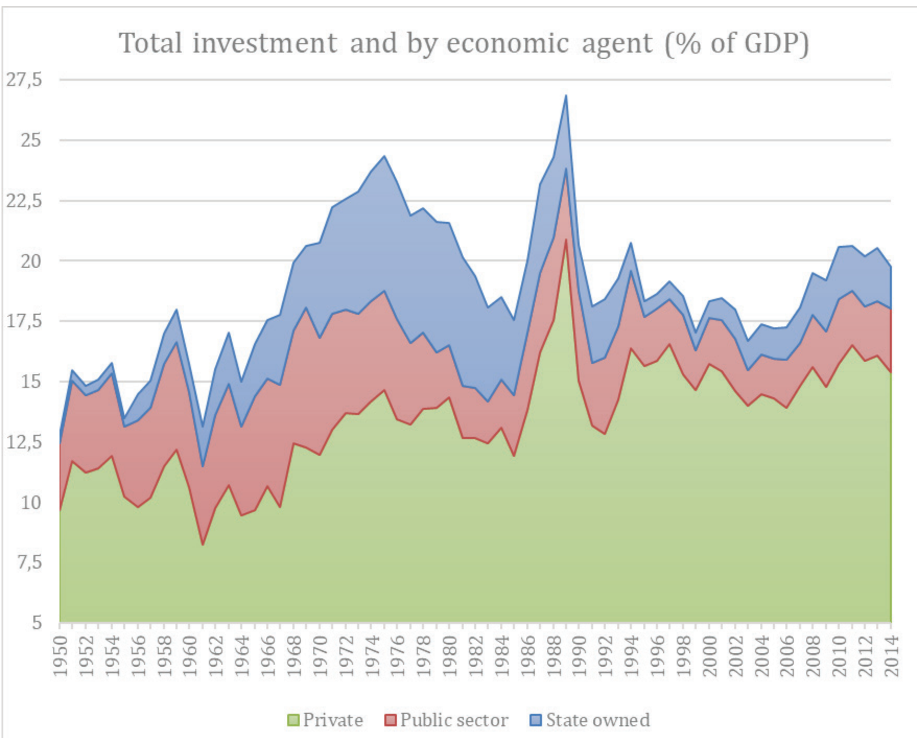
Graph 7 data show the various stages and combinations of public and private investment throughout contemporary Brazilian history. It was in the 1960s and especially in the 1970s that public investment reached its peak, through state-owned companies. There is the constitution and expansion of the large holdings of the state productive sector (SPE) – Petrobras, Eletrobras, Siderbrás, CVRD, the port sector, the railway sector, Itaipu Binational –, which raise the investment rate and GDP growth to unusual levels. In those years, the public sector, *lato sensu*, came to be responsible for 40% of the total investment, and the SPE, for amounts between 20% and 25%.

The late 1970s saw the last major endeavor to diversify the Brazilian industrial matrix with the 2nd National Development Plan (PND). Since then, both in the lost decade and in the years of liberal reforms, the 1990s, the deceleration is very significant, and the investment and growth rates are very low. It is worth noting here the significant privatization process behind the sharp decline in the SPE investment in the 1990s. Thus, the Brazilian economy lost an important instrument for planning, coordinating and inducing private investment.

The above conjuncture only changes in the Lula and Dilma administrations. Not only the total investment rate progressively increased, but also the public investment rate. However, it should be noted that this advance is limited by its starting point, since in the liberal period, between 1994 and 2002, the public investment rate had fallen, on average, to only 15% of the total investment, approximately 3% of GDP. During the eight years of the Lula administrations, there was a recovery of investment in relation to both public administration and state-owned companies: its average grows to 4% of GDP between 2007 and 2010 and, at the end of that period, it reaches almost 5% of GDP. Notwithstanding their relevance, these figures are not comparable, by far, with the values observed in the developmentalist decades. Furthermore, there is an essential qualitative difference in their composition: the weight of state-owned companies is much smaller: 25% of the total in the 1975–1979 period against 10% between 2007 and 2010.

Thus, we arrived at the Rousseff administration, and consequently at the developmentalist experiment of those years, with public investment not very functional to leverage private investment. In addition to the reasonably low level, which takes power from the effect of aggregate demand, what is essential is the still low absolute and relative value of investment of state-owned companies, concentrated in just two groups: Petrobras and Eletrobras, of which only the former had quantitative relevance.

Graph 7



Sources: Reichstul and Coutinho (1983); Pinheiro and Oliveira Filho (1991); Rodrigues (1990); Giambiagi and Pinheiro (1997); Afonso and Fajardo (2015). Prepared by the authors.

It is important to note some characteristics of the investment during the first Dilma administration (Graph 7). Despite the fall in 2014, the total investment rate continued rising *vis-à-vis* the second Lula tenure, increasing from an average of 19.3% of GDP to 20.3% of GDP. The set of public investment increased slightly compared to the previous period, from 4.1% of GDP to 4.3%

of GDP, proportionally divided between state-owned companies and the public administration. Its crowding-in effect on private investment is significant, as most of the increase in the aggregate rate results from the latter. In any case, as the work of Dweck and Teixeira (2017) shows, investment under the responsibility of the public administration only maintained its stability due to programs such as Minha Casa Minha Vida, relevant to sustaining aggregate demand, but little effective for the reorientation of the productive structure.

In light of the economic policies implemented in the 2011–2014 period, it is worth examining the orthodox argument that the growing slowdown in investment would have been motivated by a fall in corporate profitability, whose ultimate explanation would be the increase in wage costs, inconsistent with the increase in productivity. In this sense, its effect would have been to crush companies' profit margins. The argument is formulated, with some nuances, in publications by Cemec (2015) and by the Institute of Studies for Industrial Development (Iedi, 2016).

The argument of Cemec (2015) is that margins were reduced due to faster wage growth, *vis-à-vis* productivity, after 2009. Leaving aside the discussion on the deeper reasons that support this trajectory, it is worth asking whether the wage cost is the only determinant of the profit margin. Or, to put it another way, if its growth above productivity could not have been offset by the more favorable behavior of other elements of costs, operating and non-operating. As shown above, the economic policy of the Dilma government had as one of its axes the change in relative prices with the exact aim of increasing the profitability of companies: reduction in energy costs, in interest rates, tax relief and, additionally, devaluation of the real. The work of Iedi (2016) provides some clues as to what actually occurred, emphasizing the expansion of financial burdens on companies. However, there are additional factors, as can be observed in the data in Table 5 below.

The data show that the gross profit margin changed moderately between 2010 and 2011, remaining stable thereafter. Costs also varied in the same direction and intensity, refuting the thesis that operating costs, and in this case wage costs, were responsible for squeezing the companies' profit margins. On the other hand, if we consider the operating margin, which includes income from financial operations, it can be observed that it substantially declines, falling by half between 2010 and 2013 due to the reduction in interest rates in the economy. In other words, the large, financialized companies lost profit margins due to the drop in interest rates. The net margin, which includes financial expenses, falls even faster, indicating that companies increasingly became net debtors, as shown by the increase in leverage and net financial expenses, especially after 2013. Finally, it is noted that this conjuncture is aggravated by the deceleration that appeared as background from 2010 onwards, also depressing the rate of return on assets.

Table 5

	Industry Indicators* (in %)					
	2010	2011	2012	2013	2014	2015
Gross profit margin	25.8	22.1	20.7	22.6	22.7	22.8
Production Costs/Operating Revenue	74.2	77.9	79.3	77.4	77.3	77.2
Operating margin	13.3	11.6	7.4	6.7	9.7	7.6
Net Profit Margin	8.3	6.3	2.5	0.0	5.1	0.5
Net debt/equity	58.6	58.4	63.3	65.8	70.3	87.2
Net financial expense/operating revenue	2.7	3.7	3.9	4.7	4.6	5.9
Return on assets	5.4	4.0	1.6	0.0	3.5	0.3
Return on assets **	7.2	6.4	2.5	1.2	0.5	-3.4
Source: IEDI (2016) * without Petrobras and Vale, ** with Petrobras and Vale						

The work of Iedi (2016) and that of Cemec (2017) also found the negative effect on profitability caused by the devaluation of the real observed during the period, but mainly in 2015. The numbers show its impact on the cost of debt, indicating that not only exporting companies were in debt in dollars, but also non-exporting companies, which resorted to financing in dollars after mid-2013, given the rise in domestic interest rates.

The central proposition of this chapter is that the failure of the developmentalist experiment was already evident in 2014; therefore, before the orthodox macroeconomic policy implemented in 2015 – which was certainly a bad choice to tackle this unsuccess. To understand the inability to transform the industrial structure and the desertion of industrialists as a base of support, it is necessary to emphasize not only the inadequacies of the economic policy, but also the financialization and asymmetric internationalization of the companies through the increased share of imported content. Last but not least, it was relevant the intense and growing Chinese competition in manufacturing markets, both domestically and in traditional ones, such as South America, as shown in the text of Bastos and Hiratuka (2017).

The crisis: anatomy of the disaster

The choice of economic policy made in 2015, of an orthodox macroeconomic adjustment whose main objective was to gain market trust, was certainly a mistake, but it needs to be qualified and analyzed. The starting point is to point out that the available options were limited, despite the worst one having been chosen. That is, the failure of the developmentalist experiment was already evident, and the possibility of reaffirming it, non-existent. That is because the failure itself generated costs that appear in a progressive deterioration of the public and private sectors – households and companies – and of the external sector. The orthodox macroeconomic policy and the political crisis worsening that followed have an indisputable weight in transforming a problem of flows into an imbalance of stocks.

The central proposal of the new economic policy was to recover the trust of the local and international markets, which was expressed in the main objective of maintaining the risk classification, of investment grade, of rating agencies. Thus, there were, on the one hand, measures to cut spending, which aimed to increase and consolidate the fiscal primary balance, and, on the other hand, the recovery of public tariffs and prices, especially for energy and fuel, reducing the burden on public accounts and resuming the role of the market in their determination. Part of this logic was to abdicate from intervening in the foreign exchange market through swaps, based on the diagnosis that the real had been kept artificially appreciated during 2014. The increase in the basic interest rate, in order to fight inflation, closed the circuit. Thus, the 2015–2016 biennium is essentially characterized by simultaneous shocks promoted by the macroeconomic policy, leading to the deterioration of balances or a recession originating in the latter.

There is only one partial exception for the period: the external sector. Despite the international liquidity cycle declining but still favorable after 2010, the solid position of the public sector as a net creditor – due to the volume of reserves, of around US$ 375 billion – and the mechanism for correcting the deterioration of the current account by the recession prevented the change in the nature of the crisis, avoiding it from turning into a problem of stocks. According to data from Bacen (Table 6), the flow imbalance, expressed in a current account deficit of around 4.5% of GDP, at the beginning of 2015, was progressively corrected by the recession, reaching, at the end of 2016, the mark of 1% of GDP. It should be noted that between 2010 and the end of 2014 the deficit rises from 1.5% of GDP to 4.5% of GDP, in a context of deceleration in domestic growth. In other words, the imbalance was undeniable and needed to be corrected not by quantities, as was done, but by relative prices (see Table 6).

Based on these data, it is necessary to qualify the observation that, in the scope of the external sector, the crisis was not aggravated, remaining in the sphere of flows. This occurred, on the one hand, because current account imbalances were mitigated by two years of recession. On the other hand, because the imbalances did not reach the financial account due to the resumption of the international liquidity cycle.

Table 6

Brazil: Economic indicators						
	2011	2012	2013	2014	2015	2016
External Sector and Exchange Rate						
BRL / USD Nominal – end of period	1.87	2.05	2.36	2.66	3.96	3.26
BRL / USD – year average	1.68	1.95	2.16	2.35	3.33	3.49
Trade Balance – USD Billion	30	19	2	(4)	20	48
Exports – USD Billion	256	243	242	225	191	185
Imports – USD Billion	226	223	240	229	171	138
Current Account – % GDP	-2.9%	-3.0%	-3.0%	-4.2%	-3.3%	-1.3%
International reserves – USD Billion	352	379	376	374	369	372
Economic activity						
real GDP growth	4.0%	1.9%	3.0%	0.5%	-3.8%	-3.6%
National unemployment rate – annual average (*)	-	7.4	7.1	6.8	8.5	11.5
National unemployment rate – yearend (*)	-	7.4	6.8	7.1	9.6	12.6
Inflation						
Consumer prices (IPCA)	6.5%	5.8%	5.9%	6.4%	10.7%	6.3%
Interest rate						
Selic – end of period	11.0%	7.3%	10.0%	11.8%	14.3%	13.8%
Selic – year average	11.7%	8.5%	8.4%	11.0%	13.6%	14.2%
Real interest rate (SELIC/ IPCA) – end of period	4.9%	2.5%	2.4%	4.3%	2.6%	7.4%
Public finances						
Primary surplus – % of GDP	2.9%	2.2%	1.7%	-0.6%	-1.9%	-2.5%
Nominal Surplus – % of GDP	-2.5%	-2.3%	-3.0%	-6.0%	-10.2%	-9.0%
Net Debt – % of GDP	34.5%	32.3%	30.6%	33.1%	36.0%	46.2%
Gross Debt – % of GDP	51.3%	53.7%	51.5%	56.3%	65.5%	69.9%

Source: Itaú (https://www.itau.com.br/itaubba-pt/analises-economicas/projecoes/cenario-brasil-setembro-2017).

In the private sector, particularly in the industry, a large number of companies experienced, in 2016, a Ponzi situation. A survey by Fiesp (2016)[9] concluded that more than half of them (55%) in 2016 did not generate enough cash to service the debt. As this is a sample of large companies, most likely SMEs should be in an even more drastic situation. Between 2011 and 2104, companies have their cash flow growth reduced and their debt increased, but

9 Working with a sample of 269 companies, 114 publicly traded companies, excluding Petrobras, and 155 privately held companies, the survey covers 42% of the turnover of the manufacturing industry, concentrated in large companies.

still at a moderate rate. The net debt/EBITDA ratio,[10] after rising from 1.95 in 2010 to 2.63 in 2011, dropped to the level of 2.20 in 2014. Thus, after the initial shock, in 2011, the year in which there is an absolute reduction in EBITDA, the latter maintains a growth above that of debt, reversing the initial deterioration. Between 2011 and 2014, the main worsening factor is the cash flow, as, with regard to debt, while the devaluation of the real pushes these latter up, the reduction in the Selic and spreads restrains its growth.

The situation changes from 2015 onwards, when another sharp shift in the net debt/EBITDA ratio is observed. On the current side, recession, currency devaluation, and generalized increase in public tariffs deteriorate the cash flow, causing it to fall for two consecutive years. However, despite its intensity, this is not the main effect; the interest rate shock and currency depreciation push the cost of debt to very high levels. In one year, in 2015, the debt/EBTIDA ratio rises from 2.14 to 2.81, increasing again to 3.25 in 2106. Another indicator, the EBITDA/financial expense ratio, clearly shows the beginning of the Ponzi situation: between 2010 and 2014 it drops from 2.19 to 1.53, but in 2015 it was below one (0.78).

The situation of households, according to data from the Consumer Indebtedness and Default Survey (Peic, 2017), also deteriorates after 2015. Their percentage with some type of debt fluctuates around 60% between 2011 and 2014, but increases sharply in 2015 to 67%, only to fall shortly thereafter due to two extreme events: payment, by those who manage to do so, generally higher-income households, and default of the poorer households. In the first period, *lato sensu* delinquency declines, reducing both the number of households with overdue accounts and those in default. This situation changes radically after 2015, with the interest rate shock and the increase in spreads. Delinquency increases substantially both in terms of arrears, up from 18% to 25% of all indebted households, and in terms of default, which increases from 5% to 10% of the total.

Other indicators attest to the extremely difficult situation of households. The debts that expanded the most were those of the worst quality, shorter term and more expensive, especially credit cards. In early 2011, about 70% of indebted households had credit card debt. This number rises slightly to 73% by the end of 2014 and rises sharply to 79% by March 2016. Other forms of cheaper or longer-term debt, such as payroll-deductible loans and real estate credit, expanded in the period, but reached a low percentage of indebted families: 5% and 8% respectively.

10 EBITDA is the acronym for the expression "*Earnings before Interest, Taxes, Depreciation and Amortization.*" (N.E.)

The situation of the public sector is like that of the private sector and has a similar evolution. Between 2011 and 2014, the primary balance disappears; from a surplus of 2.5% of GDP in 2011 to a small deficit of 0.6% in 2014 (Table 6), expanding since then. If the indicator is considered according to the twelve-month criterion, the deterioration is more significant, since at the peak, in July 2011, the primary balance was 3.5% of GDP. In other words, the degradation was evident and, in a certain way, paradoxical, since the reduction in the balance should have stimulated the economy. In fact, this pattern persists in 2015 and 2016, when rising primary deficits are observed and recession increases.

The economic explanation for the fact that the primary deficit does not stimulate the economy lies in two factors. The first is more general and concerns its insufficiency to offset the deceleration and subsequent contraction of private demand after 2011, especially after 2015. In the 2011–2014 period, the very cyclical character of the Brazilian fiscal system makes the deficit appear automatically; the deceleration of revenues is faster than that of the GDP, the same not happening with the expenses, part of which is indexed by the GDP. Associated with this is the lower income multiplier implicit in the composition of expenditures, due to the low dynamism of public investment and the expansion of tax breaks. All these characteristics are maintained or intensify after 2015.

Despite the declining primary surpluses, between 2011 and 2014, public debt declined for most of the period. Net debt drops eight percentage points of GDP between January 2011 and January 2014, growing by just two percentage points this latter year. Gross debt, even absorbing the full impact of the stimulus policy through public banks and the additional purchase of reserves, remains strictly constant in the same period and, like net debt, grows by just two percentage points in 2014. The crucial factor for the fall of both is the reduction of the interest burden, between mid-2011 and 2014, to the lowest level in Brazil's contemporary history (Table 6).

The situation is completely different in 2015 and 2016, a biennium in which gross debt increases by twenty percentage points of GDP, and net debt by twelve. Despite the primary deficit growing to the level of 2%, it is much less relevant in explaining the increase in debt – the nominal deficit reaches the level of 10% of GDP in 2015 and 2016 – driven mainly by the interest burden and, to a lesser extent, by the cost of foreign exchange swaps. These latter weighed significantly in 2015, representing about 1/4 of the nominal deficit, due to the devaluation of the real and the accumulation of positions in 2014, aiming to prevent it. Its final effect on debt is ambiguous, not only because the devaluation reverts in 2016, but also because it increases the equivalent value in reais of part of public assets, the international reserves. In summary, under the impact of stock imbalances, debts return to a level – 55% for net debt and 73% for gross debt – which is similar to that of the end of the FHC administration.

Conclusions

The thesis, stated at the beginning of this chapter, was that the failure of the developmentalist experiment implemented during the Dilma Rousseff administration could only be understood by considering the interaction of factors of three orders: structural, cyclical and economic policy. In other words, the successes and mistakes of the economic policy would have to take into account the background, or the conditioning factors imposed by the Brazilian participation in the globalized economy and by the cyclical slowdown.

Regarding the structural plan, given the high financial openness of the Brazilian economy, it is worth emphasizing the relevance of the global liquidity cycle as a conditioning factor for the domestic cycle, through asset prices and credit expansion, in foreign currency and even in local currency. This influence was exacerbated and more unstable due to the policies to combat the crisis in the central countries. In the productive dimension, besides the commodity prices cycle, the formation of global value chains and Brazil's asymmetric participation reduced the role of investment in the acceleration phases of the cycle. This was also intensified by the emergence of widespread idle capacity in Asia, particularly in China, and the resulting investment decision, deteriorating profitability expectations.

In the context of the domestic cycle, the main aspect was the exhaustion of the dynamism arising from the expansion of consumption. Whether it was because of the limits to improving income distribution arising from the instruments used – increase in the minimum wage and public transfers, without significant tax changes – or, mainly, because of the impossibility of expanding credit at the previous pace, it was necessary to change the growth model, if not completely, at least in a manner that added new sources of dynamism. The pursuit of diversification of the industrial matrix and expansion of infrastructure, as well as the exploration of the pre-salt layer, constituted the chosen priorities.

Given the constraints mentioned above, the challenges faced by the economic policy were immense. These challenges immediately demanded a new social coalition capable of supporting the project. There is enough evidence to conclude that a developmentalist proposal based, on the one hand, on the strengthening and diversification of productive sectors and, on the other hand, on active policies of the State and on it having a more leading role did not find sufficient support in society. There is no longer, *tout court*, a developmentalist State in Brazil, much less a business class whose interests are linked to the country's destiny. The failure of the developmentalist experiment suggests a high financialization and internationalization of the productive segments. In turn, a very significant portion of society, particularly the middle class, has a predominantly globalized consumption profile and defines its political support and preferences in a very pragmatic way and based on short-term criteria.

Some mistakes in the operation of the economic policy must be noted, which ended up aggravating the situation mentioned above. A low capacity for negotiation inside and outside the coalition was an important feature of the Dilma Rousseff administration. Frequent changes in the management of macroeconomic prices ended up generating uncertainty. The inability to make an comprehensive infrastructure expansion take off proved crucial. Finally, the inadequate use of two powerful instruments such as the BNDES and Petrobras contributed to make the proposals lose strategic sense. In the end, the wrong choice of 2015 also contributed to leave the impression that the economic policy mistakes were solely responsible for the failure of this developmentalist experiment. However, as we attempted to demonstrate, this is an incomplete and superficial view.

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CHAPTER 22

CAPITALISM, NEOLIBERALISM AND DEMOCRACY: from Hayek to Bolsonaro

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Introduction

Classical liberalism is a normative political philosophy that, of course, values freedom. But which freedom does liberalism want? The individual is its center. Not the collective subject, the nation, or the social class, but the individual to be protected from arbitrary restrictions to his will, as long as he does not arbitrarily restrict the choice of others.

In the canonical sense of Isaiah Berlin (1958), the concept of freedom characteristic of economic liberalism is negative: the freedom of the citizen not to be hindered in the choices regarding his life and the use of his property. Therefore, the State that corresponds to this conception of freedom must limit itself according to the rule of law, that is, not invade the sphere of freedom of individuals and, on the contrary, protect it from arbitrary interference. Furthermore, such a State, supposedly resulting from the social contract between free individuals, must defend the order of contracts voluntarily established between the subjects of rights in their mutual relations.

This conception of freedom is formal: it does not require the individual to actualize it in a particular, substantive, concrete way. The effective capacity to be free is not a central theme of classical liberalism. It suffices that freedom potentially exists within a sphere protected by an adequate legal framework.

This notion of freedom is not exclusive and has coexisted, since its origin, with another, an older conception of freedom. Benjamin Constant (1819) identified it as a characteristic of the ancients, Greeks, and Romans: the right to participate in the collective decisions of the political community. Such freedom no longer concerns the right to be left in one's private sphere but rather to actively participate in the running of the republic, the real power to influence collective decisions.

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Berlin calls it positive freedom: the self-determination to participate in a political collective. While negative freedom values the private individual, the positive conception of freedom values the public man. While the first meaning takes society as a sum of free individuals, the second conceives it as a political body constituted by the debate around the justice of its own form of organization and the behavior of its members. Negative freedom protects the individual in his prerogatives. Positive freedom leads him to debate the very prerogatives of the political body concerning its members in the name of justice and ethical behavior.[2]

In the modern era, the development of capitalism and the struggle for the prerogatives of the owners of goods traded in markets valued negative freedom. The burghers, or the bourgeoisie – the free citizens of the burghs – fought for charters that guaranteed protection against arbitrary requisition of their time or resources by monarchs and nobles who were politically irresponsible before the body of subjects. Later, the subject becomes a citizen when he creates, by revolutionary acts, the constitutional monarchy or even the republic. However, the modern citizen no longer participates directly in the assembly but constitutes political representatives who must guarantee him a private sphere of enjoyment of individual liberty and constrain the monarch and the nobility. Representative democracy goes hand in hand with negative freedom from state power.

In capitalism, however, the body of citizens is separated into social classes, even though the capitalist and the proletarian are subjects of formally equal rights. In practice, the owner's freedom is more substantive and less formal than that of the dispossessed, both in the private and public spheres. In the private sphere, the proletarian has no real option to rent his labor force in exchange for a salary, submitting to the will of the wealthy contractor. In the public sphere, money buys political influence and, in the past, even the right to vote.

In the first liberal-constitutional states, the right to political participation was limited to men with possessions in censitary suffrages. The negative freedom of the minority prevailed over the positive freedom of the majority. The fear that justified the censitary suffrage was that universal suffrage would lead the poor majority to expropriate the wealthy, or at least to tax and regulate the private use of wealth, and, therefore, infringe on the (negative) freedom that the owners wanted as an absolute right.

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2 The concept of positive freedom can also be extended to the private sphere. Amartya Sen (1999) starts from the field of rational individual choice (and not from communitarianism) to propose the concepts of empowerment and agency in order to problematize merely formal characterizations of freedom. Recently, Rob Larson (2018) has argued that by abstracting the existence of economic power within capitalist civil society itself, liberalism (including Sen's) thwarts both the promise of negative (in the field of work) and positive (in the field of politics) freedom.

How did the expansion of democratic political rights coexist with capitalism? What did social democracy want in the 20th century? What is neoliberalism, and how did it react to social democracy and the struggle for social justice? How to think about economic democracy and social justice today? Do public investments and social rights imply a reduction in economic growth, or do they stimulate it and change its quality? Should public spending evaluation and prioritization be done only according to static cost-benefit financial criteria, or do they need to incorporate economic and non-economic externalities? What is the relationship of democracy with public spending, particularly with investment to create infrastructure shared by citizens of different social origins?

To reflect on these questions, we approach the historical pendulum between capitalism and democracy using concepts from Marx to Polanyi to propose two basic theoretical principles present in Marx and Keynes that can guide a research agenda of alternatives to neoliberalism.

The movement from liberalism to democracy

As Norberto Bobbio (1988) has demonstrated, the expansion of popular suffrage throughout the 19th and 20th centuries brought the two concepts of freedom into conflict: a democracy in which every citizen has one vote can and tends to elect a government with the mandate to interfere with private economic decisions and redistribute wealth and income. So, if liberalism legitimizes private property and the freedom of economic contracts on which capitalism is based, isn't democracy contradictory to capitalism?

Before understanding the effects of the coexistence between liberalism and democracy, it is essential to reject liberalism´s myth of origin. According to liberal contractualists such as John Locke (1689), individuals have natural rights before establishing the constitutional contract that establishes society. Everything happens as if individuals preceded society and the state; therefore, society and state result from the union of the free will of individuals and must protect their natural rights, including the right to own private property.

In the 17th century, Thomas Hobbes (1651) investigated the genesis and nature of the society of individuals. Hobbes witnessed the English Civil War, a moment of social anomie that threatened the lives of individuals. As a result, society moved between the impulses of desire and fear.

Hobbes refers to the state of nature as the moment when the constitutional state is absent. In this hiatus of his absence, the spoils of the State, the Mortal God, are distributed among the hordes of the torn civil society. The social contract that gives rise to Leviathan is embedded with the yearnings of desire and fear of violence by all against all. Fear is the fear of the other. Hobbes denies the idyllic state of nature as Locke will conceive it or the noble savage as Rousseau will idealize it. The state of nature in which individuals lived peacefully and man was naturally good could only exist in a society in which the State is consolidated, when sovereign laws already pacify the selfishness of civil life. The vision of the good savage, of the man predisposed to contract with the other, presupposes the State already instituted and organized.

But, for Hobbes, the possibility of the State being submerged in the crisis of civil society is permanent. He rejects the infinity of the social contract. That is, he admits that once established, sovereign power will constantly be threatened by the conflicts of civil society. Hobbes had a pessimistic view of man, a view born of the conflicts that accompanied bourgeois society in the making. There is, in Hobbes, an idea that will reappear later in Hegel: the association of individuals cannot survive without the State.

In his critique of Rousseau's general will and the noble savage, Hegel deplores the narrowness of the concept, imprisoned in the chains of empiricism that define the *general* as the common element of individual sociability. Hegel took up the idea of the State as the culmination of the Spirit, the realization of the universal, the idea that, in its realization, gives generality to particularistic interests. Through the state, particularistic interests would find a general expression.

In the Philosophy of History, Hegel defines "first, the idea of freedom as the absolute and final aim; secondly, the means for realizing it, i.e., the subjective side of knowledge and will, with its life, movement, and activity. We then recognized the State as the moral Whole and the Reality of Freedom, and consequently as the objective unity of these two elements" (Hegel, 2001[1840], p. 64).

It is only through the State that Freedom can be realized. Without Law and Morals, there is no Freedom, only passions and violence. Hence the State doesn't restrict Freedom but "presents the realization of Freedom." (Hegel, 2001, p. 55). That´s why Hegel loathes the idea of a state of nature, where "man is free by nature":

> "Examples of a savage state of life can be pointed out, but they are marked by brutal passions and deeds of violence… Freedom as the ideal of that which is original and natural, does not exist as original and natural. Rather must it be first sought out and won; and that by an incalculable medial discipline of the intellectual and moral powers. The state of Nature is, therefore, predominantly that of injustice and violence, of untamed natural impulses, of inhuman deeds and feelings. Limitation is certainly produced by Society and the State, but it is a limitation of the mere brute emotions

> and rude instincts... Society and the State are the very conditions in which Freedom is realized." (Hegel, 2001, pp. 55-56).

In the Critique of Hegel's Philosophy of Right, Karl Marx criticized Hegel not only for considering the constitutional monarchy as the democratic state par excellence, capable of harmonizing the conflicts of civil society in a "superior" unity. Nor just because Hegel sees bureaucracy as the mediating agent of human emancipation, that is, as a "universal class" in the interest of all. Marx argues that Hegel did not realize the limitations of the constitutional-bourgeois state for human emancipation, restricting it to the political emancipation of the selfish man, the bourgeois. As a result, the latter is confused with the universal man in the liberal declaration of the "rights of man." However, he cannot promote the "real" and "practical" emancipation of all citizens.

The criticism does not mean that Marx rejects the historical advance represented by political emancipation symbolized by liberal constitutions and democracy. On the contrary, Marx, a radical democrat, recognizes its universal value, stating in *The Jewish Question* that:

> "Political emancipation is indeed a great goal. It is not the ultimate form of human emancipation, but it is the ultimate form possible within the present world order. And let it be understood that we mean real, practical emancipation."[3]

Marx's point is that treating "men" as formally equal under the same civil rights does not ensure the effective equality and freedom of citizens divided into social classes. Liberal states did not resolve the social question, and, on the contrary, the legitimation of capitalism by liberalism aggravated social tragedies and authorized exploitation and misery through "free" contracts. Economic liberalism released the socially destructive tendencies of capitalism, before which the Hegelian bureaucracy could do little. Instead of the Prussian bureaucracy, Marx sees the universal historical agent responsible for humanity's real and practical emancipation as a whole in the proletariat.[4]

3 Marx (1959), p. 14. Marx, an indefatigable thinker of freedom, wrote further in the Critique of Hegel's 'Philosophy of Right': "*In democracy the formal principle is simultaneously the material principle.*" (Marx, 1970, p. 30).

4 In the famous final passage of the Introduction to the Critique of Hegel's Philosophy of Right, Marx (1970, pp. 139-142) states: "*It is not a radical revolution, universal human emancipation, that is a utopian dream for Germany, but rather a partial, merely political revolution, a revolution that leaves the pillars of the edifice standing. What is the basis of a partial, merely political revolution? It is this: a section of civil society emancipates itself and achieves universal dominance…In Germany, on the other hand, where practical life is as little intellectual as intellectual life is practical, no class of civil society has the need and the capacity*

In *Capital,* Marx demonstrates how the categories of capital imprison men, becoming real abstractions that function to serve the purposes of infinite accumulation. In this movement of categories, it is capital that is the subject that reduces individuals (praised by liberalism) to its mere "personifications" and "moments." By legitimizing capitalism and hiding economic power relations within civil society itself, liberalism cannot effectively deliver the freedom it promises. Marx also critiques the assumptions of liberalism, showing that, from the outset, in historical reality, the emergence of capitalist society did not result from the "social contract" between free individuals but depended on organized coercion that changed and redistributed property rights. The advent of the modern market as a form of socialization, initially in Northwest Europe, entailed the forced proletarianization of direct producers, a long process by which large landowners violently appropriated communal lands cultivated by peasants with the support of monarchs. The proletarianization of the peasants, however, did not immediately create the labor market.

As Karl Polanyi (1944) has emphasized following the celebrated chapter on Primitive Accumulation in *Capital*, a crucial obstacle to the expansion of the labor market and the development of the industrial labor discipline in 18th century Britain was the existence of alternatives to a 14-hour workday with miserable wages. Proletarians could migrate to occupy new communal lands, beg in the streets, join bands of itinerant workers or rely on the existing social protection network regulated by the Poor Law. As Polanyi and the historian Edward Thompson (1963; 1968) have documented, letting the poor starve to death was unethical. Therefore, it was necessary to remove or severely limit the options available to proletarians and change what was considered ethical behavior towards poverty so that the poor had no alternatives to the rigid regime of wage labor.

Legislation against vagrancy and harsh conditions of imprisonment for deviants were part of the job of disciplining the poor. The last of the traditional systems of social protection in England (the Speenhamland system from 1795 to 1834) resulted from protests induced by high food prices. It sought to restore social order by imposing a minimum wage and providing

for universal emancipation until it is forced to it by its immediate situation, material necessity, and its very chains. Where, then, is the positive possibility of German emancipation? Our answer: in the formation of a class with radical chains, a class in civil society that is not of civil society, an estate that is the dissolution of all estates, a sphere of society having a universal character because of its universal suffering and claiming no particular right because no particular wrong but unqualified wrong is perpetrated on it; a sphere that can claim no traditional title but only a human title…a sphere, finally, that cannot emancipate itself without emancipating itself from all the other spheres of society, thereby emancipating them; a sphere, in short, that is the complete loss of humanity and can only redeem itself through the total redemption of humanity. This dissolution of society existing as a particular class is the proletariat…The head of this emancipation is philosophy, its heart is the proletariat. Philosophy cannot be actualized without the abolition [Aufhebung] of the proletariat; the proletariat cannot be abolished without the actualization of philosophy."

supplies to families. Hence real incomes would not be entirely determined by the labor market´s pay, as the status of a citizen would influence it, much to the annoyance of liberal economists such as David Ricardo, Jeremy Bentham, and Nassau Senior. The new Poor Law of 1834, partly written by Senior, reversed the tendency to protect the poor and stripped away civil rights from those destitute enough to ask for help: assistance would only be provided in reformatories ("workhouses") under extremely harsh working conditions.

In the successful struggle to reform the Poor Law, classical liberal economists offered supposed scientific arguments for why not alleviating hunger was genuinely ethical behavior. Their cultural and ideological struggle was aimed at changing the way the social policy was understood to inspire and justify political movements to reform it, eliminating an obstacle to the complete consolidation of the labor market.

The theoretical point was that social poverty alleviation policies would have unintended consequences that would do more harm than good: they would harm entrepreneurs' savings and investments by taxing them excessively; they would raise wages above the "natural rate," driving more expensive workers out of the market; and would ruin the population's work ethic, bringing widespread economic ruin. These arguments legitimized the successful campaign to reshape the Poor Law and create workhouses in which the poor were forced into a grueling work routine, inducing them to accept any job to avoid detention. We will see later that the same type of criticism against wage and labor regulations would return with the neoliberal reform agenda at the end of the 20th century.[5]

Thus, modern society and markets were not born as a contractual expression of the free will of individuals but resulted from a collective movement through which large landowners appropriated and expelled peasants from communal lands. Later, liberal economists legitimized political pressure from factory owners to change the Poor Law and expand the labor market with disciplined and cheap wage workers. Overseas, the emergence of the modern world market from Western Europe involved military control of pre-capitalist

5 The great economist David Ricardo (1817) could not be clearer: "*When the market price of labour is below its natural price, the condition of the labourers is most wretched: then poverty deprives them of those comforts which custom renders absolute necessaries. It is only after their privations have reduced their number, or the demand for labour has increased, that the market price of labour will rise to its natural price, and that the labourer will have the moderate comforts which the natural rate of wages will afford... The clear and direct tendency of the poor laws is in direct opposition to these obvious principles: it is not, as the legislature benevolently intended, to amend the condition of the poor, but to deteriorate the condition of both poor and rich; instead of making the poor rich, they are calculated to make the rich poor; and whilst the present laws are in force, it is quite in the natural order of things that the fund for the maintenance of the poor should progressively increase till it has absorbed all the net revenue of the country, or at least so much of it as the state shall leave to us, after satisfying its own never-failing demands for the public expenditure.*" (p. 59-62).

regions and trade routes, both for the supply of raw materials or food and as an outlet for part of the metropolitan production and the slave trade, destroying tribal and peasant communities.

According to Karl Polanyi (1944), liberal reforms were the first swing of the pendulum between commodification and social protection that would mark world history ever since. The utopia of European economic liberalism, especially British, was to transform labor, land, and money into commodities so that markets regulated society. It was a political project of commodification based on a fiction, for labor, land, and money are not natural commodities: labor is the very activity of human beings, land is a social ("artificial") appropriation and distribution of nature, and money it is always regulated by the issuing power of the government. Furthermore, the international gold standard was a late historical creation whose operation was not automatic but required coordination and communication between central bankers.

The fundamental political problem with this utopia is that treating labor, land, and money as commodities threatens its existence: the unemployed would starve, nature would be devastated, and liquidity crises would crash banks and the entire payments system. It was "natural" for society to react to this planned utopia, as social reproduction cannot be subordinated and ensured by the self-regulated market. Thus, a pendulum movement (a counter-movement) that took different political forms and rhythms in diverse countries protected nature, fought against unemployment and poverty, and adjusted the supply of money and credit to social demands. Polanyi saw in communism, social democracy, and fascism different reactions to the social devastation brought about by the liberal utopia of the 19th century.

Analyzing this long-term movement considering the British case, the sociologist TH Marshall (1950) identified three long waves of expansion of citizenship rights. The first wave began in the 17th century and focused on expanding civil rights, emanating from the pressure for formal equality of citizens according to laws consolidated in liberal constitutions.

The second wave was the gradual expansion of political rights (to vote and to be voted on) for all citizens regardless of income and wealth starting in the 19th century. Although bourgeois revolutions abolished hereditary rights and created liberal constitutions, political rights were a privilege of the rich that successive expansions of suffrage universalized for adult men in the first decades of the 20th century (women and blacks had to fight longer).

Social rights represented the third wave. It began before the achievement of universal suffrage but was significantly reinforced by it. Social citizenship means having, in Marshall's words, "*the right to a modicum of economic welfare and security to the right to share to the full in the social heritage and* *to live the life of a civilised being according to the standards prevailing in the society*." (Marshall, p. 11).

Although Marshall doesn't quite put it this way, the new generation of social rights was anathema to the self-regulating market utopia. It was the product of society's spontaneous reaction to this utopia through the polls, strikes, and protests. While the utopia of the self-regulating market implied that unemployment was a responsibility of the individual, the development of social citizenship assumed that capitalism was partially responsible so that the citizen was entitled to social protection against its chaotic functioning. As the citizen status embodied new social rights, political citizenship would involve pressures on governments to control the economic cycle to ensure an ample supply of employment opportunities and protect those unable to achieve, in Marshall's words, "*a modicum of economic welfare and security.*"

Both Polanyi and the Polish economist Michal Kalecki (1943) saw not only social democracy but also fascism as a form of reaction within capitalism to the social devastation brought about by the crises of capitalism. Although most businesspeople rejected the different forms of social democracy and state developmentalism in the 1930s and especially after World War II, they could not resist the pressure to expand social and economic citizenship and its inexorable condition, high taxation on profits and wealth, as shown by Thomas Piketty (2013). Labor militancy and the threat of communism brought a series of political pressures that capitalist states had to accommodate:

1. Pressure to institutionalize full employment and, in the Global South, economic development as national goals;
2. Pressure to extend safety nets and welfare states, from unemployment insurance and pensions to the provision of housing, education, and health;
3. Pressure to regulate prices to ensure the expansion of real wages and, in the Global South, industrial import substitution;
4. Pressure to manage international economic relations in a way that protects regions, firms, and jobs, and also to provide States the leeway to achieve full employment or industrial transformation.

Neoliberalism would resist all this, North and South.

Capitalist rebellion and the neoliberal attack on social citizenship and democratic sovereignty

While Marx considered that the urban-industrial proletariat would make the communist movement irresistible to the point of destroying capitalism, in reality, the mass parties created by the working class in Western Europe were vehicles of the social democratic compromise that tamed, for a few decades, the inherent tendencies of capitalism towards the commodification of all social relationships, towards the concentration and centralization of capital and, therefore, of income and wealth, towards crisis and mass unemployment. Karl Polanyi (1944) believed that democracy could embed capitalism (or market society, as he preferred) in social institutions that would employ market forces to benefit social protection and harmony.

Even if the counter-movement did not lead to democratic socialism, Polanyi was confident that it would stop the pendulum between commodification and social protection in favor of the latter. The prognosis seemed to capture the spirit of a time when Franklin Delano Roosevelt (1941) proclaimed the need to protect the four freedoms: not just the three traditional negative freedoms (freedom from fear of arbitrary violence, freedom of opinion, and freedom of religious belief), but freedom from economic insecurity (Galbraith, 1987).

In the first election held after 1945, Conservative Winston Churchill was defeated by Labor Clement Attlee. Accompanied by Aneurin Bevan, his Minister of Health and father of the National Health Service, Attlee designed the architecture of the British Welfare State, inspired by John Maynard Keynes and the report prepared by William Beveridge in 1942. The Beveridge Report (entitled Social Insurance and Allied Services) planted the stakes that would underpin the policies of the Welfare State. Moreover, the *Beveridge Report* received the collaboration of the concepts of the *General Theory of Interest, Employment and Money* – the great work by John Maynard Keynes.

Beveridge pointed to the "five giant evils" that governments were forced to face: want, disease, ignorance, squalor, and idleness. In his *Report,* Beveridge proclaimed that ignorance is a weed that dictators cultivate among their followers but that democracy cannot tolerate among its citizens.

In the West, the social democratic compromise was stable for almost three decades after the defeat of fascism and the socioeconomic tragedies between the two world wars. More than considering the state as a potential source of coercion on the liberty and property of citizens, the working class and the poor who voted for social protection considered politics an ally to increase freedom against the economic constraints inherent in the functioning of the self-regulated market.

The welfare state was based on the positive meaning of freedom (freedom "to") inherent in social rights. As the public services would not be sold but financed by taxes, the negative freedom desired by the rich (e.g., not being "arbitrarily" taxed) conflicted with the concrete freedoms most of the population desired. In a democracy, the majority principle created a structural advantage of positive freedom over negative freedom. Therefore, Friedrich von Hayek saw no radical difference between Beveridge, Keynes, Stalin, and Mussolini (who, by the way, was hailed by Ludwig von Mises just as Hayek himself would celebrate Pinochet). For him, placing social justice at the center of the political and ideological agenda would put Western liberal society on a path of servitude, inevitably leading to the subordination of negative freedom to positive freedom, thanks to the principle of the democratic majority. Therefore, it was necessary to insulate economic management against democracy, shield the minority's right to private wealth against the democratic majority in the public sphere and, thus, make the principles of neoliberalism not only the values of a specific ruling coalition but the basis for the constitution of the state.[6]

Indeed, after the coup that instituted the neoliberal military dictatorship in Chile, Hayek (1973, p. 9-10) admitted that there was a contradiction between capitalism and democracy. He wrongly assumed that most of the population wanted a neoliberal market but was unwittingly led to socialism because of the dynamics of democratic competition in distributing rights. Therefore, a strong man, a dictator like Augusto Pinochet, was needed to institute a new political constitution for freedom, to lay the foundations of a neoliberal state that would bar political "intervention" on the negative freedom of the minority of owners, protecting them against the social rights required by democratic majorities. Thus, a transitional neoliberal dictatorship would be necessary to create, without interference from the democratic majority, a neoliberal state protected by a constitution that permanently shielded it from the impurities of democracy. In Hayek's words:

> "Well, I would say that, as long-term institutions, I am totally against dictatorships. But a dictatorship may be a necessary system for a transitional period. At times it is necessary for a country to have, for a time, some form or other of dictatorial power. As you will understand, it is possible for a dictator to govern in a liberal way. And it is also possible for a democracy to govern with a total lack of liberalism. Personally I prefer a liberal dictator to democratic government lacking liberalism. My personal impression — and this is valid for South America – is that in Chile, for

6 For social and intellectual histories of the neoliberal movement, see Dardot & Laval (2009); Mirowski & Plehwe (2009); Burgin (2012); Stedman-Jones (2012); Mirowski (2013) and Slobodian (2017). For the neoliberal eulogy of dictatorships and its critique of democratic majorities, see

> example, we will witness a transition from a dictatorial government to a liberal government… When a government is in a situation of rupture, and there are no recognized rules, rules have to be created in order to say what can be done and what cannot. In such circumstances it is practically inevitable for someone to have almost absolute powers. Absolute powers that need to be used precisely in order to avoid and limit any absolute power in the future… when I refer to this dictatorial power, I am talking of a transitional period, solely. As a means of establishing a stable democracy and liberty, clean of impurities." (Hayek, 1981, pp. 4-5).

The collective reaction of capitalists against high taxes, strict labor regulations, environmental norms, limits on the freedom of wealth management, etc., assumed the ideological figure of neoliberalism, which inspired or legitimized the campaigns and reforms undertaken by Margaret Thatcher and Ronald Reagan in the late 1970s and early 1980s. The victory of the neoliberal movement belied Polanyi's hypothesis that a democratic society would control capitalism.

In fact, social democracy neither prepared the transition to another mode of production nor contained capitalism's inherent tendencies. On the contrary, induced by the pressures of competition and authorized by the cultural legitimation of enrichment, the "personifications of capital" tend to extricate themselves from the "costs" of the institutions that protect society and nature. The means of social "disembeddedness" are the various technical and organizational innovations that accelerate movement in space-time and save "living labor"; the flight to financial markets or tax havens and the recourse to financial speculation; or productive "relocation" to territories with lower labor, environmental, tax and regulatory costs.

While Polanyi-influenced authors such as Fred Block (2012; 2018) emphasize the "primacy of politics" to understand the emergence of neoliberal reforms, Marxists such as Wolfgang Streeck (2012; 2014) highlight inherent tendencies of capitalism, that is, structural pressures that induce capitalists to bypass routines and traditions (such as state regulations or old-fashioned production methods) in search for extraordinary profits. It is hard to disagree with Streeck that a system based on capital accumulation tends to expand into new sectors and geographic areas, innovating around regulations and national borders. As innovations create profit opportunities, they can also develop unknown risks for the reproduction of labor, nature, and financial systems, as exemplified by "shadow banks" in the 2008 financial crisis, robotization, and global warming.

Given this tendency to "disembeddedness" or at least "bad embeddedness" before social rules and routines, the counter-movement to "re-regulate" and protect society is anything but easy. Streeck argues that capitalism and democracy have always been contradictory. The socially destructive tendencies of the economic system are a "problem" for democracy, which needs to go after and try to contain capitalist anarchy.

Streeck is a necessary antidote against leftists who abandon the concept of capitalism and emphasize the priority of the political and the cultural in a system with uncontrollable structural impulses. Stressing structural trends, however, should not be done at the expense of assessing the correlation of social, political, and cultural forces (which Streeck does not disregard). In other words, analytically recognizing the leading role of the dynamics of capital does not mean ignoring the strength (or weakness) of social resistance. Nor can we assume that business groups interested in neoliberal reforms will sit idle, passively waiting for the microeconomic logic of deregulatory flight to emerge in a critical mass that spontaneously prevails over social opposition. On the contrary, the "personifications of capital" will likely form alliances with neoliberal politicians and intellectuals who support the "free market."

In this sense, the controversy over the primacy of creative destruction or neoliberal politics in the emergence of neoliberal institutions misses the mark: the neoliberal attack needs to occur on all fronts to be successful. That is why capitalists interested in new fields of commodification and profits rationally militate for tax cuts but incur the costs of long-term financing and liquidity provision from the markets that sell neoliberal think tanks, intellectuals, and politicians.

These reformers and bearers of neoliberal reason have the task of reorganizing not only the "economic" institutions of capitalism. They also seek to "economize" the different institutions that guarantee social reproduction in non-economic institutions and spheres of existence. That occurs in two movements. Firstly, questioning the existence or public funding of supposedly "useless" spheres (education, health, affordable housing, etc.) whose reproduction is financed by capitalists through progressive taxation. In short, it is necessary to reduce the tax burden and defund these non-economic spheres considered "useless" according to typically capitalist valuation criteria. Secondly, fight politically to make these activities financially self-sustainable, that is, commodified even if formally public, and if possible, even privatize them, that is, convert them from sources of tax costs for capitalists into new sources of profits.

In practice, this movement implies imposing criteria of private profitability and the disciplinary logic of competition on all spheres of life, returning various risks and costs to "individuals" by defunding the different institutions that guarantee social reproduction: the family and its unpaid labor of reproduction of children and the elderly, as well as of the workers themselves, deprived of daycare, health insurance or retirement, harming families dependent on public services – especially women who "invest" more time in unpaid reproductive labor; the school (in which the education of young people made human capital for a competitive society replaces the pedagogy of criticism and citizen solidarity); the university (privatized and oriented towards early specialization); the criterion of justice and the very access to the judicial apparatus (as a private cost, contributing to formally and substantively emptying the notion of social justice), as well as the environment, health, sport and cultural production.[7]

In other words, a synthesis between the structural and the political can be suggested (to be deepened by future research): individual capitalists tend to innovate to create markets or follow creative destructions that restructure markets globally and evade labor, environmental, tax, and regulatory costs imposed by national sovereignties, democratic or not. However, a collective and deliberate neoliberal movement must guide the State so that it does not oppose the structural tendencies of destructive creation but reinforces them politically and ideologically. Sometimes the government creates new markets topdown, generalizing the disciplinary logic of competition even for the operation of the State and public services.

In this sense, political power to overcome resistance and restructure institutions is a founding element of neoliberalism, as Michel Foucault realized early on. Foucault, one of the most prolific thinkers of the 20th century, is not an economist. Perhaps, for this reason, he understood the meaning of neoliberalism with greater scope and depth. Contrary to what detractors and supporters imagine, he says, neoliberalism is a "governmental practice" in contemporary society. The neoliberal creed does not intend to suppress the action of the State, but rather "Government… has to intervene on society as such, in its fabric and depth. Basically, it has to intervene on society so that competitive mechanisms can play a regulatory role at every moment and every point in society and by intervening in this way its objective will become possible, that is to say, a general regulation of society by the market" (Foucault, 2008[1979], p. 145).

Foucault gives secondary importance to the most obvious hypothesis about the neoliberal art of governing, the one that asserts the imposition of the predominance of mercantile forms over the set of social relations. For the philosopher:

7 On the insulation of the economy from non-economic norms and the invasion of economic criteria on the spheres of social reproduction, the State and subjectivity itself, see in particular Fraser & Jaeggi (2018), Wilson (2017), Brown (2015) and Teivainen (2002).

> "The society regulated by reference to the market that the neo-liberals are thinking about is a society in which the regulatory principle should not be so much the exchange of commodities as the mechanisms of competition… This means that what is sought is not a society subject to the commodity effect, but a society subject to the dynamic of competition. Not a supermarket society, but an enterprise society… I think this multiplication of the "enterprise" form within the social body is what is at stake in neo-liberal policy. It is a matter of making the market, competition, and so the enterprise, into what could be called the formative power of society." (Foucault, 2008[1979], pp. 147-8).

In his course at the College de France, offered between 1978 and 1979, later published under the title "Birth of Biopolitics," Michel Foucault took care to examine the conditions of governmentality in market societies. At a certain point, Foucault concluded that economic theory moves in an institutional and historical void. In contrast, the economic life of concrete men moves in a social order economically regulated by law "based on the market economy." It is not a matter of the market or the State, but one thing and another, and both are oriented toward the universalization of discipline through competition. We can add that the universalization of competition contributes, directly or indirectly, to the generation of profits.[8]

The neoliberal reforms did not remove the State from the economic arena. On the contrary, they were undertaken since the twilight of the 1970s to mobilize the political and financial resources of the National States to reinforce the respective corporations involved in global competition, and to strengthen capitalists vis-a-vis workers, their unions, and democratizing social movements. To shield capitalism from democracy, treaties liberalizing markets for goods and services, and protecting investments and intellectual property rights spread globally, together with strict fiscal and monetary rules administered by technocracies for the benefit of public debt creditors. In the socio-political field, governments are required to control "surplus" populations and social, gender, racial and ethnic discontent to preserve confidence in the "markets" and national attractiveness for direct investment by global corporations.

The State did not leave the scene; it just changed its program. A structuring and active neoliberal state is not a contradiction in terms. With the strong support of the State, global corporations adopted aggressively competitive

8 Foucauldian authors such as Wendy Brown (2015), Pierre Dardot & Christian Laval (2016) and Laval (2017) go beyond the brilliant intuitions of the French philosopher but recognize the weaknesses inherent in his analytical emphasis and/or his precocity in the critique of neoliberalism. Among these analytical weaknesses are the disregard of the logic of capital and the question of democracy. For less sympathetic reviews, see the collection organized by Zamora & Behrent (2016), in addition to Audier (2012; 2015) and Dean (2015).

governance standards, radically saving labor and fiscal costs, in addition to producing negative environmental externalities.

The fact that capitalism has a global scope while democracies are limited to national borders is a highly favorable structural fact for the spread of neoliberalism (Bastos, 1996). Such tension manifests itself in the movement of competitive deregulation. As a sufficiently large country like the US carries out institutional reforms that facilitate the free movement of capital and reduce taxes or regulatory costs, competitive pressure tends to induce imitation, strengthening local groups advocating neoliberal reforms in each polity.

Competitive deregulation also entailed the pressure to reduce the costs of doing business. The ideology of reduction of the so-called "Brazil-cost" due to global competition led, for example, to the abolition in 1995 of the income tax on profits and dividends of owners and shareholders of companies, leaving Brazil in the company of Estonia in this regard. Along with the argument that it was necessary to encourage the rich to save and invest (while workers should work harder with greater competition and less social protection), the maximum and minimum income tax brackets decreased in real terms. The idea was to tax more workers at the bottom and less high incomes at the top, contributing to the increase in Brazilian tax regressiveness.

Under US leadership in the 1980s and 1990s, the competitive deregulation movement was a powerful stimulus to the universalization of neoliberal reforms. Integration between the US consumer market and the Asian factory has reinforced pressures for competitive deregulation. The fact that Asian countries have combined trade liberalization, the attraction of foreign direct investment, subsidies for industrial modernization, and a vast labor market with low wages reinforces the trend toward asymmetric globalization between capital and labor.

Indeed, globalization has increased both the international mobility of capital and the number of workers vying for jobs (mainly in the manufacturing industry), facilitating the relocation of capital to areas of lower wages and labor costs. This generates pressures for the competitive deregulation of the labor market and for lowering wages and workers´ rights.

Capitalists, in turn, also began to press, with the threat of flight, for competitive deregulation in social and environmental protection, for example, and inducing "tax wars" between countries, demanding tax reductions. However, the international migration of workers seeking better salaries and working conditions continued to be severely hampered. At the same time, the regulation of minimum levels of labor, social and environmental protection did not prosper in the economic and social institutions of the United Nations (UN). Instead, the combined forces of globalization, deregulation of labor rights, and technological transformation have driven unemployment, precariousness, low pay, and the degradation of nature.

Since the 1970s, the microeconomic logic of escape from deregulation and the international logic of competitive deregulation have also revolutionized the functioning of the global financial market. After enacting the end of the Bretton Woods system and the gold-convertibility of the dollar, the Richard Nixon administration eliminated the limitations on capital exports that hampered New York's role as a global financial center and induced the flight/relocation of American bank subsidiaries to the City of London. As a result, Wall Street could compete with advantages by recycling petrodollars and expanding credit supply to the peripheries of capitalism. However, the expansion of international liquidity would soon be followed by financial contraction and crisis. When Paul Volcker's interest rate shock in October 1979 sought to restore confidence in the dollar, the financial integration provided by the Euromarket put pressure on exchange rates and interest rates in the rest of the system, causing a global recession that lasted three years, brought down the price of commodities and threw developing countries into an explosive external indebtedness trajectory. Moreover, the FED's monetary policy restricted economic policy autonomy not only in the nationalist periphery but also in developed countries that sought to implement typically Keynesian and social democratic programs, particularly under the French government of François Mitterrand (Kuttner, 2018).

Faced with capital flight and unequal competition with Wall Street and the City of London, the "European fortress" gave way. Mitterrand began to cooperate with Germany to abandon capital controls in the name of a broader strategy, the European Common Market, the strengthening of the global role of the European financial system, and later the monetary union. The OECD would soon abandon the 1961 code on capital movements, which distinguished speculative flows of *hot money* and productive long-term investments. In 1988, the Council of Europe enshrined the competitive deregulation strategy. It passed a formal directive requiring all members of the European Community to abolish remaining controls on the international movement of capital.

The integration of the periphery of capitalism into the emerging financial globalization was less smooth and involved the disciplining of economic policy by the International Monetary Fund. The adjustment programs in the 1980s exchanged bridge loans for the requirement of monetary and fiscal austerity to generate trade surpluses in a scarcity of voluntary external financing. As a result, public investment, social spending, and state-owned enterprises have entered a deep financial crisis. In the early 1990s, the recession in developed countries restored voluntary financing to the periphery. Investors fled low interest rates in the centers and sought profitability and risk abroad, even if local institutions were not yet *market-friendly*. Soon they would be, under the supervision of the IMF and the World Bank: the external bank debt was renegotiated and securitized in exchange for the structural conditionalities that spread neoliberal reforms in the peripheries, expanding the movement of privatization, financial and commercial opening, and contraction of public investment and social spending.

The inflow of capital boosted asset markets and allowed the execution of inflation stabilization programs that relied on exchange rate anchors, inducing brief neoliberalism popularity despite the premature deindustrialization of several countries. In this context, the Bill Clinton administration led the World Trade Organization (WTO) creation. The 1994 Treaty of Marrakesh limited industrial development practices: it imposed restrictions on policies to attract and regulate subsidiaries (such as offering subsidies and market access in exchange for demands for technology transfer, joint ventures, export performance, or import substitution), and limited recourse to copying technologies, subsidies, and protectionism to foster backward industries. The result was the opposite of the demand for a new international economic order favorable to convergence and development made by the so-called Third World countries in the 1970s: it opened markets to global corporations with strict limits to national regulation. As a result, it made it difficult for local rivals to emerge (Chang, 2011).

The neoliberal regulation of the global economy would reach its peak in 1997. That year, the IMF and the US Treasury, led by former Goldman Sachs CEO Robert Rubin, were about to reverse the statutes negotiated at Bretton Woods and ban capital controls between member countries when the Thai crisis ushered in the Asian financial crisis. The situation aborted the change in IMF statutes. Still, it led to unprecedented intervention by the US Treasury and the IMF to reshape development institutions in Asian countries and spread neoliberal reforms (Stiglitz, 2012).

Contrary to the neoliberal hypothesis that financial openness would allow efficient markets to harmoniously allocate savings to where they are most scarce and profitable, globalization has deepened financial instability and crises. While the post-war era of regulated financial markets did not experience any significant banking crisis, Roggoff & Reinhart (2009) documented that the proportion of countries under banking crisis fluctuated between 5 and 10% between the mid-1970s and late 1980, to 20% in the mid-1990s and 35% in 2009. Furthermore, the proportion of countries under banking crisis correlates with the degree of international capital mobility.

Why the succession of cycles and crises? Given the increasing orientation of wealth towards speculation with financial assets, the expansion and contraction of global liquidity started to depend, non-linearly, on the variation of monetary policy in the US. When interest rates are low, the carry trade inflates peripheral currencies as well as risky financial assets and commodities. Given the tolerance for the free movement of capital, legitimized by the theory of efficient markets and the scarcity of "savings" in underdeveloped countries, the speculative boom increases foreign indebtedness and appreciates underdeveloped countries´ currencies. Then, currency appreciation and trade liberalization stimulate an avalanche of imports and severely harm the manufacturing industry, while the remittance of interest, profits, and dividends increases. In other words, it is the capital inflows that, by appreciating the currency, inducing imports, and increasing foreign liabilities, increase the current account deficit and create the need for "savings" to finance it (Coutinho & Belluzzo, 1996, 1998).

For a while, markets, neoliberal ideologues, and government officials celebrate the recovery from the last crisis. At the same time, the abundance of external financing and, eventually, commodity inflation seem to give solidity to the balance of payments of indebted countries. When asset prices and interest rates increase in the US throughout the cycle until they reach a level that reduces the profit differential abroad and encourages more significant repatriation of capital, the end of the expansionary phase is closer. A financial crisis in some relevant market can trigger a reversal that, like dominoes, brings down asset, currency, and commodity prices in an uncontrollable financial contagion, inducing a "flight to quality" toward the dollar and T-Bonds. In this cyclical *flight to quality*, the demand for T-Bonds reduces interest rates in the US while increasing them precisely in countries that need financing for not issuing dollars.

Under pressure from the markets and perhaps under IMF supervision, indebted countries are led to new rounds of public spending reduction, privatization, and institutional reforms. Democracy is substantively and sometimes even formally deflated when the repressive apparatus is summoned to abort popular resistance against the austerity for which no one voted but is required to preserve the confidence of global "markets." Greece's destiny in the 2010s had already been suffered by several countries on the periphery of capitalism under IMF guidance and financial markets´ pressure.

Before the 2008 crisis, the conflict between neoliberalism and democracy was expressed in one way in Europe and another in Latin America. In Latin America, the so-called Pink Wave[9] was a reaction to the social and political

9 The following countries have elected governments to the left of the Political Center: Venezuela (1998), Brazil (2002), Argentina (2003), Uruguay (2004), Bolivia (2005), Honduras (2005), Chile (2006), Costa Rica (2006), Ecuador (2006), Nicaragua (2006), Paraguay (2008) and Peru (2011). Colombia is a known exception, and

impacts of neoliberalism and the crises in the late 1990s, with explicit questioning of the ideologies of minimum state, commercial and financial liberalization, and reliance on foreign indebtedness associated with the Washington Consensus. Reactions to neoliberalism were not the same, although they always involved a reduction in commodification as a criterion for accessing goods and rights. In general, new administrations to the left of the political center influenced income distribution, including renegotiating the distribution of the rents obtained from the inflation in primary exports. With few exceptions, the wave ebbed after the fall in commodity prices and the reaction of traditional groups. After the crises in Honduras, Paraguay, Brazil, Nicaragua, and Venezuela, who will say democracy is consolidated in the region?

In Europe, sovereign powers have been transferred gradually, since 1992, to supranational bodies with an evident representation deficit, without the constitutional treaties going through plebiscites as initially imagined. These supranational bodies - the European Commission and the European Court of Justice - did not hesitate to attack laws and regulations that protected national workers and unions on the grounds that they disrespected the equality of competition celebrated by the Maastricht Treaty, contributing to the dismantling of long-standing corporatist arrangements. Meanwhile, companies circumvented the remaining protections in two ways: either by locating themselves in countries with lower taxes and more lenient labor regulations or by hiring temporary outsourced workers who were regulated by the labor laws of their home country. As is well known, it did not take long for resentment to be channeled less against corporations than in the form of hatred against immigrants, which would worsen after the 2008 crisis (Judis, 2016; Kuttner, 2018; Tooze, 2018).

Indeed, the 2008 financial crisis drove the democratic crisis to the center of global capitalism. This has happened in history, as documented in the extensive comparative study by Manuel Funke and partners (2016, 2018) on the political impact of financial crises and long periods of unemployment. It's not just about Hungary, Poland, Turkey or Russia. Brexit, the election of Donald Trump, and the growing support for the Alternative for Germany (AfD) take place in the very centers of neoliberalism. Workers in devastated industrial areas – since the confluence of technological change, trade liberalization, and currency appreciation under Reagan and Thatcher – eventually abandoned the parties that had left them before. Yielding to neoliberalism, Clinton, Blair, and Schröder led their parties toward the so-called "Third Way" in the 1990s, that is, towards the deepening of globalization, on the one hand, and wage

Chile returned to being ruled by groups to the right of the Political Center in 2010, returning in 2014. See Natanson (2009), Weisbrot (2015), Sader et al. (2016).

stagnation and workfare, on the other. Today a significant part of the losers flirt with authoritarianism, xenophobia, and racism in a potentially violent search for strong leaders, “saviors of the homeland,” on the one hand, and vulnerable scapegoats, on the other, in a process similar to what Karl Polanyi and many others once analyzed it. Once again, the global capitalist arena is not conducive to social, labor, environmental rights, financial stability, and democracy. Once again, too much economic liberalism jeopardizes political liberalism. How is this expressed in Brazil?

Authoritarian neoliberalism on the periphery of capitalism

We have already discussed the general meaning of neoliberalism, but we need to retain what is specific to authoritarian neoliberalism and, in particular, Bolsonarism. After all, the neoliberal formula varies internationally, even if its lowest common denominator is the technocratic and financial limitation of democracy. Using as criteria tolerance for ethnic-racial diversity, gender equality and sexual orientation, and an emphasis on Law and Order, Nancy Fraser proposed to distinguish between conservative neoliberalism (Ronald Reagan, Margaret Thatcher, and Helmut Kohl) and progressive neoliberalism (Bill Clinton, Tony Blair, and Barack Obama). The original formula is the conservative neoliberalism of the 1980s, against which the tolerant “third way” emerged in the 1990s. Conservatives mobilize the “silent majority” for a conservative moral agenda regarding “normal” places of gender, race, ethnicity, and religion. Progressives spare the “competent” minority among minorities with affirmative action programs and symbolically recognize the diversity of cultural, racial identities, and sexual orientations. Meanwhile, capital’s general offensive against labor and the commons is supported as in all types of neoliberalism.

Fraser´s typology is fruitful as it combines distribution and recognition, two criteria usually separated by those who defend the analysis of class conflicts or social movements. One can go further, however. First, *Fraser’s analysis seems to juxtapose rather than combine the two criteria.* However, the combination is more apt because the moral stigmatization of workers always legitimizes the devastating distributive impact of neoliberalism. The misrecognition of workers, as opposed to the praise of entrepreneurs, is also a practice of progressive neoliberalism. The hierarchy of recognition is not just a class-determined practice of neoliberalism; it is class-determined practice with an *ideological and “moral” legitimation*: workers must lose when they are not competent, efficient, responsible, savers and innovators like entrepreneurs. What distinguishes conservative neoliberalism is greater violence against the "loser" (low-wage worker) and the criminal – even more morally stigmatized – and the more or less explicit combination of this violence with discrimination based on gender, race, and sexual orientation. Thus, the meritocratic elitism of neoliberalism is combined with sexist and racist elitism. In this case, the moral stigma of the lousy worker is combined with cultural – if not biological – racism and religious prejudice, according to which the alleged hedonism and sexual debauchery must be punished twice, in hell as on earth. The "single and licentious" mother who supposedly becomes pregnant to multiply welfare transfers, especially the black mother (the "welfare queen"), is the new witch, or at least the new Hester Prynne. For some extremists, the transgender person or the unemployed black gay occupies perhaps a position as despicable as the far-right white evangelical who commits a slaughter against them or on poor immigrants.

The declassification of the Other is the flip side of the self-delusion of moral arrogance, of the assumption that there is a cultural monopoly on competence, work ethic, the ability to save, and dedication to the family – this is the case of the "good citizen" ("homens de bem", "cidadão de bem") in the Bolsonarist newspeak. What is not realized is that neoliberal austerity is not legitimized only by economic theory arguments; it has a discriminatory moral grammar. Misrecognition justifies avoiding "wasting" public resources or paying "exaggerated" salaries. The praise of the moral qualities of the entrepreneur, the morally conservative and supposedly competent worker, on the one hand, and the stigmatization of inefficient workers or the spoiled and irresponsible "minorities," on the other, legitimizes four "austere" public policies: 1) cutting social assistance or its value; 2) workfare: conditioning assistance to "requalification" or active job search; 3) stigmatization of the service to the public good with the cut in the salary and employment stability of public employees, outsourcing and worsening public services and, hence, reinforcing dissatisfaction with the public sphere; 4) the violent and disproportionate punishment of minor deviations, particularly of non-white populations, with mass imprisonment, the best examples of which are the appeal to Law and Order by the Republicans under Richard Nixon even before neoliberalism, and Brazilian popular punitivism in recent decades. In sum, neoliberalism runs the full gradient between symbolic violence and physical state violence.

In this sense, progressive neoliberals do not abandon neoliberalism's discriminatory moral grammar. If they did, they would only be progressive and no longer neoliberal. Instead, they only spare the "competent" minority among minorities designated by cultural, racial, and sexual orientation identities. They reject sexist and racist elitism but preserve and even exalt meritocratic elitism. Thus, trade unions remain helpless in the face of neoliberal "deregulation," and "incompetent" workers of all identities continue to be punished by the restructuring of the global labor market in recent decades, albeit with less symbolic violence and eventually with more extended unemployment benefits. The criterion of supposed meritocratic "competence" continues to organize social discrimination, punishing poorer workers, blacks, Asians, Africans, Latinos, and whites who feel despised by the once social democratic parties converted to neoliberalism. In addition to being defeated by the misfortunes of capitalist competition, the humiliation associated with unemployment or precarious and poorly paid employment *is combined with the symbolic violence inherent in the meritocratic criterion that blames the worker for the "failure" of poverty* while rewarding cultural elites who consider him not only ineffective but often a culturally "deplorable" archaic traditionalist.

That is why, in the United States, someone like Donald Trump – a New Yorker Robber Baron – can present himself as a defender of the white working class who is the object of scorn by the "cultural elites" of the predominantly Democratic coastal states. Although his attack on neoliberalism is limited to foreign trade, Trump can deceivingly present himself as a champion of white workers against the "globalist" elite that allegedly betrayed the nation's genuine ancestral people – confused with the descendants of European immigrants and not the offspring of native peoples. The "globalist" elite would only have compassion for minorities descended from enslaved people and illegal immigrants. Thus, once in office, Trump could further attack the social protection of all workers, gaining increasing support among white workers without university degrees. Perhaps because he did so with greater violence against stigmatized minorities and successfully activated conservative whiteness – and not class affiliation - as a criterion for political alignment of their constituencies. A racist technique of dividing the popular strata that has been successfully used by white supremacists in the South of the United States since the 19th century and extended since Nixon (the Southern Strategy) to different regions of the North.

In this sense, the term used by Fraser to designate Trump in the presidential campaign – a *reactionary populist* – is interesting as an ideal type, but it is problematic when contrasted with the term with which she designates him in office – an *ultra-reactionary neoliberal* who had betrayed the campaign promises to attack neoliberalism. The problem is that the white industrial workers who voted for Obama and transitioned to Trump in the 2016 elections, perhaps attracted by his reactionary populism, constitute a minority of the Republican electorate who, under Trump, continued to vote for conservative neoliberalism. On the contradictory electoral front of 2020, the majority of those who voted for Trump come from evangelical groups and neoliberal smallholders (of various races, though mostly white), the traditional base of the Republican Party in recent decades. If populism is a technique of mass mobilization that seeks to activate them against an arrogant elite, *Trump's type of populism has been neoliberal since electoral propaganda.* After all, he did propose in his campaign and, once in office, applied austerity against the minority protected by the "globalist" elites who supposedly betrayed the "true people." But, apparently, he never criticized neoliberalism outside foreign trade. The neoliberal program´ result is the disaster in the pandemic, an even worse catastrophe where neoliberalism had privatized access to healthcare – like in Mexico and Peru – or where a crueler copy of Trump ruled, as in Brazil.

In addition to juxtaposing rather than combining the criteria of distribution and recognition, the second problem with Fraser's typology is that it does not sufficiently recognize the third type of neoliberalism. That is common in Latin America and predates the cases described: *authoritarian neoliberalism*. That takes state violence to another level in which the economic rights of capitalists not only trump the political rights of citizens – as in all neoliberalism – but suppresses them. It is not just about neutralizing democracy with technocratic and financial rules that limit government policies. Authoritarian neoliberalism makes explicit the ultimate political program of neoliberalism: to raise itself to the status of state policy (and not only of government policy) and impose its economic and social program against all resistance. In this case, a repressive neoliberal state reforms society, from top to bottom, without giving voice to the dissenters and political rights to the resisters. Exactly as proposed in Hayek's praise of Augusto Pinochet.

Authoritarian neoliberalism cannot be understood without the political intervention of the military "party," a state corporation excluded from the political system of developed countries since the Second World War but strengthened by the Cold War in the Global South. Fraser indeed refers to August Pinochet, but he appears as a prelude to the conservative neoliberalism of the North and not as a pioneer of authoritarian reformists who already had, in the 1970s, two similar neoliberal dictatorships in South America (Uruguay and Argentina) and would have, in the 1990s, the first neoliberal self-coup (in Alberto Fujimori's Peru). Jair Bolsonaro fits into this type of neoliberalism. Still, he complements the use of the military party with a neo-fascist mass mobilization that bears less resemblance to the political propaganda technique of military dictatorships than to Integralism, updated for the time of social media.[10]

Another feature of authoritarian neoliberalism from Pinochet to Bolsonaro is the rejection of Latin American or Third World economic nationalism,

10 Integralism was the Brazilian fascist movement and party in the 1930s.

that is, the execution of a "globalist" economic program despite the symbolic valorization of the "national tradition" in the field of moral intolerance. The "genuine people" that would be defended by authoritarian neoliberalism against globalism is no longer the worker of the manufacturing industry protected from foreign competition but the conservative moralist who rejects the "import" of the "globalist" struggle for racial, gender, and sexual orientation equality. Or the import of human and ecological rights guidelines that are the subject of international treaties, UN agencies, and NGOs. Moral traditionalism, punitivism, and economic globalism are also characteristics of conservative neoliberalism in the Global North. Still, its corporations globalize more than they are "globalized"; that is, they buy smaller companies from the Global South, lead and gain from the diffusion of neoliberal treaties and the opening of emerging markets across the globe. In the Global North, the reaction against globalization in *reactionary populism* combines cultural traditionalism and neoliberalism domestically with a limited resumption of economic nationalism. It means nationalist action against imports of goods and immigrants that would harm local workers, as opposed to the economic globalism typical of all forms of neoliberalism. Thus, economic nationalism, to different degrees, characterizes Trump's America, Brexit's England, Marine Le Pen's France, Putin's Russia, Kaczyński's Poland, and Orbán's Hungary, but not Latin American's *authoritarian neoliberalism* from Pinochet to Bolsonaro.[11]

In Brazil, the connection between the old Third-world nationalist authoritarianism and the new neoliberal authoritarianism is the *declassification and exclusion of the working people* legitimized by meritocratic, sexist, and racist elitism and the anti-communist and libertarian rhetoric shared with the American extreme right. In the authoritarian neoliberal imaginary, the people who, after the unique democratic experience of 1946-1964, could no longer vote because (as expected) they had shown "not knowing how to vote" started to vote "wrong" again after redemocratization in the 1980s by being "bought" by demagogues who only offered costly rights without demanding duties and disciplines. Worst still, the supposed demagoguery of labor rights from pre-1964 populism extended post-1985 to the issue of rights to the recognition of "identity" differences. From the perspective of the contemporary extreme right, any concession of social rights and recognition of diversity came to be seen as a retreat from the supposed new tactic of global communism, manifested in "Cultural Marxism" and "globalism." "Cultural Marxists" would seek a

11 Intermediate cases between nationalist reactionary populism and authoritarian neoliberalism are perhaps those of Erdogan in Turkey and Duterte in the Philippines, which we have not dealt with for reasons of space (Bluhm, K.; Varga, M., 2019).

new Road to Serfdom by adding “identity” agendas to the old populism of labor and social rights, in any case placing the agenda of social equality at the center of the political agenda. In the face of the alleged risk of communism posed by the fact that the struggle for democratization that resulted in the 1988 Brazilian Constitution extended rights to the political and social terrain and the battle for equality of gender, race, ethnicity, and sexual orientation, Bolsonarism wants a return to the Point Zero before the start of the new Road to Serfdom. In the current reactionary movement, it would be required to return to the pre-Constitution period of 1988 and even pre-Consolidation of Labor Laws, the legislation that codified labor rights in 1943. As Bolsonaro said at dinner in Washington on March 17, 2019, before Olavo de Carvalho, Steve Bannon, Walter Russell Mead, and other traditionalist far-right intellectuals:

> “What I always dreamed of was freeing Brazil from the influence of the nefarious left-wing ideology... Brazil is not an open terrain where we intend to build things for our people. We must deconstruct a lot, undo a lot, and then start doing it again. May I serve so that at least I can be a turning point, I’m already very happy. Our Brazil was moving towards socialism, towards communism, and God´s will was, I understand myself that way, that two miracles happened, one my life, the other the election. It is this mission that we were given... so that we can carry out what we want to deliver, not in terms of the presidency, but in terms of democracy and freedom for our children.” (Marin, 2019).

Therefore, in the Bolsonarist imaginary, what is the usage of the Brazilian people, given that it should not have labor and social rights, and perhaps even political ones? The people serve to work without whining, obedient, willful, and silent before the bosses, as opposed to lazy and indolent, even rogue and vagabond, as represented by the stigmas attributed to manual workers and “non-graduates” throughout Brazilian history. In Bolsonarism, neoliberal symbolic violence stigmatizes and encourages hatred against “indolent” and “rascals,” “pampered” and “victimized,” and, at worst, “thugs” and “vagrants.”

The misrecognition of the people not only legitimizes more exploitation, justifying upward income redistribution, as in all neoliberalism. In authoritarian neoliberalism, the radicalization of symbolic violence authorizes physical violence not only to exploit more but to *expropriate* – be it labor and social rights, be it emergency aid or basic income to enjoy the social distance necessary to survive a pandemic, be it time to unpaid reproductive work, whether public, indigenous, or maroon lands and ecological conservation areas. To legitimize a violent movement of large-scale expropriation, the meritocratic ideology typical of all neoliberalism is not enough; it is necessary to reinforce the duality of recognition/stigmatization between the "good citizen," on the one hand, and the discrimination of gender, race, ethnicity and sexual orientation, on the other.

The target of the Brazilian far right is not just the rabble but also the liberal-democratic political system that protects rights against violent expropriation. This justifies conceptualizing Bolsonarism as neo-fascist (Boito, 2020), emphasizing the authoritarian revolt of part of the middle class (defined by non-manual work and the ideology of meritocratic competence) against the rise of manual workers (formal and informal). Hence the middle-class functions as a mass base for the employers' offensive against workers in general. However, the criterion of social class preferred by Boito (from Nicos Poulanzas, 1970) is insufficient because it does not incorporate the discrimination of gender, race, ethnicity, and sexual orientation as necessary.

By the way, in an insightful analysis of the emergence of left and right populisms, John Judis (2016; 2018) argues that any populism interpellates the people against an elite enemy (using the concept of populism in terms of Ernesto Laclau, 2005; and Chantal Mouffe, 2016). The difference is that, on the left, the elite is economic-based and is blamed because it gains from globalization, while the majority of workers (defined by the left based on professional insertion and not racial or ethnic characteristics) lose rights, jobs, and relative income. In right-wing populism, the interpellation is not addressed to workers as a whole but to the set of workers racially and ethnically identified, supposedly *as the true Nation*. The "genuine people" are also interpellated against an elite, but against a "globalist" elite that protects racial and ethnic minorities, and groups with a "debauched" sexual orientation, using resources stolen from the "genuine people." Therefore, it is not just about attacking the rights of minorities but also the elites that defend universal human rights not restricted to the supposed "genuine people." As this elite has a power base in the liberal-democratic political system, it is necessary to reform democracy or, in the most extreme movements, to replace it with a dictatorship.

In Brazilian neo-fascism, in fact, structural machismo and racism are inseparable from the attack on democracy. Therefore, Bolsonarismo combines neo-fascist and neo-Nazi elements, particularly in a long connection between Bolsonaro and the Brazilian neo-Nazi movement (Filho, 2019; Demori, 2021). In the Bolsonarista imaginary, the "good citizen" is harmed by the minorities of dissolute feminists and gays, by rogue or even murderer blacks and Indians who are protected by the "corrupt" and "globalists" of the old political elite. The subaltern targets of the ire of the "new politics" became accustomed to "suckling on the teats of the State" for the benefit of "corrupt" and "populist" politicians who bought their votes with a "politically correct," "paternalistic" and "globalist" discourse. An "elitist" discourse that defends the "human rights" of bandits but ignores the damage that the violence of criminality has on orderly workers. The "old politics" also justifies the punishment of police officers who take risks to protect the "good citizen" and, to make matters worse, impose high taxes to feed corruption and to help those who have no merit through monetary transfers to the poor and inmates, racial quotas, and public banks. The "good citizens," in turn, have merit and work ethic, so they do not need corruption, welfare assistance, or crime to ascend. However, they are harmed by a lack of morality and impunity: the alleged result of so much moral and political corruption was the economic crisis of 2015 and 2016 and the explosion of urban crime. In fact, according to an opinion poll by Data Popular (Alencar, 2015), 67% of respondents declared that the main cause of the economic crisis was corruption (not austerity, neoliberalism, or capitalism). Given the hegemony of the moralistic interpretation of the crisis, for a large part of the population, only a harsh intervention, above and against the system, could destroy so much indecency. Especially if led by white men like Bolsonaro and judge Sergio Moro, and having the northeastern Lula da Silva excluded from the dispute due to political persecution masked as a neutral judicial process.

This is not to say that all those who voted for Bolsonaro in 2018 are sexist, racist, neo-fascists, and, much less, neo-Nazis. Many undoubtedly wanted to restore old social, racial and gender hierarchies threatened by the struggle for equality and recognition. Among these, are those who, even after the pandemic disaster, continue to support Bolsonaro unconditionally. However, it is likely that the majority of Bolsonaro voters in the 2018 second round yearned for an alternative solution to the traditional political system in the face of economic disaster, corruption scandals, and the rapid expansion of crime since 2015. Bolsonaro's loss of popularity in 2021 indicates that machismo and racism are not a majority or, at least, strong enough to ensure unconditional support. All the more so because neoliberalism has been proving to be as illusory a solution as the "new policy" of a government plagued by corruption scandals and increasingly supported by the "old politics" that Bolsonaro had promised to fight.

It is not just through the globalization of the struggle against "Cultural Marxism" and "globalism" that the American extreme right has influenced the Bolsonarista movement. Financial liberalization, trade liberalization, and the liberal doctrine of comparative advantages connect like a glove to the interests of the employers' coalition that supported the 2016 coup and the rise of Bolsonaro. In 2015 and 2016, a united capitalist alliance was formed against the Dilma Rousseff administration that even incorporated the interior industrial bourgeoisie. However, the political coalition was led by the banking bourgeoisie and the bourgeoisie associated with foreign capital (Bastos, 2017). The entry of industrialists into the anti-PT bloc would end up weakening the party organization that protected them from foreign capital in the power bloc, creating the conditions for a new round of neoliberal reforms that would expand "free competition" not only for workers but also for entrepreneurs who depended on state protection against foreign capital. The existence of a social coalition does not exclude the possibility of adjustments of positions with the change of administration. If, with Michel Temer, the advance of the associated bourgeoisie and foreign capital against the temporary alliance of the interior bourgeoisie and workers is clear, this accelerated with the Bolsonaro administration (Bastos, 2020) without harm to the banking bourgeoisie:

1. The retraction in the role of public banks, manifested in the sharp deceleration in the growth of their balance sheet and the sale of assets, led to the cut of cheap commercial credit offered to small companies, with the possible objective of privatizing public banks or, at least, increasing the shares of market and interest differentials charged by large private banks;
2. In addition, the shrinkage of credit subsidies operated by public banks, particularly BNDES, has the same effect of harming non-financial companies that depend on local loans and favoring the private financial sector;
3. The contraction in public orders for goods and services associated with the reduction of public investment by the direct and indirect administration under the impact of the fiscal austerity policy is demanded by the financial markets and by private companies that compete with public ones, but it also harms non-financial companies and workers;
4. The main neoliberal reform of the Bolsonaro government – the pension reform – aimed at instituting a capitalization regime that would expand the private pension market even more than the growth potential resulting from the actual reform, that is, the elimination of public pension by contribution time (regardless of age);
5. The massive disinvestment by Petrobras and the change in the Pre-Salt concession form - with permanent tax exemptions - favor multinational corporations and minority shareholders at the expense of local suppliers, workers, and state and municipal finances, which can be reproduced on a smaller scale with the capitalization of Eletrobrás (the

public electric power conglomerate) and other privatizations (such as state water and sanitation companies, or the Brazilian Mail - Correios);

6. The inflation of oil derivatives, electricity, gas, and other administered prices, thanks to the reduction of subsidies and the insistence on treating state-owned companies as if they were private corporations subject to stock-value maximization rules, favors shareholders and harms consumers and business users;
7. Tolerance of foreign acquisition of local corporations (such as Embraer – later rejected by Boeing) tends to harm the interests of local suppliers, workers, and municipal finances. It may also bring higher prices to users (due to market concentration and calculating local profits in dollars).

From Temer to Bolsonaro, the result of the neoliberal program is a failure from the point of view of its declared objectives in terms of economic growth, unemployment, and the public debt/GDP ratio. An even more severe failure if we consider the imminent risk of acute water shortages provoked by droughts that, in high probability, result from climate change and the deforestation of the Amazon rainforest supported by the Bolsonaro government.[12]

Deforestation in the Amazon is a product of the pressure to open up land and expand the frontier of capital accumulation inherent to a productive structure increasingly specialized in agricultural, mineral, and metallurgical commodities. This structural connection began before the Bolsonaro government and even before the 2016 coup. 2010 was the last year of a 7-year series, starting in 2004, of reducing emissions associated with land use change. The further deterioration was concentrated in the Amazon region, representing 87% of the total in 2019 (Alencar et al., 2021). This started before the dismantling of command and control institutions, deriving from the pressure that the end of the stock of cheap land created by the record of deforestation between 1992 and 2003 (taken advantage of by the agricultural expansion until 2010-2). In sum, it was connected to the dynamics of the land market pulled by the growth of the extractive and predatory economy (Costa, 2021).

Ideologically, the expansion of the frontier of bare land integrated into the world market is articulated with the liberal doctrine of comparative advantages: the Global South is responsible not only for specializing in the supply of agricultural, mineral, and metallurgical commodities but also for greenhouse gas emissions inherent to deforestation. For diplomatic coverage of the intended acceleration of the expropriation of indigenous lands and conservation areas in the Amazon, the Bolsonaro administration sought to lean

12 According to interviews with climatologists Carlos Nobre (Azevedo, 2021) and José Marengo (Pontes, 2021).

on Donald Trump and US ecological imperialism. Contrary to a nationalist critical of "globalism," upon returning from a visit to the US, Bolsonaro stated as an authoritarian neoliberal that he had offered Donald Trump and US mining companies the priority of expropriating land in the Amazon, thus justifying his intention to appoint his son Eduardo Bolsonaro as ambassador to Washington.[13] The subordinate association project involved the proposal to build a US military base in the Amazon – confirmed by the president in a televised interview and abandoned under solid objection from the armed forces (VEJA, 2019).

In mid-2022, the result of the authoritarian neoliberal program is tragic not only in the economy and ecology. Brazil is the second country most affected by the Covid-19 pandemic in terms of deaths (in absolute numbers), with more than 685,000 deaths. Is it an exaggeration to call the tragedy a neoliberal genocide? If the authoritarian neoliberal gave the people the task of working without whining so that social isolation would not hinder the economy and the generation of profits? The denial of the pandemic, mask use and vaccination, and the praise of the "early treatment" of chloroquine connect with the rejection of the evidence that governments that decided earlier to flatten the curve of infections also recovered their economies faster. The comparative evidence is that, once the pandemic is uncontrolled, the expansion of voluntary isolation is inevitable even before the overcrowding of hospitals, morgues, and cemeteries imposes the enactment of lockdowns that deepen the damage to the economy. The later the enactment of lockdowns, the greater the damage to the economy. In this case, there is no economic recovery with laissez-faire but with public planning.[14]

However, the result of the neoliberal program is a success from the point of view of its undeclared objectives, that is, to put trade unions and social movements on the powerless defensive in the face of the attack on labor and social rights; to return the cost of the tasks of social reproduction to families dependent on public services – especially women who perform unpaid reproductive labor -; to transfer public assets to private companies

13 In April 2019: "When I was with Trump now, I talked to him that I want to open up for him to explore the Amazon region in partnership. As it is, we are going to lose the Amazon, that area is vital for the world." (Deutsche Welle, 2019). In July 2019: "Very rich land (it is the Yanomami indigenous reserve). If it joins with Raposa Serra do Sol, it's absurd what we have of minerals there. I'm looking for the first world to explore these areas in partnership and adding value. Hence, my approach to the United States. That's why I want a person I trust at the US embassy. Do you think I would put a son of mine in a prominent position like that to pay shame? I want quick and immediate contact with the American president" (Dal Piva, 2019).

14 Bastos et al. (2021); Dabla-Norris, E., Khan, H., & Lima, F. (2021). It is clear that early social isolation to flatten the curve of infections earlier must be accompanied by testing policies, quarantine of the infected and contact tracing to avoid the resurgence of the pandemic, as well as a government guarantee of income protection to reinforce adherence. to isolation (Knudsen, 2020).

(especially foreign ones) and increase the profitability of large corporations. In short, the movement to reduce salary, tax, and regulatory costs is defended by the business associations that support the Bolsonaro government and the expansion of privatization, commodification, and financialization of public goods and services that harm workers, consumers, public servants, and small and medium-sized companies. It is difficult to imagine that the promise of neoliberalism was not illusory, given its political objectives and, in particular, its scarce scientific foundation, which we will now analyze.

The reality of neoliberalism and the urgency of the alternative

Neoliberal reforms promised to release the manifestation of intrinsic inequalities between individuals to increase savings and the growth rate. However, even before the 2008 crisis, failure was evident. The concentration of income and wealth has brought about a reduction in growth rates and the duration of expansionary phases, as studies by the IMF have fully shown analyzing several countries (Ostry et al., 2014a; 2014b; 2016). With a methodology that compares countries of similar income before and after neoliberal reforms, Mark Weisbrot (2015) also documented a reduction in growth rates among developing countries.

The concept of prior savings as a determinant of productive investment and the natural growth rate should have been further shaken as, in the US, the unprecedented increase in the share of profits in income did not bring about an increase in the investment/GDP ratio. Despite tax cuts, financial liberalization, the massive increase in leverage, and the expansion of credit at low interest rates from 1990 onwards, the proportion of investment in GDP fell from 20.5% in the 1980s to 18,7% between 1990 and 2009 (Chang, 2011).

It is not just that the financial system has changed: the pursuit of short-term gains with financial assets, rather than the patient accumulation of productive capital, has governed the accumulation of assets by the "productive" corporations themselves. As a result, the ratio of financial assets/non-financial assets of US non-financial corporations rose from a relatively stable level of 38% (between 1972 and 1982) to 57% in 1989, 73% in 1997, more than 100% in 2001, falling to 82 % in 2007 and stabilizing around 100% between 2009 and 2011.

Despite the evidence, the theoretical prevalence of the previous savings-investment link in contemporary orthodoxy is overdetermined by the permanence of a conception that continues to understand consumption as the purpose of capitalism and, therefore, conceives investment merely as consumption deferred in time. However, if the purpose of investment is not consumption, but the accumulation of abstract wealth, then financialization is not a deformation but an exacerbation of the goal of capitalism. It is because productive investment is just one alternative among others and is dominated by the unstable valuation of a set of financial assets and national currencies that Keynes proposed, in the face of the financialization of his time, both controls on international movements of capital, “financial repression” and the “socialization of investment.” After all, free capital markets do not specialize so much in investing in the creation of new productive capacity as in speculation on changes in the prices of assets representing old wealth, and this dominates the valuation and accumulation of new wealth (Keynes, 1936, ch. 17; Belluzzo, 2016).

The transfer of a growing portion of “savings” to the financial system in search of the valorization of existing assets does not deviate but instead reiterates and deepens the finality of capital as the accumulation of abstract wealth. Under neoliberalism, capitalism was “disembedded” from the old social controls that “repressed” finance and forced its allocation to new productive investments. In France, the profit rate of financial corporations was negative between the early 1970s and the mid-1980s. Still, it reached the profit rate of non-financial corporations in the early 1990s, at around 5%, reaching more than 10% in 2001, while the profitability of non-financial companies fell to 3%. In the US, the profit rate of financial companies was lower in the 1960s-1970s, but after 1980 it varied between 4-12%, while it ranged between 2-5% in non-financial companies (Duménil & Lévy, 2005). As a result, financial companies’ profits reached half of those of non-financial companies in the 2000s, starting from 20% in the 1970s and 1980s (Glyn, 2006). However, the comparison underestimates the importance of finance to overall profitability because, as we have seen, the profit of non-financial corporations has come to rely on increasing profits generated from financial operations.

The growth of finance was much more significant than the “underlying” economy, an indicator that the increase in “savings” was not channeled into new productive investments and that the extraction of rents through control over the financing channels and the system of payments grew without social return. The stock of financial assets in relation to world production increased from 120% to 440% between 1980 and 2007, reaching 700% for highly financialized economies such as Great Britain (Palma, 2009). In the US, it fluctuated between 400-500% between 1950-1980 but reached 900% in the early 2000s (Crotty, 2007).

In short, the idea that there is a restriction on the supply of savings or of involuntary unemployed that would nullify the public spending multiplier by forcing interest, wages, or inflation to rise is entirely refuted by the plethora of financial wealth and unemployment that accompanied financialization even before the 2008 crisis, although it was radicalized afterward. It is not the savings constraint that limits economic policy; it is the political, economic, and ideological power of big finance and big corporations. It is not the availability of surpluses per se but their distribution and the criteria of power and valuation that allocate them.

Contrary to the assumption of exogenously determined potential output, one must start from the Latin-American historical-structuralist conception that the diversification of the economy increases the growth rate and its sustainability over time. In other words, a structuralist alternative to the *mainstream* must start from the understanding that the limit to the growth rate of a capitalist economy, especially a peripheral economy, is not the scarcity of previous savings or voluntary unemployment but the complexity of the productive structure. And not only because the degree of complexity influences the balance of payments structural constraint.[15]

Production complexity is manifested in growth rates and the sustainability of expansion, as complex productive chains a) spread innovations more quickly and increase productivity; b) increase the multiplier and accelerator effects of autonomous spending as the productive structure becomes denser; c) reduce demand leakage (increase the multiplier and reduce the income elasticity of imports) and can stimulate an increase in the complexity and (income and price) elasticity of exports; d) due to the impact on the elasticity of exports and imports, they limit the occurrence of the balance of payments restrictions. This line of research goes far beyond the mere macroeconomic impact of autonomous spending.

In this sense, a structuralist view must also admit that there are limits to growth that are not reduced to the size of effective demand impulses, even if such limitations are not those indicated by the economic *mainstream*. Although the limit to growth is not prior savings, this does not mean any investment can be made regardless of market size, external competitiveness, technological capacity, and the financial centralization possible in each economy. The crucial difference is that such limits do not result from a sum of individual "choices" between consumption and savings (investment) but from the structural inability to carry out certain investments (public and private), even with demand incentives. It is not, therefore, a question of further limiting the consumption of the masses to increase "prior savings" but of attacking structural limitations, particularly in the coordination of investments, technological capability, and financial centralization.

In addition to seeing "prior savings" as an essential constraint in the economic sphere, neoliberal reason seeks to "economize" everything, that is, to invade all spheres of existence and value them according to economic criteria,

15 For a good synthesis between the structuralist tradition and the economy of complexity, see Gala (2017).

or rather, the criteria of contemporary finance and its short-termism. Financialization, by the way, socially means an extension of the evaluation criteria and discipline of short-term financial markets to other markets and spheres of society (Lazzarato, 2011; Sotiropoulos, Milios & Lapatsioras, 2013).

A long-term post-neoliberal alternative cannot limit itself to correcting the “market failures” of financialization. Instead, it should propose another way of valuing public and private investments that society can regulate through the State, as we will see. Financialization is not just a “market failure” but a systemic pattern of wealth management (Braga, 1993).

The IMF gives an example of a partial and insufficient reaction to disciplinary mechanisms or at least to the economic crises resulting from financialization. One of the recent changes in the IMF’s recommendations is the admission of some propensity to financial risk, which could not fail to occur after the exchange rate crises in the 1990s and the 2008 crisis. So, the IMF started recommending temporary capital controls to protect the balance of payments and macroprudential regulation to identify and control internal risks (Blanchard et al., 2010; 2013; Ostry et al., 2012a, 2012b).

However, neither financialization is seen as structuring the new capitalism’s dynamics, nor do the asymmetries of globalization and financialization have structural effects on “developing” countries. That means that international asymmetries only appear as they are accounted for in the balance of payments but not as reflected in the financial and productive structure of developing countries. In other words, the *mainstream* preserves the assumptions of neutrality of money (and financial assets) when analyzing domestic risks and the international transfer of “savings” between relatively circumscribed national economic systems when analyzing balance of payments imbalances.

In this case, an alternative to the mainstream depends on returning to *the fundamental methodological principle of the Latin American structuralist tradition. That is, researching how dependence is internalized in underdeveloped countries and modifies their structure from within,* as it integrates them as a subordinate part in the accumulation strategies of global corporations and constrains economic policy.[16]

It is essential to go beyond the macroeconomic aggregates and inquire about the articulation between the accumulation strategies of national companies and foreign subsidiaries, on the one hand, and the financial and commercial flows that are recorded in the balance of payments, on the other. The hypothesis

16 A broader programmatic discussion could start, for example, from the set of proposals made by Robert Kuttner (2018, chap. 12). The issue of structural dependence on global capitalism will be a central theme of Celso Furtado (1973) until his last book, being also emphasized by Maria da Conceição Tavares (1971; 1985; 1997; 2000) and Tavares & Belluzzo (1980; 1984; 1997). For the interpretation and presentation of data on the recent development pattern and its crisis in Brazil along these lines, see Rossi, Mello & Bastos (2020).

is that these flows are subordinated to those strategies and, therefore, to change the flows, it is necessary to change the accumulation strategies first.

It is necessary to avoid, from the outset, a separation between "real" and "financial" capitalism, which is often expressed, on the one hand, in a critique of "fictitious capital" without understanding, on the other hand, global corporations as the maximum expressions of the "financial capital" closely intertwined with the logic of financialization (Chesnais, 2016). Therefore, it is not just a matter of reaffirming, correctly, that capital flows condition the evolution of the current account, instead of meeting the "savings" needs to be determined by the excess of internal "absorption" and consumption in the manner of the open economy IS-LM models (Mundell-Fleming). And not just to reaffirm that such capital flows are subject to *feast and famine cycles* and that, therefore, capital controls and regulation of the derivatives market are necessary to insulate the foreign exchange and securities markets against portfolio operations that constrain macroeconomic policies (Coutinho & Belluzzo, 1998; Carneiro, 1999, 2008a; Bastos, 1996, 2003; Bastos et al., 2006; Prates, 1997, 2005; Conti et al., 2014, Rossi, 2015).

Financialization affects microeconomic decisions not restricted to agents operating in the capital, foreign exchange, and derivatives markets, whether financial or non-financial companies. For example, it is not just a matter of remembering that an essential part of inter-company foreign loans comprises arbitrage or financial speculation operations that only reduce transaction and tax costs compared to traditional loans or portfolio investments. Both are destined for operations in asset markets and not for *greenfield operations*. Or remember that mergers and acquisitions of existing wealth, aimed at concentrating markets and rationalizing capacity on a global scale, assume increasing importance in FDI compared to new productive capacity, especially in times of deceleration, crisis and exchange rate devaluation in peripheral countries.

Furthermore, financialization has changed how the productive global corporation operates, and not just in the sense of leading it to maximize treasury operations with old wealth, as we have seen. In general, the shortening of the terms and the increase in the expected rate of return on financial operations influenced productive investment. Corporations tended to re-concentrate their *core business* near their headquarters and rationalize production chains globally, that is, to "repatriate" and to re-specialize certain activities previously (partially) decentralized in different regions of the global periphery. Increasing profitability in the *core business* of technological innovation, patent production, product design, and brand advertising required streamlining the group's global operations. That meant the elimination of redundancies through disinvestment and cost reduction on the periphery, impoverishing previously verticalized production chains and dense industrial systems like the Brazilian one, as the "multi-domestic" corporation gave way to the global network. In this network, there is remote control of the production chain's peripheral links, internalized by affiliates or externalized to subcontractors with strict production specifications. That became possible and profitable due to the lowering of data processing, communications, and transport costs and the cost-cutting produced by the specialization of the *core* and periphery, in addition to reducing trade tariffs. With very few exceptions, global competition is led by aggregator companies (Nolan et al., 2008; Nolan, 2012) and not by national companies or even by subsidiaries of large groups in peripheral countries, which specialize more in assembling final goods (as in Mexico and Brazil) and/or in intermediate links in the global chain (as in Asia).[17]

Furthermore, financialization did not only influence how the global corporation operated in redefining the international division of labor and in the internalization of this division within the group through intra-firm trade. In general, the transfer of company ownership to institutional investors and the maximization of shareholder value as a management criterion shortened productive investment and technological research horizons. Short-termism is mitigated when costs are externalized to the public fund (where there is a national system of innovation) or shared in technological alliances between giant aggregator corporations on a global scale.[18]

In this sense, Hopkins & Lazonick (2014) even document an increase in resources allocated by large global corporations to R&D (despite an even greater increase in the allocation of resources to share buybacks) and a significant drop in R&D productivity. That has occurred as the in-house research labs of large companies, which employed long-term scientific teams, were dismantled and replaced by *startups* run by scientists and funded by venture capital firms interested in rapidly extracting value from innovations. The value extraction is done less with the long-term use of innovations than with the IPO of the startup or its acquisition (or rather, its patents, without mandatory transfer of technical teams, especially when proprietary) by an already consolidated corporation, taking advantage of the boom phase in stock appreciation.[19]

17 In the typology proposed by John Dunning (e.g. Dunning & Lundan, 2008), FDI between centers tends to be efficiency-seeking, strategic asset-seeking and market-seeking, while investment in the periphery tends to be market-seeking or resource-seeking, in this case in search of natural resources and/or abundant and cheap labor.

18 Chesnais (2016); Hopkins & Lazonick (2014); Mazzucato (2013); Weiss (2012; 2005).

19 To explain the loss of R&D productivity in a context of financialization (especially in the US), we raise three other complementary hypotheses that should be researched: 1) it is necessary to distinguish and estimate the monetary cost of R&D (currently intensive in well-paid professionals and technological inputs sold at high profit by patent-protected oligopolies) and the number of hours actually devoted to R&D, as a positive growth rate in the monetary value of total R&D is compatible with a much lower growth rate in the number of hours

The problem is that the impact of financialization on productive investment seems even more significant in peripheral countries with currencies and markets that are vulnerable to liquidity and commodity price cycles and do not have S&T systems comparable to those of the centers. In this sense, the greatest hope of "attracting" investments in countries with large domestic markets without a significant number of aggregator companies is to increase the rate and sustain the growth phases of these markets and the planning of the recovery of some of the lost productive links with industrial and technological policies, when private investment is induced by growth (Bastos, 2012). In Brazil, on the contrary, the financial instability, the weakness of the S&T base, and the subordinated integration in the global value chains were reflected in the horizon and profile of industrial investment of the foreign subsidiaries and local companies, favoring quick modernization against the long expansion of the new capacity, reducing innovative risks and, therefore, deepening international technological asymmetries (Carneiro, 2008b; Bielschowsky et al., 2015).

In this sense, the form of insertion and operation of foreign subsidiaries in the strategies of global corporations seems to represent a structural limitation to development. That said, it is essential not to exaggerate the novelty of these dilemmas or idealize the pre-globalization past, as the root of the problem is older. As several Latin American authors pointed out, decades before financialization, the control of foreign subsidiaries over the main branches of the manufacturing industry in Latin America and, in particular, in Brazil, allowed the internalization of specific productive and technological capabilities that would or would not have been created in-house or would take a long time to be. However, the essential part of the technological development was preserved in the headquarters (not being duplicated by the subsidiaries) and transferred in the form of intra-firm trade of capital goods produced, on a profitable scale, in the headquarters or under its command.20

The composition of exports would also change relatively little and slowly in peripheral countries that were industrializing with a strong presence of subsidiaries, as the technological dependence of the subsidiaries and their subordination to the global strategies of the parent company limited their penetration in developed markets and the industrial branches of greater growth.

actually devoted to R&D and even with its reduction; 2) to be more specific, the increase in the monetary cost of R&D may be related to the rising cost of inputs and the increasing remuneration of scientists and other professionals who own the startups (as opposed to long-term employees in the old laboratories) and thus may overestimate the number of hours actually dedicated to R&D; 3) this is all the more likely because there is a tax incentive to register various activities under the R&D rubric (in order to be entitled to illegitimate tax credits), which, by the way, is tacitly encouraged in the advertising of several tax planning companies on the internet and has been investigated by the IRS since 2016.

20 For example Furtado (1967, ch. 23; 1969, ch. 21; and 1973), Tavares (1967; 1971), Tavares; Serra (1970), Fajnzylber (1970a, 1970b, 1976), Coutinho; Belluzzo (1977), Tavares; Belluzzo (1980).

International. Thus, the long-term local development of innovative capabilities was limited, as innovations were concentrated around the national innovation system at the centers of global corporations. That is why the proportion of foreign-owned patents in the Brazilian total has always been much higher than in the Core and why both local patent creation and R&D are smaller. That has always had little to do with educational provision, tax rates, or the exchange rate/wages ratio, coexisting over time with wide oscillations of these variables.

The Latin American authors mentioned above pointed out the difference between the ability to produce when the most modern production goods can be imported and the ability to innovate and compete in the technological frontier. This technological asymmetry modifies the form of Core-periphery relations because the capacity to produce industrial goods can advance with the transfer of technologies carried out by FDI and with the internalization of part of the sector of production goods. However, it reproduces the international polarization of the producing centers of new technologies and user regions.

Specifically for Brazil, the limits for import substitution have been in the segments of production-to-order capital goods with higher technological content and tonnage, plus some branches of innovative consumer goods since the 1970s. Moreover, given the incomplete internalization of the production goods sectors, the limits for improving the quality of exports always existed even at times when the exchange rate was significantly depreciated and real wages historically reduced, that is, in the 25 years between 1967 and 1992. After all, even when industrial FDI was "multi-domestic," with nationally highly-verticalized production chains, the branches in Brazil privileged production capacity for the domestic and regional market but always depended on the global supply network of higher added-value parts, pieces, and components. That only deepened when the technological frontier changed in the 1970s and 1980s and when globalization increased the specialization of developed countries in certain links in the production chain far from the core business of corporations in the most technology-intensive branches (Sarti & Laplane, 2003; Hiratuka & De Negri, 2003).

It was not because Brazil had an appreciated currency that it was left out of the investments that changed the technological matrix of the world manufacturing industry in the 1970s and 1980s, as the Brazilian currency depreciated. Of course, the technological asymmetry worsened when neoliberals opened the market, imagining this would be enough to attract greenfield FDI. Still, the increasing Brazilian lag from the changing technological frontier did not result only from the 1991 trade opening and the 1994 currency overvaluation shock. On the contrary, it is undeniable that the subordinated integration project to the global corporation value chains, in a context of financialization and short-termism of the subsidiaries, increased technological dependence and reduced the domestic added value. But the lag from the technological frontier precedes neoliberalism (Suzigan, 1992, 2000; Coutinho & Ferraz, 1994).

In summary, the division of labor within large global corporations always has overdetermined and limited the degree of technological advance in the manufacturing industry and the foreign trade specialization in Brazil, regardless, for example, of fluctuations in the exchange rate/wage ratio. That became clear once more after the global overproduction generated by the 2008 crisis and reactive strategies in the West and Asia (Bastos & Hiratuka, 2020). Therefore, if currency appreciation did not fully determine the type of integration of Brazil in globalization, it is unlikely that currency depreciation can itself reverse it.[21]

The issue should be further studied. Bastos (2012), for example, proposed combining currency depreciation with domestic market growth (not only induced by wage increases but also by industrial policy and infrastructure investments) to stimulate Brazilian reindustrialization. The Dilma Rousseff administration carried out both initiatives without the expected results (Bastos, 2017). Perhaps the hypothesis that the exchange rate positively correlates with industrial profits and accumulation should not be assumed but demonstrated. The problem is that it supposes, at the limit, a structure composed only of national firms or at least a system in which financial liabilities and production goods only originate in local currency, that is, the inverse of the existing structure. Under conditions in which gross external liabilities (not just *hot money flows* and derivatives market positions) and a high import coefficient of technological inputs are structural elements, that is, do not result from a sporadic excess of internal absorption, currency depreciation does not depress real wages only. It also seems to lower companies' profit rates (financial and non-financial) in which financial and technological dependence is expressed. As national companies are less capable of leading global production chains as aggregators of systems, they may be even more vulnerable than subsidiaries to currency depreciation, with no guarantee of an increase in exports that compensates for the higher cost of foreign financial liabilities and imported inputs. Without ready answers, it is necessary to study more and better the impact of exchange rate movements on the profitability of capital in conditions in which dependence has been internalized in the structure

21 All the more so because, as we will see below, the inflation in external inputs and liabilities makes the impact of currency depreciation on capital accumulation and the rate of profit uncertain without previous structural transformations. As Bresser-Pereira has been suggesting, the negative impact of currency appreciation on certain industrial sectors can be offset by trade policy (tariffs for imports and subsidies for exports), avoiding the generalized impact of currency depreciation on costs associated with external liabilities and imported inputs without national similar. The author considers such a policy *second-best* (if exports of commodities are not taxed and the inflow of foreign capital is not blocked) and, contrary to what is suggested to investigate here, he prefers a linear increase in import taxes on manufactured goods to the option of selective tariffs for competing and non-substitutable products: Bresser-Pereira (2012; 2018).

of the economy and the balance sheet of companies, subsidiaries or not, integrated or not to global value chains.[22]

In short, a genuinely structuralist understanding of development constraints requires a comparative analysis of the structure of capital ownership, financing, production, and insertion into intra-firm value chains that goes beyond basic macroeconomic prices, as well as policy proposals that recognize such structural asymmetries. That is even more important in the contemporary context. The structural weaknesses in financing capital accumulation, productive-technological specialization, and the insertion of the Brazilian economy into world capitalism are more clearly revealed now that the pattern of competition and technological trajectories are undergoing profound transformations.

At the time of the Covid-19 pandemic, China, the United States, and the European Union announced recovery and reconstruction programs that clarified the national priority given to the so-called Green Transition and Industry 4.0. Due to the catastrophic risks perceived with climate change, the announced projects of industrial transformation are combined with investment programs in infrastructure and transformation of the energy matrix that point in the direction of productive transformation in the coming decades. The success of industrial/technological policy and investment plans coordinated by the Chinese state imposed a new competitive challenge that even the advanced degree of financial centralization and technical complexity of business organizations in the US and Europe seems incapable of overcoming without state coordination and public investment at a new level (Belluzzo; Elias, 2020). After decades of neoliberalism, the infrastructure and energy

22 In this sense, at least since Krugman (1986), neoclassical international economics has presented models and econometric studies that suggest a significant reduction in the exchange rate elasticity of foreign trade in a context of globalization of value chains by corporations and the use of transfer pricing and pricing to market in intra-firm trade. For recent studies, see Ahmed et al. (2016), Bussière et al. (2016), Fontagné et al. (2017) and Soyres et al. (2018). In the heterodox field, several studies have been incorporating “original sin” in estimating the impact of exchange rate variations on earnings and growth: Kohler (2017), Ribeiro, McCombie & Lima (2017). For studies of the Brazilian case, see notably Santos, C. et al. (2015a, b), Carvalho & Teixeira (2015) and Diegues et al. (2017). Furtado already pointed to the problem in 1974 and, in 1983, proposed to understand the relationship between the globalization of production and the price system in the following way: “The transnationalization of important sectors... (heralds) the emergence of a more comprehensive system, whose contours and other structural features are only sketched. There is no doubt that the price system that governed international transactions is undergoing important changes. This system was the result of interactions between economies endowed with monetary autonomy. Exchange parities were defined as a function of balance of payments positions... In the present situation, a large part of foreign exchange operations takes place within the scope of the companies themselves. As production costs become internationalized, the significance for foreign trade of variations in exchange rates is reduced... The comparative costs of the traditional theory referred to an trade between economic systems, while trade that takes place within the scope of a transnationalized company is based on a calculation concerning the organization of production... Thus, a price system specific to the transnationalized space tends to emerge, independent of the local monetary authorities” (Furtado, 1983, pp. 110-). 1). See also Furtado (1974), item 1.

transition programs announced in the West in 2021 are an attenuated copy of the planning according to national missions for the coordination of public and private investments that was typical of Brazil before neoliberalism and became exemplary of China from the 1980s onwards.[23]

In the Global South, however, such coordinated national investment strategies can have the opposite effect on economies specializing in supplying agricultural, mineral, and metallurgical commodities whose production, as in Brazil, is intensive in natural resources and Greenhouse gases. Although the demand generated by such commodities represents a boost to economic growth, it can threaten their environmental sustainability and increase conflicts provoked by the predatory expansion of the agricultural, logging, and mineral frontier. In addition, it reinforces a predatory productive specialization that deepens ecological risks in Brazil and, paradoxically, makes the country more vulnerable to retaliation from the same markets where the demand for commodities originates. Whether the climate super-imperialism of developed countries to punish countries that deviate from climate agreements – or what geographers Joel Wainwright and Geoff Mann (2013; 2018) call *Climate Leviathan* – is more likely than global Eco-socialism in the short term in the face of ecological tipping points (Noam Chomsky and Robert Pollin, 2020), Brazil's unsustainable trajectory can only be resolved from within, albeit with international cooperation. If, in Brazil, the correlation of forces makes more advanced solutions unfeasible in the medium term – or in the short time available before the ecological disaster – unsustainability can only be avoided if the country also imitates, in its way, the model of planning according to national missions for the coordination of public and private investments that will organize the capitalist competition and the green and digital technological trajectories in the advanced capitalist countries. It is beyond the scope of the chapter to explain why such a response to the new global challenge remains far from Brazil. However, it goes without saying that it is entirely contrary to the neoliberal-authoritarian orientation of the Jair Bolsonaro administration.

23 Isabella Weber (2021, p. 244ff) showed how the economists who were responsible for the Chinese strategy in the 1980s studied and sought to imitate positive aspects of Brazil's development strategy, the destination of some of their visits to get to know the Brazilian reality with a large number of long interviews (one of which at Unicamp with one of the authors of this chapter).

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