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**The new role of Multilateral Financial
Institutions in Brazil in the 2010's – a
comparative analysis with Chile**

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Summary

Since their inception in the second half of the 20th century, Multilateral Financial Institutions have played a key role in financing the reconstruction and the development of country-members. Due to the level of social and economic maturity achieved in Brazil in the 2000's, there is room for a gradual adjustment in the way the World Bank and the Inter-American Development Bank maneuver programs in the country. Despite its enormous challenges, Brazil has experienced a long period of macroeconomic stability and consistent policies addressed to overcome social inequality. In Chile, the framework of the programs of the Multilateral Financial Institutions is based on advisory and knowledge-intensive services, as a result of the level of development experienced in that country. It is expected that in Brazil the traditional Multilateral Banks' lending programs be gradually relatively less important, as opposed to the improvement of a non-lending services portfolio in the country.

Key-words: Brazil, Chile, World Bank, Inter-American Development Bank, Multilateral Financial Institutions

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1 Introduction: Brazil and the Multilateral Institutions

This paper aims at discussing the new perspectives related to the role of Multilateral Financial Institutions in Brazil, namely the World Bank and the Inter-American Development Bank. Brazil has already reached a level of maturity in its social and economic development, despite of all the challenges and structural gaps that still have to be addressed. Considering the current status of development of the country, there is room for a reorientation of the Multilateral Banks' strategies, focusing on non-lending services and technical assistance rather than on traditional loans provided to the country-members.

The method of analysis used is a comparative study between Brazil and Chile. The latter has been a step ahead of the other South American Countries (Brazil included) in respect to social and economic development and therefore has been addressed with non-lending services by the Multilateral Banks along the last decade. This operational framework that was designed and executed due to the institutional, social and economic stability reached by Chile in its recent history.

The paper is organized in the following chapters:

- a) In this introductory chapter, the main macroeconomic and social achievements in Brazil in the last two decades are discussed, with the addition of an analysis on the breaches and difficulties that still hinder the growth and development of the country. In parallel, this chapter provides an overview on the multilateralism, focusing on the aftermath of the creation of the "Bretton Woods" Institutions (IMF and the World Bank), and the subsequent creation of the Inter-American Development Bank (IDB) in the 1950's. Considering that the World Bank and the IDB are the most important Multilateral Financial Institutions working in Brazil, the chapter also discusses the institutional strategies of these Banks, as an anticipation of the particular strategies that will be described in the following chapter.
- b) In chapter 2, a brief discussion of the Chilean recent developments in the realm of macroeconomic management serves as a starter for a comparative analysis with Brazil. The two countries are then put side by side in a framework of selected economic, social and "governance" indicators.

- c) In chapter 3, the current strategies prepared by the World Bank and the IDB for Brazil and Chile are portrayed, revealing the priorities and the more important themes that are highlighted in the agenda of the referred Multilateral Institutions for the countries which are subject to this analysis. The Brazilian case is subject to a specific analysis concerning the clear shift of the operations from the federal to the subnational levels in the last decade.
- d) Finally, in the final chapter the “country strategies” outlined by the Multilateral Banks for Brazil and Chile are compared in regard to the main issues addressed by those strategies and the instruments used by the Banks in each country. The conclusive remarks indicate that there is room for development of an even more qualified approach of multilateralism in Brazil, not only through the execution of a lending program, but also with the deployment of services that can add value to the public policy design and implementation, following the trend that has already been put in place in Chile.

1.1 Brazil: an overview of the 90´s and 2000´s and the challenges ahead

Brazil has made considerable economic and social progress since the mid 90's, when stability was achieved with macroeconomic adjustment, inflation reduction and exchange rate stabilization. In the last decade Brazil strengthened a policy of conditional cash transfers to the poorest families, to break the cycle of poverty from one generation to the next.

This virtuous combination has elevated tens of millions of people from poverty and built a stable economy, with high foreign currency reserves and a growing internal market. The country paid off its International Monetary Fund debts and was one of the first economies to effectively tackle the 2008/9 global economic crisis.

1.1.1 Economic aspects

1.1.1.1 The macroeconomic milestones achieved in the last two decades

Economic policy in Brazil has been managed for almost two decades under a pragmatic centrist position (Kingstone and Ponce, 2010, p. 99), which was characterized by: i) commitment to monetary stability and control of inflation, ii) a

flexible approach to the Washington Consensus¹ program and iii) commitment to reverse poverty and inequality.

Under the two terms of the Fernando Henrique Cardoso Administration (1995-2002) Brazil consolidated its monetary stability, which was achieved after the issuing of the “Plano Real” in 1994. The consolidation of a market-oriented strategy followed the economic liberalization initiatives that had been originated in the early 1990’s. The most important outcome of the “Plano Real” was the control of inflation, “with positive effects on poverty, consumption, and foreign investment” (Kingstone and Ponce, 2010, p. 103).

The struggle against inflation depended on controlling the fiscal imbalances and attracting strong capital inflows, notably through very high real interest rates which had collateral effects on the public sector debt and domestic investment. Since a more fundamental fiscal adjustment imposed politically controversial changes that could not be achieved in the short run (such as the social security reform), control over inflation in the first term of President Cardoso had an emphasis on maintaining high interest rates and an overvalued exchange rate anchor to guarantee the price stability. According to Baer (2008, p.133), “as imports prices in local currency terms fell, price increases among domestic producers, by necessity, became increasingly moderate”.

Due to an overvalued exchange rate that caused negative impacts on exports and to the absence of an effective fiscal adjustment, the GDP Growth in 1998 was close to zero, reflecting the pessimism that followed the crisis in Asia (1997) and Russia (1998).

“Thus the government found itself in a vicious circle: to maintain the exchange rate and to finance its deficit it had to borrow at a rising interest rate, which in turn worsened the fiscal situation and, by extension, further undermined investor confidence” (Baer, 2008, p.141)

In the end of 1998 Brazil received an adjustment package from IMF and the World Bank, which imposed basic fiscal reforms, including the social security system. Up to that time, the government had been dealing with its fiscal problems relying on the receipts from privatization and the increase in internal and external indebtedness. In early 1999 the bundled “high interest rate + overvalued exchange

¹ A set of policy advices addressed by the Washington-based institutions (IMF and World Bank) to Latin American countries as of 1989, which included: fiscal discipline, a redirection of public expenditure priorities toward fields offering both high economic returns and the potential to improve income distribution, tax reform (to lower marginal rates and broaden the tax base) , interest rate liberalization, a competitive exchange rate, trade liberalization, liberalization of inflows of foreign direct investment, privatization, deregulation (to abolish barriers to entry and exit) and secure property rights (Williamsom, 2000)

rate” were abandoned and the government allowed the exchange rate to float freely. Afterwards, the government initiated the fiscal measures to achieve the primary budget surplus required by the IMF and established an inflation-targeting policy.

With the inflation under control, the high level of interest rates caused the nonperforming of banking loans by many firms and individuals and compromised the results of many private and public financial institutions. According to Baer (2008, p.145), in the first three years of the Cardoso administration (1995-1997), the Central Bank liquidated, intervened in, or closely oversaw 43 financial institutions. To guarantee a stable environment for the banking operations, the government founded a deposit insurance mechanism called Credit Guarantee Fund, to which all financial institutions were required to contribute a percentage of all balances in accounts that would be covered by the Fund. Mergers and acquisitions were fostered by the government and financed through the Program of Incentives for the Restructuring and Strengthening of the National Financial System (PROER), which provided a line of credit below the market interest rate for the acquiring banks. In the case of the state banks, which were mostly used to bridge state treasuries’ credit shortfalls, the government implemented the Program of Incentives for the Restructuring of the State Public Financial System (PROES). This in practice represented the “federalization” of the state banks, with the purpose of reducing the role of the public sector in the financial system.

In the field of the real economy in the second half of the 90’s, Brazil had a significant improvement in the capital formation, due to increased direct investment of domestic and foreign groups that were taking over privatized enterprises (Baer, 2008, p.143). Competition resulted in a constant effort of the firms to improve technology and the labor productivity.

In the early 2000’s Brazil had experienced a smooth transition to a flexible exchange rate. After a strong devaluation occurred in 1999, the monetary and fiscal restraint helped the economy to make this transition and stabilize (Gallo, 2010, p.45). In 2000 the Government enacted the Fiscal Accountability Act (LRF), which: i) established limits for personnel expenditures and indebtedness at all levels of government; ii) attached new permanent spending mandates to permanent revenue increases, and iii) forbade debt refinancing between different levels of government. Due to the compliance with these provisions, the Federal and sub-national levels reduced the net public sector (federal and sub-national

levels) debt-to-GDP ratio from 57% in 2002 to 38.5% in 2008 (World Bank, 2011, p.2). As a result, Brazil was recognized in 2008 as a secure and stable environment for investment by the rating agency Standard & Poor's, which upgraded the country to investment grade, a move that was later also confirmed by Fitch Ratings.

In late 2002 and early 2003 the nervousness and fear came over the financial markets in the aftermath of the election of the leftist President Lula da Silva, who took office in 2003. But the fears were gradually overcome, considering the orthodox management of the economy by the Lula administration, which expressed irrefutable commitment to price stability and kept the inflation targeting as the central mechanism of the economic policy. According to Mann (2010, p.239) the inflation targeting regime established severe self-imposed limits on authorities' macroeconomic room for maneuver.

In 2003 the control of inflation was also supported by fiscal surpluses, restrictive monetary policies and greater openness toward international capital (Kingstone and Ponce, 2010, p.108). Subsequently, this orthodox approach provided the benefits to the economy and the monetary policy was gradually loosened, resulting in an average annual GDP growth of 4.7% in the period from 2004 to 2008 against an average of 1.9% in the period from 1999 to 2003.

The global economic environment provided important favorable conditions in part of the two-term period of the Lula administration. China and India were keeping the pace of the growth in the world economy, which resulted in surpluses in the Brazilian balance trade and the accumulation of significant amount of international reserves. These reserves summed US\$ 288.6 billion against a gross external debt of US\$ 351.9 billion, both measured by the end of 2010. The improvement in the external liquidity was extremely relevant, considering that by the end of 2003 Brazil had international reserves of only US\$ 49 billion and a gross external debt of US\$ 235.4 billion ².

One of the most relevant consequences of the orthodoxy, represented by tight fiscal and monetary policies in the early years of the Lula administration, was the solid performance of the current account in the balance of payments, due to a continual growth in the exports and recovery of the foreign direct investments (Baer, 2008. P.158). The performance of the balance trade in the 2000's was obtained mainly through the modernization, expansion and diversification of the

² Source: <http://www.bcb.gov.br/?RED-SERIERIH> and <http://www.bcb.gov.br/?SERIEDEBH> (accessed on February 29th, 2012)

agribusiness, due to the consolidation of agricultural research, professionalization of commercial farmers and development of agribusiness complexes (Mueller and Mueller, 2010, p.138). In addition, Brazil also diversified its export markets, with large increases in trade with the Mercosul, the Asia-Pacific region (especially China), and the European Union, not only with commodities but also manufacturing products.

The sequence of two terms of the Cardoso administration followed by the two terms of the Lula administration adopted a liberal pattern of accumulation more integrated with the global economy (Silva, Braga and Costa, 2010, pp.127-129). The set of dominant economic policies in this 16 year-period (1995-2010) can be summarized by the following decisions:

- a) The creation of the real, currency which reunified the functions of money (medium of exchange, unit of account and store of value) and restored economic stability;
- b) The restructuring and capitalization of the banking system, in which the Central Bank has a high level of independence and public banks (such as BNDES, Banco do Brasil and regional Banks from the Northeast and Amazon regions) provide the funding for productive investment;
- c) The expansion of productive investment by large companies, in response to growing internal consumption;
- d) The upgrading of agribusiness competitiveness, resulting in a significant increase in exports and a positive contribution to the balance of payments;
- e) The reduction of external vulnerability due to the growing accumulation of international reserves and assets, which exceeded the external debt since January 2008.

1.1.1.2 The challenges ahead in an instable global economy

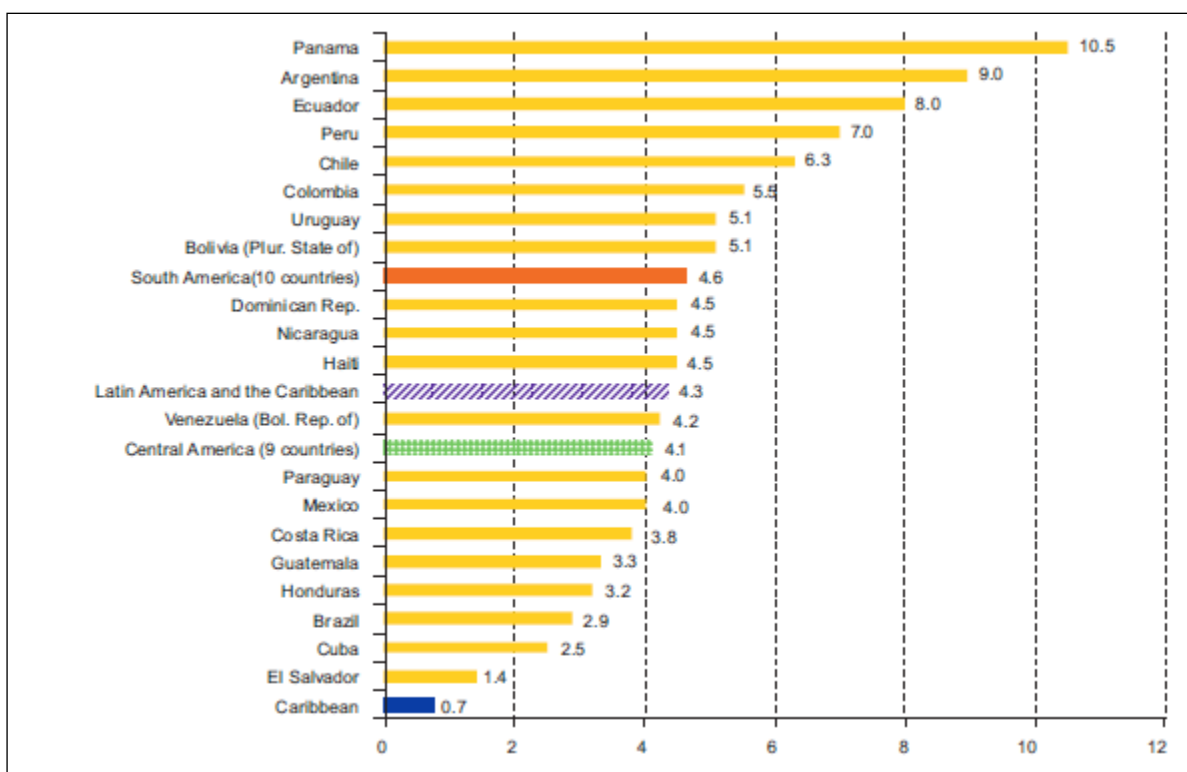
According to the World Bank (2011a, p.3), Brazil has shown relative resilience during the global financial crisis, as a result of the good countercyclical macroeconomic management and the soundness of its financial system. In sequence to the 2008 global economic crisis, the country suffered a reduction in external and domestic credit and a decline in external demand and investment, resulting in a recession that lasted only two quarters. The measures adopted by the Government to face the crisis combined: injection of liquidity into the banking

system, a reduction in interest rates, and expansionary fiscal policies such as tax reductions for selected consumer goods and public investment growth.

Due to this prompt countercyclical response by the government, the Brazilian economy recovered from a close to zero GDP growth in 2009 to a significant 7.5% growth in 2010. Household consumption contributed with 4.4 percentage points of the referred GDP growth in 2010. Considering an Aggregate Demand³ side analysis of the GDP, investment grew 21.8% in 2010 compared to 2009, while household consumption increased by 7%, reflecting the growth of wages and credit operations.

After the significant growth of 7.5% in 2010, Brazilian GDP lost momentum in 2011 and the growth remained below the Latin American average, following the forecast by ECLAC (figure 1).

Figure 1 – Latin America and the Caribbean – Estimate Growth Rates – 2011



Source: Estimates of the Economic Commission for Latin America and the Caribbean (ECLAC, 2011b, p.10), on the basis of official figures

The estimates of the Economic Commission for Latin America (ECLAC)⁴ and the Caribbean indicate that the economic recovery of 2010 in the Latin

³ The GDP expressed by the Aggregate Demand side is the linear sum $C + I + G + NX$, where C is the consumption by domestic households on final goods and services, I is the investment in new capital goods, G is the Government purchases of goods and services and NX are net exports (exports minus imports)

⁴ The ECLAC is one of the five regional commissions of the United Nations and was founded with the purpose of contributing to the economic development of Latin America, coordinating actions directed towards this end, and reinforcing economic ties among countries and with other nations of the world (www.eclac.org.br)

American countries was sustained by the countercyclical macroeconomic policies implemented to face the financial crisis of 2008-2009 (ECLAC, 2011, pp.10-11). In this regard, the expansionary policies that were adopted, with cuts in taxes and increasing in the government expenditures, had to be downsized in 2011. In addition, the inflationary pressures imposed the need to maintain high interest rates, especially in Brazil, where the cooling of economic growth was deliberately instigated to avoid overheating after the growth surge in 2010 (ECLAC, 2011b, pp.11).

In the second half of 2011, the world economy was still under a cloud of uncertainty due to the debt crisis in the euro area and the mediocre growth of the United States economy. This pessimism had an impact on international commodity prices, especially metals and some agricultural commodities what explains in part the sluggish recovery of the trade balance in Brazil in 2011.

According to ECLAC (2011, pp.27), in the period from 2007 to 2010 the Brazilian exports were distributed between the United States (12.5%), Europe (23.2%), China and Japan (14.0%) and Latin America (22.1%). Although Brazil does not depend on a specific regional market, the country may face difficulties in its balance trade due to the cooling economic activity especially in Europe, which is driving down the demand for goods. If the emerging economies such as Brazil continue to grow faster than the developed countries, the impact on exports of the former will depend on the relative importance of each market.

The environment of uncertainty as depicted by ECLAC is confirmed by the World Bank (2011, p.6) in its prospects on the Brazilian economy for the period from 2012 to 2015:

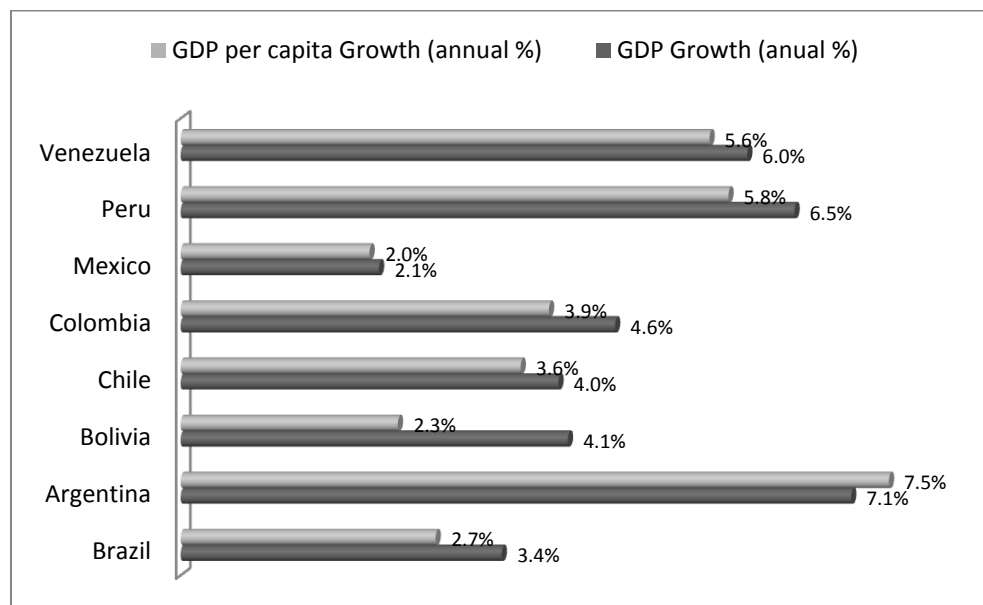
“The medium term macro outlook points to an annual GDP growth range of 4% to 4.5%. In the short term, after a slowdown in economic activity in response to the initial tightening of monetary policy and worsening external conditions, growth could be further depressed by a further reduction in external demand, lower foreign investment flows, tighter international credit conditions and a deterioration of consumer and business confidence. In the medium term, growth is likely to be driven by strong domestic aggregate demand. Investment growth, in particular, will be spurred by the development of new offshore oil fields and the preparations for the 2014 World Cup and 2016 Olympics”.

In this unstable global environment Brazil faces the challenge of reaching a higher development level, which requires more innovative, integrated

and knowledge-intensive approaches. One of the key-challenges to be tackled is the increase of competitiveness through human capital improvements. The human capital formation demands initiatives related to worker training and development of entrepreneurial skills, through removal of bureaucratic barriers to the economic activity to boost productivity. According to Abel, Bernanke and Croushore (2011, p.231), “people with the ability to build a successful new business or to bring a new product to market play a key role in economic growth”.

Despite the consistent achievements in the macroeconomic management in recent years, Brazil still faces structural weaknesses in its real economy (Kingstone and Ponce, 2010, p.111), what explains the relative modest average GDP and GDP per capita growth in the period from 2003 to 2009, in comparison to other Latin American Countries, as seen in figure 2.

Figure 2 – Average growth of GDP - Brazil and America Latina – 2003/2009



Source: the author, based on data from Kingstone and Ponce (2010, pg.110)

The high levels of both tax burden and interest rates are some of the structural weaknesses which are endogenous to the model of capital accumulation and inflation-targeting strategy adopted in Brazil. In the Lula administration the tight fiscal policy was combined with a significant increase in the generation of revenues (Baer, 2008, p.154). In 2004, the tax burden in Brazil reached 36% of its GDP (a number that is the average of OECD⁵ countries), while other South American countries like Chile and Argentina had a tax/GDP ratio of around 18% in

⁵ Organisation for Economic Co-operation and Development (www.oecd.org.br), which includes many of the world’s most advanced countries but also emerging countries like Mexico, Chile and Turkey

that same year. In 2010, despite the occurrence of a slight reduction (33.6% of GDP), the tax burden in Brazil was still at a level close to the most developed countries, where this ratio is justified by the high level of effectiveness of the respective governments.

Beyond being excessively onerous, the tax system in Brazil is fragmented and complex. It has a significant negative effect on the competitiveness of the country. The contributions and levies on payroll imply a large burden on labor income with adverse effects on employment in the formal sector (Mourougane, 2011, p.16). Reform packages were introduced in Congress in 2003 and 2008 to simplify the system and unify state-level Value Added Tax rates (ICMS), but the initiatives have failed in securing support from state governments.

The real interest rate in Brazil is still one of the highest in the world and remains as one of the most effective monetary policies used in Brazil to control inflation. The criticism of some authors such as Baer (2008, p.156) is that the inflation-targeting framework imposes a dilemma, “since such targeting implies that all other policy goals (including social objectives) would be subordinate to the primary goal of achieving a certain level of inflation”. Not to mention the impact of high levels of interest rates in the economic growth, discouraging the productive investment and capital formation, notably in Brazil, where the time of transmission of a change in interest rates is shorter than in most G7 countries (Mourougane, 2011, p.30).

Nonetheless, in response to the disinflationary effect of the deterioration in the global economy, the Central Bank has been reducing its policy rate since July 2011. In January 2012 the annual basic interest rate was defined at a level of 10.5%, which still results in the major real interest rate in the world.

While the tax burden and interest rates are issues to be addressed by the macroeconomic authorities, other structural weaknesses which impact the real side of the economy still prevail. Kingstone and Ponce (2010, p.123) believe that macroeconomic stability has done little to address the gaps in competitiveness and to boost the dynamism in the economy.

Despite the fact that not all economists agree that more infrastructure investment is crucial to increase productivity, Abel , Bernanke and Croushore (2011, p.231) confirm that “some research findings suggest a significant link between productivity and the quality of a nation’s infrastructure – its highways, bridges, utilities, dams, airports, and other publicly owned capital”.

The World Bank (2011a, p.7) asserts that the infrastructure constraints in Brazil are the result of relatively low investment rates. Brazilian aggregate fixed capital accumulation averaged 16.7% of GDP during 2000-2009 while China, India and the Russian Federation had investment rates of respectively 39.1, 28.4% and 19.1% of GDP during the same period.

According to the World Bank, public investments in infrastructure have been falling over the past two decades as a share of GDP, with negative results on the competitiveness of Brazilian firms. Total public and private investments in electric power, land transportation, telecommunications, and water and sanitation fell from 5.1% of GDP in the early 1980s to 2.1% of GDP in 2001-06, while Chile increased its investments in those sectors from 3.4 to 5.2% of GDP in the same period.

To finance the country's investment needs, it is a common sense that an increase in domestic (and namely public) savings will be necessary. According to analysis from the OECD (Mourougane, 2011, p.14) the ageing of the population represents an additional risk that may lead to an imbalanced fiscal situation in the long term due to the expenses related to the social security system. The forecast is that it will be necessary to create fiscal space to support growth-enhancing and social development programs in the years to come.

According to analysis of the Inter-American Development Bank (IDB, 2009, p.14), some of the main constraints to economic growth in Brazil are the low rate of capital accumulation and the low domestic savings rate which lead to low levels of investment. The lack of investment in infrastructure and public goods are factors that could limit the sustainability of growth in the short term, according to the Bank.

Nevertheless, the Growth Acceleration Plan (PAC), implemented in 2007 by the government, represented a convergence of public investments in a total amount of R\$ 463.9 billion in the period from 2007 to 2010⁶ in roads, railroads, airports, ports, waterways, energy plants and social and urban infrastructure.

The PAC intends to increase Brazil's aggregate investment rate to 22% of GDP in 2014 and the World Bank believes that although external savings could help increase investment, domestic savings would result in a more sustainable long-term growth. There is room for improvement in this indicator, considering that

⁶ <http://www.planejamento.gov.br/noticia.asp?p=not&cod=2194&cat=264&sec=29>

Brazil's domestic saving rate averaged 16.2% of GDP in the period from 2000 to 2009 (basically private savings) while the other BRICs (China, India and the Russian Federation) had domestic savings of 30 to 47% of GDP in the same period.

On the realm of these macroeconomic challenges, President Dilma Roussef, who succeeded former President Lula and took office in 2011, has kept a strong commitment with fiscal adjustment, having put in place budget cuts in noninvestment spending, although still relying on revenue strength. A BRL 50 billion cut to the 2011 federal government Budget was put in place, corresponding to a reduction in spending by about 0.5 percentage point of GDP compared to 2010, but the government preserved the social programs and the PAC from pruning. The OECD (Mourougane, 2011, p.14) evaluates that these choices were appropriate, given the importance to increase spending on infrastructure, notably to projects with the highest pay-offs, and the power to boost potential growth in the medium term.

The Dilma Roussef administration has pledged its commitment with the modernization of public sector management to "do more with less". Following the initiatives adopted in 2011, the Government has also announced its intent to keep on limiting growth in current expenditures, leverage private savings, stimulate private investments and promote innovation. In this regard, it is important to mention the relevance of scientific and technical progress to stimulate the productivity growth. Aber, Bernanke and Croushore (2011, p.231) assert that the basic research is an important investment to society, and even further, that the applied and commercially oriented research should deserve government aid.

ECLAC (2011b, p.28) recently summarized the main aspects of an overall scenario of the economy in Latin American. This scenario fits Brazil in most of the topics which already have been or still need to be addressed:

(i) international reserve levels have been restored, so the expected current-account deficit could be financed without draining them;

(ii) public accounts have improved during the period 2010-2011, and (exceptfor some Caribbean countries) indebtedness is low and would enable several countries of the region to place debt in the domestic and external financial markets;

(iii) inflation has stopped rising and is expected to fall in 2012, both globally and in the region; several countries (especially those that had raised their benchmark rates) thus have some monetary policy space for countercyclical action;

(iv) the 2008 global financial crisis left the region a legacy of experience in coordinating countercyclical fiscal and monetary policies and measures for heading off a liquidity crisis in domestic financial markets; hence the countries not only have resources—they have recent, hands-on experience in countercyclical response to a global crisis, and

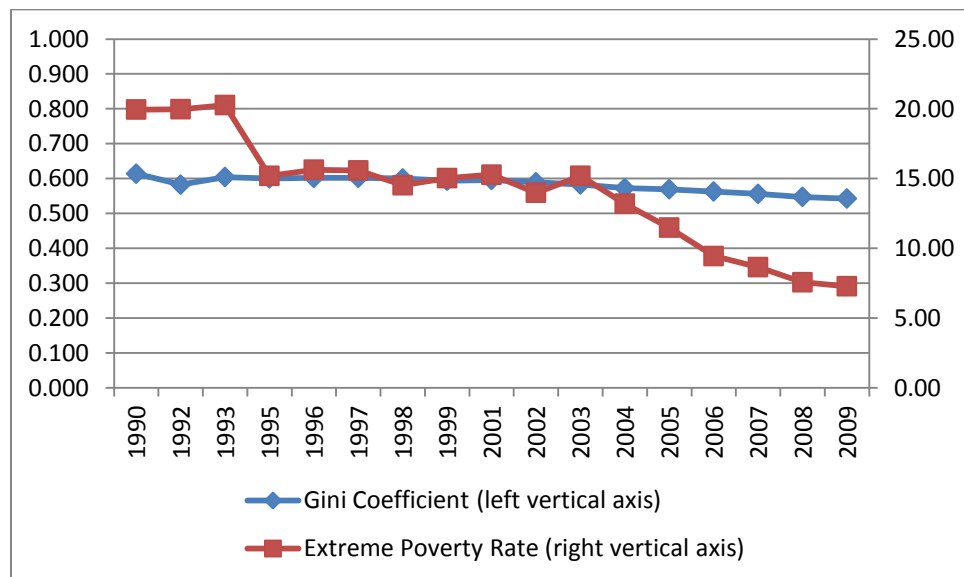
(v) The fiscal space available for countercyclical measures is tighter than in 2008, however, and both vulnerability and the capacity to deploy policies to address the impact of the global slowdown in growth differ from country to country.

1.1.2 Social aspects

1.1.2.1 The consolidation of social inclusion policies

Despite the adoption of sound macroeconomic policies in the last 20 years, Brazil has struggled, for the time being, with one of the highest levels of inequality in the world, as measured by the Gini Coefficient⁷. Figure 3 shows that starting in 2001 there is a slight trend of reduction in the inequality. The Gini went from 0.596 in 2001 to 0.519 in January 2012, its lowest historical level in Brazil (Neri, 2012)

Figure 3 – Brazil Gini Coefficient and Extreme Poverty Rate – 1990/2009



Source: Graphed by the author, based on data from <http://www.ipeadata.gov.br/>

Silva, Braga and Costa (2010, p.129) point out that this reduction in inequality results from improved social policy initiatives developed and

⁷ A Gini coefficient of zero expresses perfect equality where everyone has an exactly equal income, while a Gini coefficient of one expresses maximal inequality, where only one person has all the income

implemented both in the Cardoso and Lula administration, targeted to the poorest sector of the population. Among the initiatives, the referred authors mention:

- a) The implementation of a new retirement system for rural workers that didn't require previous contribution or official labor registration. This benefits a population historically deprived from material development;
- b) The Family Grant Program (Bolsa Familia), which pays a subsidy to families, under the condition that children are sent to school and have their basic medical care addressed and managed by the families themselves. This program was created in 2003 by the Lula administration as a result of the integration of other cash transfer programs that were developed in the Cardoso administration.

According to Baer (2008, p.163), the Family Grant program is supposed to strengthen the formation of human capital at the family level by the fulfillment of the conditions related to education and health. The program currently benefits more than 13 million families⁸. Hall (cited in Kingstone and Ponce, 2010, p.112) recognizes that

“Bolsa-Familia is a low-cost, high-visibility program that increases low-income families’ purchasing power but is less promising with respect to creating fundamental changes in Brazil’s social and economic structure”

Conversely, Figure 3 depicts the significant impact of the implemented social policies in the trend of the “Extreme Poverty Rate” in Brazil in the last two decades. On the right, the measures on the secondary vertical axis show that Brazil reduced the percentage of the population in extreme poverty⁹ from 20% in 1990 to around 7% in 2009. According to Neri (2012) in 2011 poverty in Brazil continued its downward trend at a rate of 7.9% a year, a rate three times faster than required by the United Nations millennium goal to halve poverty in 25 years¹⁰.

In a recent study from Fundação Getulio Vargas (FGV), coordinated by Neri (2012), it was concluded that in the period from 2010 to 2011 the inequality (measured by the Gini Coefficient) has been dropping at a rate of 2.13% a year. Inequality has been dropping now for 11 consecutive years in Brazil.

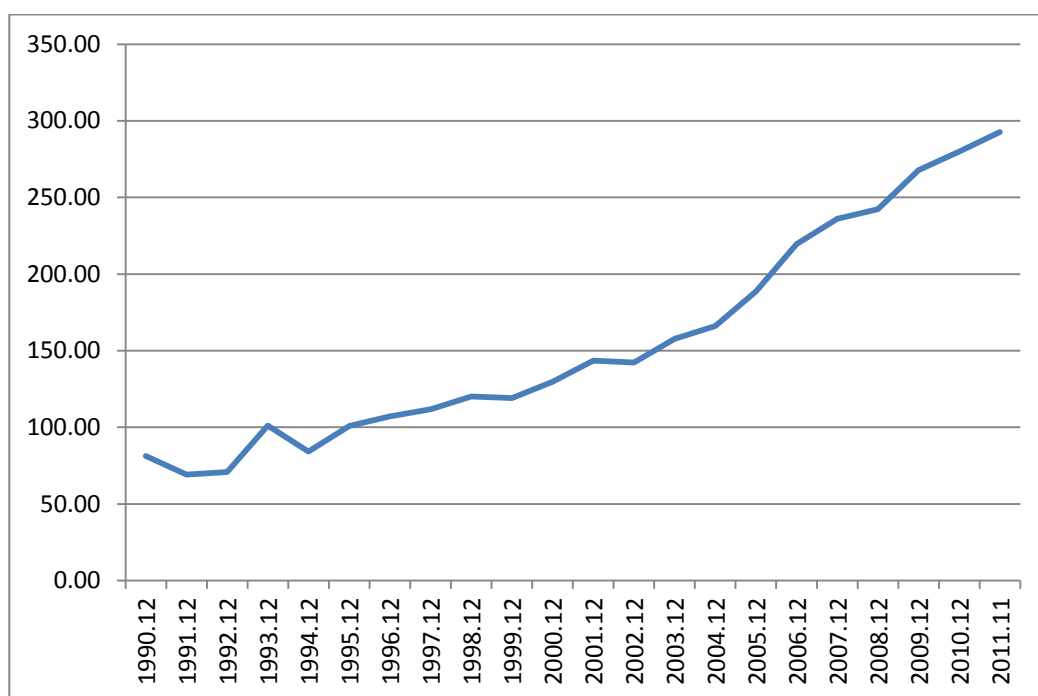
⁸ <http://www.mds.gov.br/bolsafamilia>

⁹ % of the population with a monthly per-capita income of less than BRL 70,00, according to <http://www.mds.gov.br/brasilsemmiseria>

¹⁰ <http://www.un.org/millenniumgoals/poverty.shtml>

Kingstone and Ponce (2010, p.110) attribute the reduction of the poverty rate to the economic growth, decreasing unemployment and rising minimum wages (see figure 4). These authors consider that although Bolsa Familia has played an important role in reducing extreme poverty rates in Brazil, it “may now be in a situation of diminishing returns” (p. 117).

Figure 4 – Brazil Minimum Wage in US\$ - Purchasing Power Parity¹¹ – 1990/2011



Source: Graphed by the author, based on data from <http://www.ipeadata.gov.br/>

The World Bank (2011a, pp.6-7) follows this understanding and calculates that economic growth explains about one half of the reduction in poverty recently observed in Brazil, while the remaining 50% results from the growth in labor income and the increased government transfers. According to the Bank, one of the largest potential sources of further poverty reduction is the increase in the productivity and salaries of workers who are at the bottom of the income distribution.

ECLAC (2011a, p.14) reinforces this same argument, stating that the decline in inequality in the Latin American countries is a consequence of a more equitable distribution of labor income per person employed while public cash-

¹¹ Represents, in each month, what was the price in US\$ for the same bundle of goods that could be acquired with a minimum wage in Brazil. The conversion is done by the 2005 World Bank rate of purchasing power parity (PPP) adjusted for inflation to the consumer in the United States and Brazil. Data published in <http://www.ipeadata.gov.br/>

transfers are a second source of income that has helped to redistribute income. Hence, reducing inequality cannot be left up to social protection and safety nets alone.

1.1.2.2 The social gaps to be addressed

The increase in labor income seems to be, according to the analysis provided by ECLAC and the World Bank, the key factor to be addressed in order to obtain higher levels of equality.

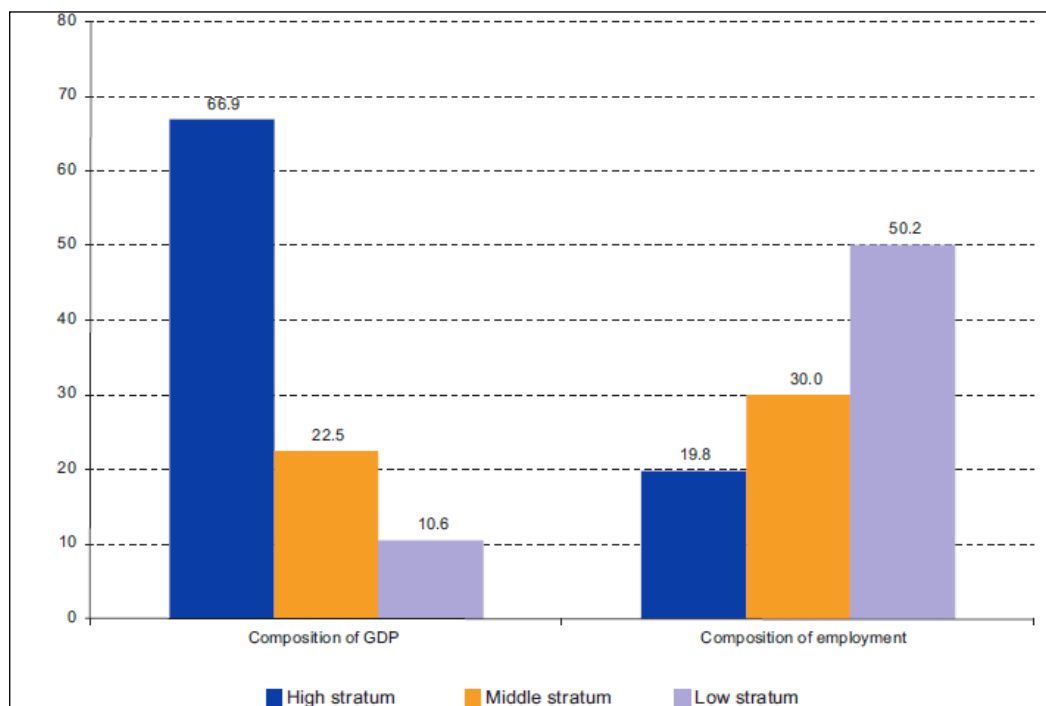
ECLAC (2011a, p.15) highlights that narrowing the gaps between more highly-skilled and less-skilled workers is one of the factors that contribute to the income distribution. In economic terms, this would mean to increase the marginal productivity of labor¹², as a result of improvement in technology and employment of highly-skilled workers. In this regard, Abel, Bernanke and Croushore (2011, p.74) teach that the labor demand by the firms in the economy is increased by the rise in productivity of labor, since firms are inclined to hire more (skilled) workers in what macroeconomists name as a beneficial supply shock.

Of course there is a close relation between the skills workers develop and supply to firms and the level of employment and income distribution. It is possible to conclude that the decrease in inequality depends strongly on the reduction of the structural unemployment in the economy. The structural unemployment occurs when unskilled or low-skilled workers who did not have adequate education, are only able to obtain jobs that do not last long, with low wages and little chance for training or advancement (Abel, Bernanke and Croushore, 2011, p.91).

The inequality in Latin American countries has its roots in a structural heterogeneity, where the firms that encompass large-scale export activities (high stratum) account for 67% of the GDP and employ around 20% of the workers, while the informal sector (low stratum) accounts for only around 11% of the GDP and employs 50% of the workers. In this categorization, the middle stratum includes small and medium-sized enterprises (SMEs), which account for 22% of the GDP and 30% of the total employment. The data depicted in figure 5 was generated by ECLAC (2011a, pp.25-26) and shows this so called heterogeneity on the basis of year 2009.

¹² Marginal product of labor is the additional output produced by each additional unit of labor (Abel, Bernanke and Croushore, 2011, p.65).

Figure 5 – Latin America: Structural Heterogeneity indicators around 2009



Source: Economic Commission for Latin America and the Caribbean (ECLAC, 2011b, p.10), on the basis of R. Infante, “América Latina en el ‘umbral del desarrollo’. Un ejercicio de convergencia productiva”, Working document, N° 14, Inclusive development project, Santiago, Chile, ECLAC, June 2011.

Inequality in income distribution is undoubtedly a consequence of structural heterogeneity which reveals a crucial division in the labor market: formal employment, which is close to the technology vanguard, demands a higher level of education, better labor conditions and is provided with a greater protection from labor institutions. On the other hand, the low-productivity employment is associated with informal employment, less income, a lower education level, instability, limited social security coverage and lack of labor contracts.

In the period from 2002 to 2008 the total factor productivity (which includes the productivity of labor) in Brazil grew at an annual rate of 1.1%, which is equivalent to the rate of output per worker growth in the U.S. during the previous three decades (Blanco et al cited in World Bank, 2011, p.8). The World Bank conclude that Brazil’s “aggregate efficiency of the economy would have to grow at an even faster rate to help reduce the country’s income gap with more advanced economies” (World Bank, 2011, p.8). Following the same conclusions of ECLAC, the World Bank refers to the need of improvements in quality of human capital to increase labor productivity and address inequality in a more effective way.

Brazil must additionally face the issue of inequality in regard to the regional particularities and inequalities. The North and Northeast regions, despite

their significant competitive economic advantages, still exhibit lower average incomes than the rest of the country. There is a clear link between the environment and poverty notably in these regions, where uncontrolled deforestation, soil erosion, and water pollution more severely deprive the poor of income sources (Thomas, 2006, p.24). Also the effects of urban degradation, such as inadequate water and sewerage, have a huger impact on health of poor households.

In the arena of environmental policies, Brazil faces the challenge to implement its low carbon development strategy. According to the World Bank (2011a, p.9), the country aims at contributing to global climate change mitigation by adopting a unilateral goal of reducing greenhouse emissions by 36 to 39% by 2020, under its National Policy for Climate Change. The country has one of the “cleanest” energy matrices in the world and continues to implement its national policy for prevention and control of deforestation in the Amazon and other biomes, such as the Cerrado and the Caatinga.

Despite its privileged geography, without occurrence of radical events like earthquakes and tornados, Brazil already struggles with negative effects that result from climate change.

“Negative effects include prolonged droughts, reduced potential for agriculture production, and increased evaporation from lakes, dams, and reservoirs. Moreover, long periods without rain will be punctuated by brief torrential downpours resulting in floods. Some of these effects are already evident in the increased recurrence of flooding and droughts that have caused significant social and economic impacts in Brazil. Dealing with increasingly frequent extreme weather events will require a systematic and coordinated approach to disaster risk management.” (World Bank, 2011, p.10)

In summary, the social aspects that have demanded the closer attention of the government result clearly of the economic gaps that have not been addressed effectively. As already discussed earlier in this paper, Brazil has historical problems with its level of human capital and the velocity of the improvement does not keep the pace required to fulfill the demand of skilled labor and guarantee the reduction of inequality. In the late 90’s Brazil subsidized the profitability of domestic and foreign capital through directed credit, tax breaks, and price policies. Thus, while physical capital was heavily supported, there was underinvestment in basic human capital (Thomas, 2006, p.51).

According to the Inter-American Development Bank (IDB, 2009, p. 4), the average number of years of schooling for the total population over 25 has been rising since 1981 from 4 to 7 years, but the level of education and skills of workers remains as the main obstacle to growth. The social programs like Bolsa Familia have had an important redistributive impact, but its effects on the intergenerational transmission of poverty depend, in the long term, on a consistent human capital formation.

1.2 The multilateralism and the role of international financial institutions

The Multilateral Financial Institutions were created in the context of the necessity to balance and to foster the global economy in the second half of the 20th century.

The International Bank for Reconstruction and Development (World Bank) was created in 1944 at the Bretton Woods Monetary and Financial Conference¹³. In that same summit the International Monetary Fund (IMF) was created. These Multilateral Institutions were supposed to develop a framework of economic and financial rules for the post-war era. In the case of the World Bank, the mandate gradually evolved since its creation, from the reconstruction of infrastructure (mainly of Europe and Japan), to a more comprehensive program, including worldwide poverty alleviation. Presently, the World Bank is managed by 187 member-countries.

In the 1970's the World Bank was intended to support investment projects through long-term loans to developing countries, that otherwise would not be funded by private finance. Elson (2011, p.43) mentions that the financial transactions from the World Bank were gradually given the status of "preferred creditor" by the recipient governments, allowing the Bank to provide credit at lower interest rates.

The Inter-American Development Bank was established in 1959 to attend 26 Latin American and Caribbean borrowing members, which have a majority ownership of the IDB. 22 other countries (the United States, Canada, Japan, Israel, the Republic of Korea, the People's Republic of China, and 16 European countries) are non-borrowing members that provide capital and have

¹³ Delegates from 44 allied nation gathered in Breton Woods, New Hampshire and established the International Monetary Fund (IMF) and the World Bank, "to provide services and functions for the benefit of the international community that no one individual nation would necessarily have an incentive to provide" (Elson, 2011 pg 40)

voting representation in the Bank's Board of Governors and Board of Executive Directors.

Boas and McNeill (2003, pp. 8-9) assert that Multilateral Institutions have historically had an "engineering" approach in promoting development, preferring to treat the underdevelopment as a technical issue rather than a more complex political process. They underscore that the Multilateral Institutions have concentrated their lending program in traditional sectors, while projects should include social and environmental components and "new cross cutting themes" such as governance, involuntary resettlement, and indigenous peoples.

Apart from this criticism, the referred authors consider the importance of Multilateral Institutions in offering some protection for weaker actors in the global arena. In this regard, multilateralism would be preferable to unilateralism, due to the doctrine of neutrality of the former, a key factor that enables the fulfillment the three major functions of Multilateral Institutions: project assistance, program lending and policy advice. (Boas and McNeill, 2003, p.12).

The participation of the Multilateral Financial Institutions is recognized to have a positive macroeconomic impact for the recipients of the loans. According to Mallick and Moore (2005, p.367), the loans from the World Bank have helped to boost infrastructural investment and raise the expected level of social and private investment returns. In addition, the World Bank structural adjustment loans (SAL) include a package of structural policy reforms, which a country accepts as a condition for receiving the loan.

Mallick and Moore (2005, p.373) state that the countries which are equipped with reasonably developed institutions and legal systems can benefit more effectively from the investments originated from the international lending. It is worthy to note the conclusions reported by Mallick and Moore (2005, p.379) as a result of their investigation of the link between per capita GDP growth and World Bank loans in 30 recipient countries. The mentioned authors conclude that the growth effects (considered in terms of output per capita as a measure of the long-run steady-state path of development) of external loans can be limited if the funds are mainly used for politically motivated public sector consumption, as opposed to increasing productive capital formation for economic activities. Thus, if the macroeconomic climate is accounted for, a direct positive effect of the external lending on growth rates may not hold.

In another study, Butkiewicz and Halit (2005, p.382) agree that it is more likely that the external funding attains the intended results when the

borrowing countries adopt sound policies and structural reforms based on the “Washington consensus” (namely transparency and good governance). On the other hand, the referred authors also conclude that the World Bank credits are most helpful in low income countries with poor democracy, where positive effects occur through increased public investment.

A side effect of the international aid is considered by Tavares (2003, p.104), when related to the level of corruption. The thesis presented is that foreign aid results in rules and conditions that limit the discretion of the recipient country’s officials, thus decreasing corruption.

Agostino (2008, p.1698), when analyzing the reasons that lead a country to seek the assistance of Multilateral Institutions, points out that the countries tend to approach the International Banks:

- a) When they have a balance of payment need of financial resources, as a consequence of a shrinking at the level of international reserves; or
- b) When there is a low investment level, measured as the gross fixed capital formation; in this case, the country has limited imports of capital and intermediate goods and fails in attracting investors, and is therefore more likely to seek the International Banks’ assistance.

Despite the difficulty to establish a rigid set of conditions that could guarantee the effectiveness of the assistance provided by the Multilateral Banks, it is possible to assert that the governance and macroeconomic aspects of the borrowing countries play a significant role in this regard. Hence, the foreign aid (through lending or grant projects) is more effective in countries with good governance, transparency, and sound macroeconomic policies. On the other hand, the external loans help to strengthen and sometimes establish the foundations of such a framework. The point to be discussed, then, is whether countries like Brazil and Chile have reached a different level of economic and institutional development, so that those countries can be addressed with the non-lending portfolio of the Multilateral Institutions.

To further develop this discussion, the global strategies of the World Bank and the IDB will be subject to a more detailed analysis.

1.2.1 The institutional strategies of the Inter-American Development Bank

The IDB Institutional Strategy¹⁴ was updated in 2010, in the same occasion in which the member countries provided its Ninth General Increase of Resources¹⁵. The following two overarching strategic objectives are stated by the Bank (IDB, 2010, p.7) in relation to the development in Latin America:

- a) Reduction of poverty and inequality. According to the Bank, the inequality in the realms of education, health services and housing prevents the economic and social development from happening in the necessary pace, affecting the access to good jobs and the economic opportunities;
- b) Sustainable growth. The concept of sustainability refers to the long-term improvement of the living standards in the Latin American countries, balanced with the environmental issues related to climate change and energy requirements for development. The Bank believes that broadening the economic base and fostering the regional integration beyond the traditional trade agenda are necessary steps to be taken.

Beyond these major and comprehensive objectives, the strategy of the IDB also focus on the following complementary strategic goals:

- a) To address the needs of the less developed and small countries, tackling the significant intra-regional development gaps. The Bank (IDB, 2010, p.7) reports that Bolivia, Guatemala, Guyana, Haiti, Honduras, Nicaragua and Paraguay have a per capita GDP that is a quarter of the regional Latin American average and a rate of population living in poverty that is twice as high as the average for the region.
- b) Development through the private sector, especially small and medium enterprises (SMEs). The private sector creates on average 90 percent of all the jobs in Latin America and can be an effective tool to speed up the region's growth.

¹⁴ Available at <http://www.iadb.org/en/about-us/strategies.6185.html> (accessed on February 18th, 2012)

¹⁵ Due to the increase in demand for IDB resources prior to and after the global economic crisis, together with the long-term development needs related to climate change, lagging productivity and social and economic inequality, the IDB's Board of Governors on July 21, 2010, agreed to the terms of the proposed increase of the Bank's Ordinary Capital by \$70 billion.

Apart from the lending activities, the IDB has a portfolio of non-financial “Knowledge and Capacity Building Products”. These products are addressed to increase the intellectual and institutional capital of regional member countries and private sector clients, through the following activities¹⁶:

- a) Advisory services including products derived from client-driven needs with a short-term scope.
- b) Policy and capacity development including forward-looking, client-driven products that require a longer deployment time.
- c) Outreach and dissemination including products that originate in the Bank and have a shorter-term scope that draw on knowledge that is readily available—or at least easily located.
- d) Research and development including forward-looking products, which are originated within the Bank and are aimed at deepening the Bank’s knowledge in new subjects that would help countries.

These activities must be aligned with each country’s strategy and are supposed to have their costs recovered through a fee-based services funding, imposing that the Bank effectively provide the supply of relevant products, aligned in favor of the member-countries (IDB, 2010, p.20).

1.2.2 The institutional strategies of the World Bank

The World Bank comprises two institutions: the International Bank for Reconstruction and Development (IBRD), focused on the poverty reduction, and the International Development Association (IDA), which addresses its actions towards the world’s poorest countries. The following strategic themes¹⁷ drive the Bank’s work, and are integrated by the same framework of the United Nation’s Millenium Development Goals:

- a) The poorest countries, especially in what concerns to hunger, malnutrition, climate change, communicable diseases (HIV/AIDS and malaria).
- b) Post-conflict and fragile states: according to the World Bank, 80 percent of the 20 poorest countries have suffered a major war in the

¹⁶ <http://www.iadb.org/en/topics/development-effectiveness/knowledge-and-capacity-building,1257.html>
(accessed on March 24, 2012)

¹⁷ <http://web.worldbank.org/WBSITE/EXTERNAL/EXTABOUTUS/0,,contentMDK:20103838~menuPK:1696997~pagePK:51123644~piPK:329829~theSitePK:29708.00.html> (accessed on February 17, 2012)

past 15 years and even with rapid progress on economic recovery, it can take a generation or more to return to prewar living standards.

- c) Middle-income countries, which still have a heavy concentration of poverty in specific regions or ethnic groups. For the Bank, these countries, despite of having access to financial markets, face constraints in mobilizing the funds they need to invest in infrastructure and essential services and need help to reform policies and institutions to improve the investment climate. In these cases, the Bank is addressing the specific needs of the countries with “tailored assistance” based on competitive financial products and knowledge and learning services.
- d) Global public goods, such as the environment, public health, international trade and financial infrastructure, acting in the “market failures” and reaching an integrated approach that individual countries’ policies will not tackle.
- e) The Arab world, which still remains poorly integrated into the global economy apart from the oil sector, with high unemployment and low economic participation by women, lack of economic diversity, weak public accountability, and conflict.
- f) Knowledge and learning, focused on an in-depth analysis of local challenges of poor and developing countries and gathering of practical experience that can be used as benchmarks for other countries. According to the bank, this strategy is executed through reports, data and analytical tools, conferences, the Internet, and the improvement of the learning and capacity-building programs.

In the realm of knowledge sharing, the Bank aims at offering support to developing countries through policy advice, research, training and technical assistance. The approach of this “knowledge sharing” and capacity development strategy is regularly provided under the projects financed by the Bank, mainly in the poor and developing countries. Among the criticisms related to the effectiveness of the World Bank operations, Elson (2011, pp.125-124) advocates that the Bank should devote more resources to the issues of program evaluation and impact assessments of social assistance initiatives.

It is evident that the countries around the world are in different stages of development, due to historical, geographical, social and economic reasons. To

more effectively address the assistance to each country, the following country categorization is used by the World Bank (Shepherd, 2010):

- a) Category 1 countries are eligible for grants and loans that are geared towards basic infrastructural development, and are available to countries that possess the lowest per capita income and the lowest credit rating.
- b) Category 2 countries are eligible for IDA (International Development Agency) loans, which are intended for countries with low per capita income that cannot borrow from IBRD because they do not meet World Bank standards for creditworthiness. These are interest-free loans and grants for improving living conditions and economic growth. This category can also comprise those countries that are eligible for 20-year loans.
- c) Category 3 countries are eligible for IBRD loans with a 17-year lending period.
- d) Category 4 countries are eligible for IBRD loans with a 15-year lending period (which translates into less money repaid to the Bank in interest than the 17- or 20-year periods).
- e) Category 5 countries are considered graduated from the IBRD and no longer in need of these resources.

Countries are not framed in one specific category regardless of changes in their social and economic situations. Thus, countries can move into the other categories if their situation either deteriorates or improves.

2 Brazil and Chile: a cross-country analysis

2.1 Economic management and social policies in Chile in the 2000's

After the redemocratization process, which took place after the dictatorship in the "Pinochet" era, Chile was subsequently administered, in the years 1990 and 2000, by a coalition of center-left parties (the "Concertación"), which implemented the main economic reforms in the country.

In the early 1990's the economic debate in Chile was no longer "whether market reforms were good or bad for the country, but rather what government could do to build on them while making the more marginal sectors of society enjoy the fruits of the neoliberal model" (Manzetti, 2009, p.245). From the beginning, the notion of preserving sound macroeconomic policies was integral to the redemocratization process in the country. According to Taylor (2006, p.121), Chile was a benchmark in terms of good governance and an example of how to put in practice the "Washington Consensus" prescriptions.

In the period from 1990 to 2000 former presidents Patricio Aylwin and Eduardo Frei ran their administrations through fiscal discipline, tight monetary control and controlled exchange rate. The government continued the process of privatization of state-owned companies (which had been initiated by the Pinochet regime) and created new instruments for investing domestic and foreign capital, such as concessionary and associational forms of public-private partnership. The interest rates were kept high to attract foreign capital inflows and mitigate inflation, which was kept at an average annual rate of 3.72% in the period from 1992 to 2001.

The World Bank (2002, pp.2-3) states that in the beginning of the 90's Chileans were convinced that growth and stability were fundamental for obtaining economic prosperity and reduction of poverty and inequality. Presidents Aylwin and Frei based their economic policies on the pillars of: macroeconomic stability, increase in productivity and efficiency on a basis of sustainable economic growth, international opening of the economy, and larger government expenditures in health, housing, education and social security.

The Chilean economy benefited from a large amount of inflows of foreign investment in the 90's, which were allocated among technological

upgrading in agro-export sectors and mainly in copper extraction (40% of world copper reserves are in Chile).

In the years 2000, the socialist presidents Ricardo Lagos (2000-2006) and Michele Bachelet (2006-2010) ran the country, still under the “Concertacion” coalition. In 2010 President Sebastian Pinera, the first right-wing politician to be elected president in decades, took office. Despite its leftist orientation, the Lagos and Bachelet governments maintained free market economic policies in Chile, protecting macroeconomic stability to generate economic growth through integration with world markets and conservative fiscal policies (Huber, Pribble and Stephens, 2010, p.82).

The Lagos government adopted a fiscal discipline characterized by the strict linking of the government budget to macroeconomic indicators and creation of a structural fiscal surplus (on a basis of 1% of the GDP) that provided the resources which were used by the government to run countercyclical measures in the troughs of the business cycles in the 2000’s.

In the field of monetary policy the Lagos administration strengthened the independence of the Central Bank. In regard to the international markets, the imports tariffs were lowered to a uniform tariff of 6% and free trade agreements were signed with the United States, European Union, and Japan. Taylor (2006, p.147) notices that Chilean economic expansion in the 2000’s was closely related to a rise in commodity prices (such as copper) and the interest of foreign capital to invest in these sectors.

Taylor (2006, p.148) also points out that China became and remains one of the most important destinations of Chilean exports, namely copper and copper derivatives. According to ECLAC (2011b, p.28), Exports to China and Japan accounted for around 30% of total Chilean exports in the period from 2007 to 2010.

Manzetti (2009, p.244) claims that Chile has been internationally perceived as a secure place to invest due to the increased transparency and institutional accountability that were put in place during the “Concertación” administrations. Thus, with clear rules and protection of property rights, the government power was balanced and accountable for its actions, while gaining the legitimacy essential for market reforms effectiveness and sustainability.

Under the Bachelet administration, the fiscal surplus policy had its importance demonstrated when the resources were used to fund a stimulus

countercyclical package that was used to minimize the consequences of the global economic crisis (Huber, Pribble and Stephens, 2010, p.84).

On the other hand, specialists commonly refer to the gaps that still remain unaddressed in the realm of economic development: the lack of technology-based industrial upgrading (Taylor, 2006, p.149), and the low risk appetite by capital owners (Huber, Pribble and Stephens, 2010, p.87) who lack enthusiasm in investing in high-technology manufacturing and training the labor force. In this regard and in order to prevent the Chilean economy to suffer from the so called “Dutch disease”¹⁸, the Ministry of Finance under the Bachelet administration proposed the use of the Social and Economic Stabilization fund (which is financed by the copper stabilization fund) for investment in education and technological investment.

Despite the fact that extreme and moderate poverty have been falling in Chile for the last 20 years, as a result of consistent economic growth and targeted social policies like the Chile Solidario Program (similar to the Brazilian “Bolsa Familia”), income inequality still remains high. According to the World Bank (2011b, p.5) in 2009 the average income of the richest 20 percent of Chileans was 12 times that of the poorest 20 percent, a very similar number to that registered in 1990.

In May 2010, the Republic of Chile deposited its instrument of ratification to the Convention on the Organization for Economic Cooperation and Development (OECD), becoming the first South American country to join this organization¹⁹. The ratification of the OECD Convention “raised the bar” for Chilean social and economic indicators, since every comparison is now made with the average measures of the “OECD countries”.

The OECD (2011, p.5) reports that Chile has not kept in the 2000’s the same speed of economic growth that was verified in the 90’s. The analysis of the World Bank (2011b, p.2) is that while the annual average growth of the country since 1985 has been 5.4% percent, in the period from 2000 to 2009, the economic annual growth averaged only 3.5%.

According to the OECD the slow growth of productivity explains the major part of the slowdown in economic growth in the last decade. The total factor

¹⁸ Decline of the manufacturing export sector caused by large inflows of foreign exchange (due to the discovery and export of natural resources), which overvalue the national currency. The term refers to the experience of the Netherlands after the discovery of a large natural gas field in 1959 (Huber, Pribble and Stephens, 2010, p.87)

¹⁹ http://www.oecd.org/document/58/0,3746,en_2649_201185_1889402_1_1_1_1,00.html

productivity (TFP) is a measure of the overall effectiveness with which capital and labor are used (Abel, Bernanke and Croushore, p.60). Increases in the TFP refer to improvements in production technology that allows the production inputs to be utilized more effectively.

The World Bank (2011b, pp.9-10) states that Chile is one of the most competitive countries in Latin America, but still lags the more advanced nations in areas such as innovation potential, availability of skilled workforce and dynamism of competitive markets.

In regards to public management, the opinion of the World Bank is that the delivery of public services is relatively good compared with other Latin American countries. The main challenges highlighted by the Bank refer to the areas of accountability of public institutions, efficiency of performance management systems, financial regulation and decentralization.

In November 2010, the Pinera administration launched a development agenda for the country ("Chile País Desarrollado"), which sets the goal of achieving a high-income developed country status by 2018 by following a higher level of long-term development path and eradication of extreme poverty by 2014. This agenda includes the strengthening of social policies and protection of environmental strategic areas, focusing on the following goals: i) achieving greater competitiveness, including the modernization of the state; ii) improving job creation and job quality; and iii) promoting investment (World Bank, 2011b, p.15).

2.2 Comparative analysis of indicators from Brazil and Chile

Despite their geographical, cultural and historical differences, Brazil and Chile have shared important similarities for the last two decades, namely in the economic and social realms. Both countries had a political transition from military dictatorships to democratic regimes in the late 80's, managed macroeconomic policies focused on the control of inflation and openness to international trade and social policies aimed at the reduction of inequality.

Of course the pace of each country's movements and the results obtained were somewhat different, but by the end of 2010 Brazil and Chile seemed to face a set of similar urgent challenges, namely the struggle against the persistent inequality and the urge to foster competitiveness and productivity in the private sector and modernization and accountability in public management.

The following data was collected from the World Development Indicators (WDI) which is the primary World Bank database for development data from officially-recognized international sources. Most indicators selected represent relative numbers, because of the difficulty of comparing, with a conclusive approach, the absolute numbers of Brazil and Chile. The different sizes of their economic and social variables make a direct comparison misleading.

Table 1 – Brazil and Chile – Economic Indicators in 2010

	Brazil	Chile
GDP per capita growth (annual %)	6.6	4.2
GDP growth (annual %)	7.5	5.2
Total reserves (% of total external debt)	83.2	32.2
Foreign direct investment, net inflows (% of GDP)	2.3	7.1
GDP per capita, PPP (constant 2005 international \$)	10,055.9	13,595.9
Ease of doing business index (1=most business-friendly regulations) ²⁰	120.0	41.0
Cost of business start-up procedures (% of GNI per capita) ²¹	7.3	6.8
Business extent of disclosure index (0=less disclosure to 10=more disclosure) ²²	6.0	8.0
Exports of goods and services (% of GDP)	11.2	38.7
Sum of exports and imports of goods and services (% of GDP)	23.3	70.6
Gross savings (% of GDP)	16.5	23.1
General government final consumption expenditure (% of GDP)	21.2	12.5
Household final consumption expenditure, etc. (% of GDP)	60.6	59.2

Source: World Development Indicators & Global Development Finance database

From the economic indicators displayed in Table 1, it is possible to verify that both countries have followed very similar paths in regards to macroeconomics. In 2010 the GDP and GDP per capita had significant growth, in comparison to the rest of the world (especially the developed world, in the same year). In 2011 the pace of the growth has not been maintained by Brazil, whose

²⁰ Ease of doing business ranks economies from 1 to 183, with first place being the best. A high ranking (a low numerical rank) means that the regulatory environment is conducive to business operation. The index averages the country's percentile rankings on 10 topics covered in the World Bank's Doing Business. The ranking on each topic is the simple average of the percentile rankings on its component indicators

²¹ Cost to register a business

²² Disclosure index measures the extent to which investors are protected through disclosure of ownership and financial information. The index ranges from 0 to 10, with higher values indicating more disclosure

GDP had a growth of 2.7%²³, while the Chilean GDP kept increasing at an annual rate of 6.2%²⁴. According to the International Monetary Fund (IMF), growth in emerging and developing economies slowed in 2011 more than was forecast, possibly due to the greater-than-expected effect of macroeconomic policy tightening.

In the Brazilian case, the lower growth (in comparison with Chile) can be explained by the monetary contraction applied by the government, due to the commitment to the inflation targeting policy. In 2011, the annual inflation rate measured by the growth of the prices to the final consumer reached 6.5% in Brazil and 4.4% in Chile²⁵. In 2010, the GDP per capita in Chile was 40% higher than that measured in Brazil. Despite this measure, inequality in both countries still remains as an important issue to be addressed.

On the expenditure approach of the GDP²⁶, the Brazilian economy is more dependent on the government expenditures, which account for more than 20% of the gross domestic product, as opposed to 12% in Chile. In both countries, the household consumption is accountable for 60% of the GDP.

While Brazil has a very comfortable position in the global economy in terms of liquidity, with a significant amount of international reserves in relation to the gross external debt, Chile has a sound business environment that fosters competitiveness and entrepreneurship, with more favorable indicators related to the costs to register a business and the easiness of doing business in the country.

Despite the high level of international reserves accumulated by Brazil, the Chilean economy is largely more open, which can be measured by the ratio of the sum of imports and exports over the GDP. This ratio reached 23.3% in Brazil and three times that percentage in Chile (70.6%) in 2010.

Some other indicators related to the economic environment, from the perspective of infrastructure, are depicted in Table 2.

²³ <http://www.ipeadata.gov.br>

²⁴ According to the World Economic Outlook by the International Monetary Fund (<http://www.imf.org/external/pubs/ft/weo/2012/update/01/index.htm>)

²⁵ Data from Brazil collected from IPEA (www.ipeadata.gov.br) and data from Chile collected from <http://es.global-rates.com/estadisticas-economicas/inflacion/indice-de-precios-al-consumo/ipc/chile.aspx>

²⁶ The Gross Domestic Product can be measured by the product approach (market value of final goods and services produced), the income approach (value of the income received – wages received by workers and profits received by owners of firms) and the expenditure approach (value of the amount spent by ultimate users of the output produced). In the expenditure approach, the Gross Domestic Product equals the summation of C (consumption by domestic households) + I (spending for new capital goods) + G (expenditure of government in acquiring goods and services) + NX (spending on final goods and services that are produced in the country and exported, minus the goods and services imported, which are already included in C, I and G) (Abel, Bernanke and Croushore, 2010, pp.23-25).

Table 2 – Brazil and Chile – Infrastructure Indicators

	Brazil	Chile	Year of the Indicator
Burden of customs procedure, WEF (1=extremely inefficient to 7=extremely efficient) ²⁷	3.3	5.7	2010
Liner shipping connectivity index (maximum value in 2004 = 100) ²⁸	31.7	22.1	2010
Quality of port infrastructure, WEF (1=extremely underdeveloped to 7=well developed and efficient by international standards) ²⁹	2.9	5.5	2010
ICT service exports (% of service exports, BoP) ³⁰	2.0	2.2	2010
ICT goods exports (% of total goods exports) ³¹	1.8	0.2	2009
High-technology exports (% of manufactured exports) ³²	11.2	5.5	2010
Fixed broadband Internet subscribers (per 100 people)	7.2	10.5	2010
Internet users (per 100 people)	40.7	45.0	2010
Mobile cellular subscriptions (per 100 people)	104.1	116.0	2010

Source: World Development Indicators & Global Development Finance database

From these indicators, it is possible to verify that Chile has a more qualified port infrastructure allied to a more efficient set of customs procedures. These are core issues that may explain the relevance of international trade to the Chilean Economy. On the other hand, Brazil has a higher score in the index that refers to the “shipping connectivity” as a whole. This indicator is composed of elements such as number of ships, their container-carrying capacity, maximum vessel size, number of services, and number of companies that deploy container

²⁷ Burden of Customs Procedure measures business executives' perceptions of their country's efficiency of customs procedures. The rating ranges from 1 to 7, with a higher score indicating greater efficiency. Data are from the World Economic Forum's Executive Opinion Survey, conducted for 30 years in collaboration with 150 partner institutes

²⁸ The Liner Shipping Connectivity Index captures how well countries are connected to global shipping networks. It is computed by the United Nations Conference on Trade and Development (UNCTAD) based on five components of the maritime transport sector: number of ships, their container-carrying capacity, maximum vessel size, number of services, and number of companies that deploy container ships in a country's ports

²⁹ The Quality of Port Infrastructure measures business executives' perception of their country's port facilities. Data are from the World Economic Forum's Executive Opinion Survey, conducted for 30 years in collaboration with 150 partner institutes

³⁰ Information and communication technology service exports include computer and communications services (telecommunications and postal and courier services) and information services (computer data and news-related service transactions).

³¹ Information and communication technology goods exports include telecommunications, audio and video, computer and related equipment; electronic components; and other information and communication technology goods. Software is excluded

³² High-technology exports are products with high R&D intensity, such as in aerospace, computers, pharmaceuticals, scientific instruments, and electrical machinery

ships in a country's ports. In this regard, despite the weak port infrastructure as well as bureaucracy and lack of efficiency in the customs procedures, Brazil has an enormous potential to “connect” to traders offshore and strengthen the relevance of international trade in its economy.

The exports in both countries are mostly based in commodities (copper in Chile, and oil, iron ore and soy in Brazil). The value-added products such as information and communication technology goods and services account for a very small part of the exports in both countries, but in Brazil the high technology exports have accounted for an average of 12% of the manufactured exports, compared to an average of 5% in Chile.

The population in Brazil and Chile is gradually more “connected” through the access to telecommunication services, such as mobile cellular phones and the internet (the number of broadband subscribers has been increasing gradually from 8% in 2008 to 10% of the population in 2010 in Chile and from 5% in 2008 to 7% of the population in 2010 in Brazil).

Table 3 reveals some aspects related to the social policy arena in Brazil and Chile. Both countries still struggle with a high level of inequality, revealed by the Gini Index, which is positioned far away from the perfect equality of 100 points. Brazil had in 2009 around 20% of its population living below the national poverty line. In 2003 this number was close to 36%. In 2003 this indicator for Chile was 18%, and was reduced to 15% in 2009. Brazil experienced a more radical reduction in this indicator, due to the policies already discussed in this paper, namely the conditional cash transfer programs such as Bolsa Familia and the recovery of real wages.

In regard to education policies, the numbers of Brazil and Chile reveal some nuances and differences, which have symmetry to what happens in the labor market of the two countries. It is reasonable to conclude that the literacy rate of the Chilean population (nearly 100%) results from, among other factors, a larger number of years in primary school (6, as opposed to a duration of 4 years in Brazil).

Table 3 – Brazil and Chile – Social Indicators

	Brazil	Chile	Year of the indicator
Primary education, duration (years)	4.0	6.0	2010
Literacy rate, adult total (% of people ages 15 and above)	90.0	98.6	2008
Public spending on education, total (% of GDP)	5.1	3.4	2007
Public spending on education, total (% of government expenditure)	16.1	18.2	2007
Expenditure per student, primary (% of GDP per capita)	17.3	11.9	2007
Expenditure per student, secondary (% of GDP per capita)	18.0	13.4	2007
Expenditure per student, tertiary (% of GDP per capita)	29.6	11.5	2007
Percentage of the population living below the national poverty line	21.4	15.1	2009
GINI index	54.7	52.1	2009
Labor force with primary education (% of total)	42.9	24.8	2006
Labor force with secondary education (% of total)	28.9	48.5	2006
Labor force with tertiary education (% of total)	8.6	25.2	2006
Unemployment with primary education (% of total unemployment)	51.6	17.0	2006
Unemployment with secondary education (% of total unemployment)	33.6	57.6	2006
Unemployment with tertiary education (% of total unemployment)	3.6	24.7	2006

Source: World Development Indicators & Global Development Finance database

Both countries spent in 2007 an average of 17% of the government expenditures on education, but in Brazil these expenditures are notably concentrated in tertiary education (college degree) through the government-funded federal universities. At the three levels (primary, secondary and tertiary education), the expenditures per student in Brazil are relatively higher (expressed in terms of a percentage of the GDP per capita). One may infer that Chile has a more efficient allocation of the expenditures in education than Brazil, but it is necessary to note the geographic disparities between the countries and the process of allocation of the resources. Brazil is a country with continental proportions, where the budgetary resources for education are mostly transferred to the local levels (states and municipalities), which are responsible for managing primary and secondary education.

The depiction of the unemployment rates shows a very clear difference between the two countries. While the unemployment in Brazil is concentrated in the population with only primary education (who account for 51.6% of total unemployment) in Chile, the unemployed are mainly among those with secondary and tertiary education (who account together for 82% of total unemployment). In this realm, it seems that Chile faces a different typology of unemployment, with a surplus in the supply and a shortage of demand for skilled workers. On the other hand, Brazil faces the inverse situation: a huge demand by firms and a shortage in the supply of skilled workers, which is, in theory a problem that can be addressed by education and training policies.

Beyond the economic and social issues which are being used in this chapter as comparative criteria of analysis between Brazil and Chile, it is also important to address the question of governance, which can be defined as the set of mechanisms and ways in which authority is exercised for the common good (Thomas, 2006, p.105). Poor governance is in fact a menace to the social and economic development, for it leads to arbitrary policy making, lack of accountability, weak legal systems, excessive centralization of power in the executive branch and lack of engagement of the civil society in public matters.

According to Manzetti (2009, p.20) in the late 1990's the World Bank and the IMF began to include governance clauses in the loan agreements, with emphasis on the fight against corruption. The conclusion of these Multilateral Institutions was that good governance was fundamental for the success of structural reform programs, especially in emerging markets.

Manzetti (2009, p.21) states that "better governance was positively associated with substantial improvements in poverty reduction and standards of living". Once the market reforms under the neo-liberal prescriptions alone did not address the question of corruption and institutional deficiencies, the issues of accountability, transparency, and the fight against corruption had to be gradually developed and institutionalized by the governments and, albeit belatedly, sponsored by the Multilateral Institutions.

Table 4 – Brazil and Chile – Governance Indicators - 2010

	Brasil	Chile	Latin American Average Percentile
Voice and Accountability	63.5	82.0	61.5
Political Stability	48.1	67.5	53.7
Government Effectiveness	56.9	83.7	58.4
Regulatory Quality	56.0	91.4	57.0
Rule of Law	55.5	87.7	52.6
Control of Corruption	59.8	90.9	58.8

Source: Kaufmann D., A. Kraay, and M. Mastruzzi (2010), *The Worldwide Governance Indicators: Methodology and Analytical Issues*

Table 4 depicts an overview on the issues related to governance in Brazil and Chile. The aggregate governance indicators were developed by researchers from the World Bank (Kaufmann, Kraay and Mastruzzi, 2010) and were constructed on a basis of six dimensions of governance. Each dimension is supported by several hundred individual underlying variables, which come up from a wide variety of existing data sources that capture the range of perceptions, in each country, concerning the dimensions which summarize the evaluation.

These indicators were built on a perception basis and the data sources include surveys of firms and households, and the subjective assessments of a variety of commercial business information providers, non-governmental organizations, and a number of multilateral organizations and other public sector bodies on the following dimensions:

1. **Voice and Accountability:** this dimension captures the perceptions of the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media.

2. **Political Stability and Absence of Violence/Terrorism:** captures perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including politically motivated violence and terrorism.

3. **Government Effectiveness:** captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies.

4. Regulatory Quality: this dimension captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development.

5. Rule of Law: captures perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence.

6. Control of Corruption: this dimension captures the perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests.

Despite the fact that there are possible biases concerning the referred "governance indicators", due to the different perceptions and ideological orientation of the respondents, the framework derived from the consolidation of such indicators in 2010 for Brazil may be useful for the purpose of the comparative analysis aimed at in this paper. To allow a comparative approach, the indicators are depicted in table 4 in its percentile form for Brazil and Chile. The percentile ranks from 0 (lowest) to 100 (highest) among all countries worldwide. The Latin American average percentile is placed in the last column, and provides an extra comparative analysis of the positioning of each country in relation to the average of Latin American countries.

Chile is ahead of Brazil and the Latin American average in all six dimensions. The best Brazilian scores are those related to the dimensions "voice and accountability" and "control of corruption" (in which Brazil's position is higher than the Latin American average) while in the issue of "political stability" the country has its worst score.

It is a fact that both countries had a democratic transition from military dictatorships, but Chile found its institutional equilibrium in the 90's more effectively, through the political framework known as the "Concertación". In the same period, Brazil went through the impeachment of President Collor, and a series of scandals of corruption involving all the levels and branches of government took place.

In the 2000's Brazil attained important milestones related to the control of corruption, namely the creation of the Office of the Comptroller General (CGU), the federal agency within the Executive Branch, in charge of assisting the President of the Republic in matters related to transparency, internal control

activities, public audits, corrective and disciplinary measures, and corruption prevention and combat. CGU is also in charge of technically supervising all the internal audit units within the indirect public administration, providing normative guidance as required. The joint activities of CGU, the Federal Police Department and the Federal Public Prosecutor Office resulted in the dismantling of a series of cases of corruption and collusion in the last decade. Brazil also put in place, through the CGU, the Transparency Portal³³, with real time disclosure of all the financial transactions made by the Federal government.

Despite the referred initiatives, there is room for improvement, especially in regards to the deep rooted corruption in the political process, which is one of the most important restrictions to Brazil's development. Hence, the adoption of effective punishment against wrongdoing and pursuit of political reforms are core aspects to put Brazil on track for lasting progress (Thomas, 2006, p.107).

Therefore, in regard to the governance indicators it is possible that the perceptions, especially in Brazil, may be more strongly biased by the awareness of press, civil society and population in general of the occurrence of cases of corruption, which does not necessarily mean that it has increased overtime.

³³ <http://www.portaltransparencia.gov.br/>

3 The approaches of Multilateral Financial Institutions in Brazil and Chile

This chapter aims at analyzing the strategies of the World Bank and the Inter-American Development Bank (IDB) for Brazil and Chile. Such strategies are joint formulations of the Multilateral Institutions together with the respective governments and normally cover a period of 4 years.

In the case of the IDB, the document entitled “Country Strategy” and its content determines how each country’s priorities coincide with the Bank’s development strategies for the region. Each “Country Strategy” includes an overview of the country’s current social and economic situation, focusing in a depiction of areas such as rural and urban development, health, education, government modernization, transportation, trade, and the environment, among others.

The World Bank periodically produces, with the participation of respective governments and civil society, the “Country Partnership Strategy” (CPS), aimed at reducing poverty and promoting economic development. The CPS describes how the Bank will support the country’s development program during a certain period. The CPS is designed to the local conditions in the country and designates funding targets for projects, studies, and other actions that can be targeted by the Bank to each specific country.

3.1 The Multilateral Institutions’ “Country Strategies” for Brazil

3.1.1 World Bank Strategies for Brazil

Before discussing in detail the current Country Strategy prepared by the World Bank for Brazil for the period from 2012 to 2015, it is useful to highlight some of the main points of the two latest strategies, prepared for the Fiscal Years 2003-2007 and 2008-2011.

The Country Strategy for the period from 2003 to 2007 was built under a certain level of uncertainty concerning the maintenance of Brazil’s macroeconomic fundamentals under the Lula administration. The report 27043-BR was finished in November 2003 and stated the importance to maintain economic stability with growth, equity, and sustainability, with simultaneous actions on the economic and

social fronts. The Bank assessed that it would be necessary to gradually integrate the subnational levels in the development of the solutions for the country development. The first strategy prepared in the early 2000's was characterized by an emphasis on inclusive and sustainable growth (reinforced by the commitment to the Northeast and the North, areas with higher levels of poverty), quality of public expenditures, and governance (themes in the public agenda that were replacing the primary focus on the fiscal balance). The instruments prioritized by the World Bank for the period from 2003 to 2007 were:

- a) **Policy-based programmatic lending** at the federal level, complemented by technical assistance loans to support the policy framework in the thematic areas of the Country Strategy. These lending operations aimed at consolidating reforms had already been enacted, increasing the country's commitment to the reforms and the leading role of the government. The loans would be broad in scope (for example, covering fiscal reforms ranging from macrofiscal balance and structural reforms to public expenditure and public sector management issues), allowing more flexibility in its use.
- b) **Sectorwide approaches (SWAPs)** as an investment lending platform (in areas such as social assistance, youth employment, and housing), aimed at the mitigation of the operational impacts of fiscal austerity. In the SWAP operations the commitment, impact, and flexibility are increased, considering that the Bank resources are pooled with government funds and disbursed from the same account, under the same fiduciary rules applied to the national resources, which opens the possibility of tying financing to a robust results framework.
- c) **Integrated approach in support of multisectoral, rural and urban development strategies at the subnational level**, respecting the constraints required by fiscal adjustment, but merging the existing cooperation with state governments into integrated state strategies with an emphasis on municipal governments as key partners. The Bank reinforced its strategy to selectively lend to creditworthy states, using traditional investment lending and SWAPs. State strategies would include policy reviews, public expenditure and other economic analysis, and fiduciary reviews and capacity building.

d) **Continued strong program in analytic and advisory activities**

(AAA) for a catalytic role in reform and program design, while focusing on a more effective exchange of lessons and on the development of knowledge networks. The Bank, in the early 2000's, considered that the AAA program had been successfully implemented in Brazil, including comprehensive reports on key economic and sectoral issues, often developed in partnership with local research institutions, which helped to build consensus on policy and program design. The 2003-2007 strategy defined that a comprehensive Public Expenditure Review would be subject to an AAA initiative, in collaboration with IPEA (Instituto de Pesquisas Econômicas Aplicadas) and other partners.

The Report 62477-BR (May, 2008) defined the Country strategy for Brazil relatively to the Fiscal Years 2008-2011, keeping untouched the thematic approach related to the pillars of equity, sustainability and competitiveness, on a basis of sound macroeconomic fundamentals and good governance in public management. For this period, some aspects oriented the Bank's approach: a) the fiscal consolidation and reduction of indebtedness at the state level had contributed to a stronger macroeconomic situation, due to the implementation of the Fiscal Accountability Act, in conjunction with a prudent fiscal stance on the part of states and municipalities but; b) economic growth had been slow and there was a persistence of flaws in dealing with deforestation and other major environmental challenges and; c) the lending was still concentrated at the federal level, despite the explicit guideline in the previous strategy. Only in the last two years of the Country Strategy for the period from 2003 to 2007, the Bank's lending to states started to address more complex development issues such as the quality of public sector management using highly-innovative, results-oriented instruments.

For the period from 2008 to 2011, the following guidelines provided the path for the use of instruments by the bank, to fulfill the strategy:

- a) Offering of **traditional lending** at the federal level and more flexible repayment terms to better manage the rollover risk in operations at the sub-national level, where there was a growing interest in using the flexibility of IBRD loans at a project and portfolio level.
- b) Both at the federal and subnational levels, offering of **guarantee products for credit enhancement to catalyze private sector**

investment or to help develop the state and municipality bond market.

- c) In this strategy, despite the consideration of the possibility to unbundle the Bank's knowledge and lending services, with the experimentation of the fee-for-service mechanism as a possible tool for some limited cases, the government decided that it liked the "bundled model", with more range and flexibility in the technical services components. Hence, the referred strategy stated that, due to consistent demand from Brazil, there would be greater **emphasis on Analytic and Advisory (AAA) work integrated with lending**, and addressed more at the "how" of policy implementation rather than on the "what". The intention asserted in the strategy was that the AAA engagements would require joint initiatives with IPEA, especially on highly sensitive and strategic issues such as hydropower, civil aviation and highspeed trains, as well as strengthening debt management at the State level.
- d) Nonetheless the preference of the government for "bundle" operations, where technical and advisory work are attached to lending, the Bank specified the intention to engage in **fee-for-service reimbursable technical assistance** in response to specific government requests as in the issues of Public Private Partnerships in Irrigation and Civil Aviation.

The report Nr. 63731-BR (September, 2011) contains the current World Bank Group Strategy for Brazil and was approved on November 1, 2011. This strategy will guide the Bank's overall program in the country for the fiscal years 2012-2015, in integration with the federal government Extreme Poverty Eradication Program, "Brasil sem Miséria". The main goal established in referred document is "for the Bank to contribute to Brazil's aim of faster, more inclusive and more environmentally sustainable growth, with macroeconomic stability".

The strategy is detailed in 4 strategic objectives that are sub-divided into 14 result areas. Tables 5 to 8 summarize each strategic objective, the respective result areas and specific objectives for each result area. The two last columns in each table present the number of projects that are in the lending pipeline for fiscal years 2012-2013, and are, in any of its components, connected to one or more of the specific result area. It is important to note that one single project can relate to more than one single result area. Hence, the summation of all the figures in

referred columns in tables 5 to 8 will not equal the total quantity of 24 projects of the Indicative Lending Program for FY12-13. There is, as expected, a clear concentration of projects addressed to the subnational level.

Table 5 – World Bank Country Partnership Strategy for Brazil – Fiscal Years 2012-2015 – Strategic Objective 1: Increase the efficiency of public and private investments

Result Areas	Specific Objectives related to this Result Area	FY 2012- 2013 Number of projects of the Indicative Lending Program for Fiscal Years 2012-2013, related to each result area	
		At the federal level	At the subnational level
1.1 Improved Fiscal and Public Sector Management	<ul style="list-style-type: none"> • Improvement of public investment management by development of capacity to screen, select and appraise projects; • Enhancement of tax enforcement, through the update of taxpayer records and property values. • Increase in the quality of personnel expenditures, through strong payroll management controls and strategic workforce planning, aimed at attracting and retaining skilled staff and modernizing career structures; • Promotion of a strategic approach to the government supply chain management, increasing value for money and transparency in purchases; • Improvement of the quality of internal controls systems, transparency and accountability; • Enhancement of fiscal consolidation, to guarantee that policy decisions achieve their objectives with efficiency and efficacy; • Development of debt sustainability analyses and debt management strategies; • Enhancement of participatory mechanisms to incorporate citizen and regional perspectives in the policy making process; • Enhancement of geographic equality and equity in the offering of justice services with transparency and accountability; • Adoption of modern performance management techniques in the planning, budgeting and policy cycle. 	2	14
1.2 Enhanced Private Sector Development Policies	<ul style="list-style-type: none"> • Enhancement of innovation, competitiveness, and productivity growth • Generation of analytical work on the drivers of productivity growth and the impact of selected Government programs, mainly at sub-national level; • Strengthening of institutional and regulatory frameworks for public-private partnerships, improving Government capacity to better design and monitor PPP; • Promotion of financial inclusion, through technical assistance to regulatory agencies and incorporation of financial inclusion in social protection programs; • Provision of technical assistance and advisory services to support policies that remove microeconomic barriers to firms' entry, competition and exit 	1	13

Source: elaboration of the author, based on information from World Bank, 2011a, pp.16-21

Table 6 – World Bank Country Partnership Strategy for Brazil – Fiscal Years 2012-2015 – Strategic Objective 2: Improve quality and expand provision of public services for low income households

Result Areas	Specific Objectives related to this Result Area	FY 2012- 2013 Number of projects of the Indicative Lending Program for Fiscal Years 2012-2013, related to each result area	
		At the federal level	At the subnational level
2.1 Consolidated and strengthened social protection system	<ul style="list-style-type: none"> • Generation of analytical work on poverty dynamics, to improve the design of poverty reduction programs; • Enhancement of the implementation, monitoring and evaluation of social programs (namely Bolsa Família) by subnational governments; • Improvement of the beneficiary identification system (Cadastro Único) and the governance of the program Bolsa Família; 	1	14
2.2 Improved quality of education for low income groups	<ul style="list-style-type: none"> • Strengthening of Early Childhood Education, through improvement of normative and oversight functions and support to large municipalities in the design, implementation and impact evaluation of programs targeted to low income households; • Improvement of teacher quality, repetition rates, age-grade distortions, and secondary education quality; • Production of analytical work focused on generating options for improving the quality and efficiency of the vocational and technical education system; 		
2.3 Improved access to health care for low income households	<ul style="list-style-type: none"> • Improvement of quality assurance mechanisms and access of vulnerable groups to the Family Health Program (PSF) and evaluation of the impact of basic health programs on health status; • Strengthening of the linkages between public health, primary health care and medium and high complexity health facilities; • Support to improvements in emergency care and integration to PSF by selected sub-national Governments; • Support to decentralized implementation, governance, and results-based management of the national HIV/AIDS and Sexually Transmitted Diseases (STD) Programs; • Expansion of health-oriented Public Private Partnerships designed to serve poor and middle-income groups. • Generation of strategic analytic work on broader health financing and health system reform issues; 		
2.4 Expanded affordable housing and improved living conditions for low-income and vulnerable groups	<ul style="list-style-type: none"> • Improvement of the effectiveness of housing subsidies, through technical assistance to the Federal Government. • Improvement of the functioning of housing and land markets through the development of more effective regulatory instruments by subnational governments • Support to higher coordination between policies in the areas of land use, housing, transport and disaster risk management, in partnership with subnational governments. • Increase in the sustainability of slum upgrading investments and crime and violence prevention initiatives; • Strengthening involuntary resettlement policies to ensure that urban development programs do not leave some community members worse off. 	-	4

Source: elaboration of the author, based on data from World Bank, 2011a, pp.16-18;21-26

Table 7 – World Bank Country Partnership Strategy for Brazil – Fiscal Years 2012-2015 – Strategic Objective 3: Promote regional economic development through strategic investments and policies

Result Areas	Specific Objectives related to this Result Area	FY 2012- 2013 Number of projects of the Indicative Lending Program for Fiscal Years 2012-2013, related to each result area	
		At the federal level	At the subnational level
3.1 Improved policy coordination at territorial level	<ul style="list-style-type: none"> • Support to State Governments to design and implement innovative sustainable rural development programs with a territorially integrated approach and improved natural resource management; • Support to State Governments to promote cluster development in urban areas. 	-	10
3.2 Expanded access to improved basic sanitation	<ul style="list-style-type: none"> • Strengthening of Government capacity to perform regulatory and policymaking functions, including investment planning and monitoring in coordination with sub-national Governments; • Development of an integrated approach to water resources management, supply and sanitation, involving actions in housing and disaster risk management; • Improvement in sustainable access to safe water among the poor, especially in underserved areas; • Support to municipalities in implementing and enforcing the Solid Waste Law; 	4	11
3.3 Improved transport infrastructure and management	<ul style="list-style-type: none"> • Improvement in the management in the transport sector, with a focus on integration, governance, overall efficiency and greener transport; • Development of priority multi-modal transport corridors, including highway, railway and waterway transportation; • Enhancements in urban transport governance, with a focus on integrating transport in the broader context of city planning for equitable and sustainable development. • Development of affordable and sustainable rural transport solutions. 		
3.4 Increased supply of clean and efficient energy services	<ul style="list-style-type: none"> • Strengthening of Brazil’s policy and regulatory framework for the energy sector, with a view to promote the supply of cost-effective and sustainable energy to meet the evolution of demand in the medium and long-term; • Support to research and development (R&D) on cutting edge technologies to transport efficiently and reliably large blocks of energy across continent-wide distances. • Support to energy diversification and to the development of new second generation biofuel feedstock such as wood fiber. • Increase in the energy efficiency by improvement of the operational, commercial, and financial performance of six distribution companies in the North and Northeast; 		

Source: elaboration of the author, based on data from World Bank, 2011a, pp.16-18;26-30

Table 8 – World Bank Country Partnership Strategy for Brazil – Fiscal Years 2012-2015 – Strategic Objective 4: Improve sustainable natural resource management and climate resilience

Result Areas	Specific Objectives related to this Result Area	FY 2012- 2013 Number of projects of the Indicative Lending Program for Fiscal Years 2012-2013, related to each result area	
		At the federal level	At the subnational level
4.1 Integrated Water Resources Management	<ul style="list-style-type: none"> • Strengthening of the institutional capacity for improving water resource planning and management at the Federal and sub-national levels, especially in the Northeast; • Support to the federal and state governments to better coordinate its various programs in the water sector; • Development of innovative long-term irrigation approaches on a sustainable basis in partnership with the private sector, focusing on the semi-arid areas of Brazil. 	2	11
4.2 Expanded sustainable agriculture	<ul style="list-style-type: none"> • Support to the adjustment of extension services and the leveraging of financing mechanisms to accelerate the shift to a low-carbon agriculture and livestock production; • Mapping of degraded areas across all Brazilian biomes and development of financial incentives to promote their rehabilitation; • Support to increased sustainability of agricultural production and forestry in the Cerrado; • Increase in the agricultural resilience to climate change, by generation of analytical work to inform policy making and support to the adoption of climate-smart practices and technologies. • Development of sustainable forest management through enhancement of the policy and regulatory framework. 	2	6
4.3 Improved environmental management, biodiversity conservation and climate change mitigation	<ul style="list-style-type: none"> • Strengthening and integration of the environmental management systems in the federal and sub-national governments, through the implementation of Rural Environmental Registries; • Improvement of the efficiency and effectiveness of environmental licensing and monitoring systems, including transparent and user-friendly tools to speed up the licensing approval process and social participation and control; • Development of Brazil's national system of protected areas; • Support to the use of the Ecological Economic Zoning (EEZ) in the context of rural development programs; • Implementation of Brazil's National Climate Change Plan; • Promotion of low carbon growth and climate change mitigation action plans at the city level 	2	11
4.4 More effective disaster risk management	<ul style="list-style-type: none"> • Support to the Federal government in building capacity at the sub-national level for outlining local strategies for reducing natural disaster risks; • Strengthening of the preparedness of civil defense systems to cope with natural disasters and to coordinate post disaster response; • Revamp of Brazil's forecasting and early warning system; • Support to the identification of risk areas and the building of local probabilistic risk modeling capacity. 	-	12

Source: elaboration of the author, based on data from World Bank, 2011a, pp.16-18; 30-34

From a thematic perspective, the current World Bank strategy for Brazil does not differ significantly from those established by the two latest documents. Nonetheless, an important approach to what the Bank calls “second-generation development problems” and the imperative involvement of subnational governments is worth mentioning (World Bank, 2011a, p.ii). Table 9 presents how the Country Development Goals for the strategies built for the years coinciding with the Lula administration evolved to those for the period from 2012 to 2015.

Table 9 – World Bank – Country Strategies for Brazil – Periods 2003-2007 / 2008-2011 / 2012-2015

Synthesis of Country Development Goals defined in the strategies for the periods 2003-2007 and 2008-2011	How the issues are being addressed in the result areas of the current strategy for the period 2012-2015	New highlights in the strategy for the period 2012-2015
Equitable Brazil: reduce extreme poverty, vulnerability and social exclusion through improvement of knowledge and skills and achievement of longer and healthier lives	2.1 Consolidated and strengthened social protection system 2.2 Improved quality of education for low income groups 2.3 Improved access to health care for low income households 2.4 Expanded affordable housing and improved living conditions for low-income and vulnerable groups	✓ Focus on the design of Public-Private Partnerships in the health sector
Sustainable Brazil: promote natural resource-based growth through sustainable use of resources, namely water, forests and biodiversity	4.1 Integrated Water Resources Management 4.2 Expanded sustainable agriculture 4.3 Improved environmental management, biodiversity conservation and climate change mitigation	✓ Focus on result area 4.4-More effective disaster risk management
Competitive Brazil: improve competitiveness, infrastructure and investment climate	3.3 Improved transport infrastructure and management 3.4 Increased supply of clean and efficient energy services	✓ Focus on the shaping of the governance of transports and energy sector ✓ Focus on the role of subnational governments in the issues related to regional development through result area 3.1-Improved policy coordination at territorial level
Macroeconomic foundations and public sector Management: strengthen fiscal sustainability within a framework of increased private sector development, a more efficient public sector management and improvement of governance	1.1 Improved Fiscal and Public Sector Management 1.2 Enhanced Private Sector Development Policies	✓ Focus on the enhancement of the policy cycle in public management: planning, budgeting, monitoring, control and evaluation

Source: elaboration of the author, based on data from World Bank (2003, 2008, 2011a)

From an operational perspective, the strategy for Fiscal Years 2012-2015 (World Bank, 2011, p.35) establishes the importance of balancing lending

and non-lending services. The strategy states that the Bank's main products to Brazil are technical advice and services, more than the volume of lending or the lower interest rates it charges. These services, according to the Country Strategy, are supposed to be delivered in partnership with local scholars and institutions, so that it would be possible to bring "the best of Brazil to the Bank and the best of the Bank to Brazil".

Consequently, the use of the instruments to fulfill the current strategy is supposed to subordinate to the following criteria:

- a) Flexibility: the use of different instruments (Analytic and Advisory work-AAA, lending, trust funds and partnership activities) is supposed to be adjusted to effectively respond to the country's evolving needs;
- b) Selectivity: the Bank will ever more disengage from areas where institutions and organizations in Brazil have sufficient knowledge and capacity and will concentrate on areas where the country can benefit most from the knowledge and experience accessible through the World Bank;
- c) Innovation: the World Bank will support innovative investments and policy reforms which can be replicated within Brazil and abroad;
- d) Leveraging: the Bank intends to foster the leverage of resources from other development partners, the government and the private sector.

The analysis of the World Bank Country Strategies since 2003 reveals a gradual importance of the non-lending services in the portfolio of instruments delivered by the Bank in Brazil over time. The Analytic and Advisory (AAA) works are the more tangible products of this kind of non-lending services. In the early 2000's Brazil preferred to bundle such services with the traditional lending operations. The current strategy, therefore, is characterized by the flexibility and the possibility of increase in the volume of non-lending services provided by the Bank in support of Brazilian policies.

The Bank has indicated that the non-lending services represent a possibility of engagement in innovation initiatives that are more focused on "how" to manage and implement policies rather than point out to Brazil "what" to do. In this regard, the Analytic and Advisory projects in Brazil derives from a process of knowledge creation, not just knowledge transfer (World Bank, 2011a, p.140). According to the Bank, this approach would be a consequence of the fertile ground for innovation in an upper middle-income country like Brazil, where AAA has taken place to foster innovation and help to remove the barriers that suffocate it.

From 2004 to 2011, the World Bank performed a total of 107 AAA projects under the respective Country Strategies for Brazil that were in place in those years. Table 10 presents the dimensions in which the analytical and advisory works were distributed in the mentioned period.

Table 10 – Analytic and Advisory works performed by the World Bank in Brazil (values in US\$ 1,000)

	2004	2005	2006	2007	2008	2009	2010	2011	Total value	Number of AAA projects
Competitiveness	598	785.9	0.9	1,777.8	992.2	1,864.7	356	227.3	6,602.8	31
Equity	124.1	408.7	348.5	687.4	243	431	443	1,849.5	4,535.2	27
Sustainability		109.9	204	232.5	946.5		3,358.7	576.2	5,427.8	20
Foundations	359.7	448.8	1,134.7	939.9	337.4	664.6	191.3	484.4	4,560.8	29
Total	1,081.8	1,753.3	1,688.1	3,637.6	2,519.1	2,960.3	4,349	3,137.4	21,126.6	107

Source: elaboration of the author, based on data from World Bank (2011a)

From 2012 to 2013, 40 more AAA projects will be under execution in Brazil, at a total expected cost of US\$ 6.4 million. The projects that are to be executed up to 2013 cover some of the critical themes about which the non-lending approach of the World Bank can be of significant importance for the Brazilian Government, both at the federal and the subnational level.

Some of the products that are already underway are titled “National Health Finance System”, “Implications of Oil and Gas Discoveries”, “Water Resources in Northeast Brazil” and “Agriculture Productivity and Competitiveness”. Between the AAA products that are planned for 2013, it is worth mentioning projects that address issues like competitiveness and international markets (“Macro-Micro Productivity Puzzle and International Trade” and “Trade in Commodities & 1st and 2nd Moments of Economic Growth”), climate change (“Impacts of Climate Change on Brazilian Agriculture”, “Disaster Risk Management in Brazil” and “Low Carbon Emission Economy in Agriculture”), new social challenges (“Managing Health Care Financing in Brazil”, “Improving the Sustainability Protection and Promotion of Vulnerable Ethnic Minority” and “Gender Study”), and modernization of public management (“Enhancement of Public Expenditure Quality”).

3.1.2 Inter-American Development Bank Strategies for Brazil

The Inter-American Development Bank Country Strategy for Brazil relative to the period between 2004 and 2007 is contained in the document GN-2327-1 and was updated in 2008 through document GN-2477, in order to cover the period from January 2009 to December 2010. A new strategy is still pending final approval both by the Brazilian government and the Bank and is supposed to cover the period from 2012 to 2014.

For the period between 2004 and 2010, the strategy of the IDB for Brazil was designed to address the strategic areas shown in table 11.

Table 11 – IDB Country Strategy with Brazil – 2004-2010

Strategic Areas	Objectives
Productivity and infrastructure	Support sustained per capita growth, through support to credit programs for small and medium-sized enterprises (SMEs) and small producers, competitiveness, and factor productivity, infrastructure while preserving the environment, and deepening use of public-private partnership models in new investments
Poverty, equity, and human capital formation	Support social programs with emphasis on income-distribution programs, as a short-term measure for poverty alleviation, and education and health programs as sustainable measures for enhancing equity and human capital formation
Living conditions and efficiency in cities	Improve living conditions in cities, supporting subnational governments to enhance equity in access to and the quality of public services for the poorest segments of that population and integrating actions for reducing poverty in urban areas, through improvements in habitability, efficiency, and environmental quality in cities
Modernization of the State and institutional strengthening	Strengthen the performance of public sector institutions at the three levels of government, shoring up fiscal federalism and oversight agencies, with emphasis on the subnational areas of government

Source: elaboration of the author, based on data from IDB (2009)

Besides the strategic areas, the overlapping issues of integration, environment and natural resources, and reducing regional gender and racial inequalities were considered as part of the Country Strategy.

The Bank (IDB, 2009, p.v), while assessing the referred strategy, recognizes that its role as a provider of funding to the Brazilian economy is not significant in comparison to the needs of the country, and evaluates that there is room to boast a more catalytic and knowledge-centric role of the Institution in Brazil.

Despite the fact that the strategy for the period from 2004 to 2007 was built in a perspective of focus on the federal government lending portfolio, more opportunities were created to develop relationships with the states and municipalities, in the context of the Fiscal Accountability Act (LRF). At the federal

level, the Growth Acceleration Program (PAC) had been created and executed with fiscal reserves to reduce the wide infrastructure gap, and counted on the involvement of the private sector and the states.

Due to the erratic execution of the lending program based on the Country Strategy, the IDB evaluation is that the nonfinancial products have not given an adequate response to the demand for innovative and sophisticated development solutions in Brazil. Hence, the Bank asserts that the non-financial products should be related to national programs, irrespective of whether they have been financed by the Bank or not, due to the capacity of the Bank to provide efficient access to information networks and knowledge sources.

In this realm of non-financial products the Bank (2009, p.iv) foresaw a trend related to assisting mainly the subnational governments in building capacity for analysis and public administration. The Bank received demands from the subnational governments, for example, related to technical cooperation projects on evaluation of educational quality, optimization of social spending, performance-based management and participation in renegotiation of the states' debt.

Among the conclusions of the self-evaluation provided by the Bank (IDB, 2009, p.viii), the following aspects reveal a set of trends which are expected to be covered in the new Country Strategy that the Bank and the Brazilian Government are about to approve:

- a) Incorporate indicators in the program that justify the effectiveness of the lending contracts;
- b) Concentrate the Bank's nonfinancial products on the areas where Brazil does not have advantages, knowledge leadership, or recognized experience, focusing the analytic work on how things are done and on the operational and managerial skills of those who do them;
- c) Strengthen monitoring of the new *modus operandi* for work with the municipalities and states, with or without sovereign guarantees, emphasizing consistency between strengthening the participation of subnational governments in public policy, deepening integrated financial intermediation, and equitable development of decentralized institutional capacities.

These recommendations are supposed to address the program of the IDB in Brazil in the next years, and reveal the complexity and non-linearity of the strategy required for a country like Brazil.

3.1.3 The focus of the program lending at the subnational level in Brazil

In recent years most of the Multilateral Banks' loans in Brazil have been targeted to the subnational level (States and Municipalities) rather than the Federal Government. Innovation and knowledge generation have been the central elements of the Banks' relationship with Brazil, with strong flows of knowledge transfers. However, the Banks recognize that there is more room for improvement and achievement of results at the subnational levels.

Brazil's public policies, notably in the social realm, are strongly decentralized, and the Federal Government depends on the performance of the states and municipalities to ensure that health, education and poverty reduction initiatives are put in place. Thomas (2006, p.134) asserts that for Brazil there may be much value in better integrating federal, state, and municipal agencies.

The presence of the Brazilian subnational governments (states and municipalities) in the global arena has been increasing significantly in the last two decades. This international insertion is not always driven by federal government sponsorship. As an example, in the case of Agenda 21, issued by the United Nations as a comprehensive blueprint of action to be taken globally, nationally and locally in regard to environment policies, Brazilian cities (governmental and non-governmental spheres) have adopted a set of actions without a clear interface or dialogue with the federal administration (Oliveira, 2011, p.132).

Requests from the subnational levels for external loans from Multilateral Financial Institutions are overseen and monitored at the federal level by the International Affairs Secretariat (SEAIN), the Brazilian Overseas Federal Commission (COFIEX) and the National Treasury Secretariat (STN).

The International Affairs Secretariat (SEAIN) is one of the branches of the Ministry of Planning, Budget and Management. The SEAIN coordinates the negotiation process for obtaining external funding with multilateral and bilateral credit agencies, monitors and evaluates the implementation of the projects and recommends adjustments to improve performance.

The Brazilian Overseas Finance Commission (COFIEX) is a deliberative and joint body composed by high level officials from the Ministry of Planning, Budget and Management; Ministry of Foreign Affairs; Ministry of Finance and the Brazilian Central Bank. The COFIEX provides the initial assessment of the general outline of the projects presented by the governments (at the national and subnational levels) that will be funded by external loans. It is the COFIEX's duty to

recommend the design and preparation of such projects based on: i) the compatibility with the priorities and policies of the Federal Government; ii) the fiscal targets of the public sector; iii) the technical aspects of the project and iv) the performance of the portfolio of ongoing projects managed by the applicant borrower (BRASIL, 2000).

The National Treasury Secretariat (STN) is a unit within the Ministry of Finance, and is responsible for examining the subnational governments' ability to pay and also their debt ceilings. These verifications are required, since the Union provides the warranty for external loans contracted by states and municipalities.

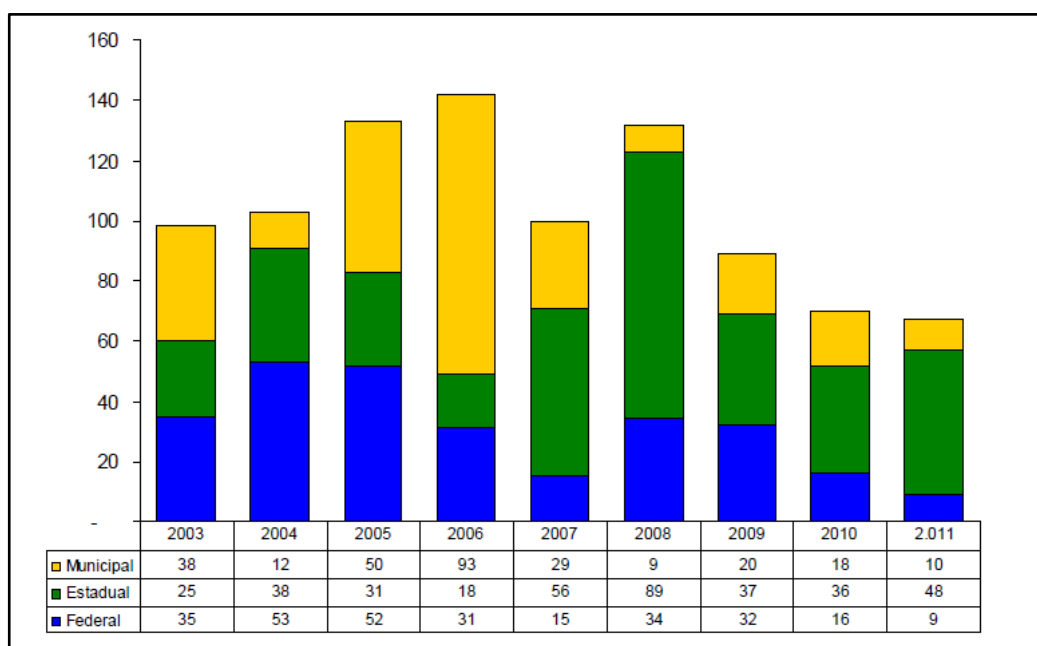
Regardless of their autonomy, the subnational levels are submitted to a set of procedures concerning the execution of projects financed by the Multilateral Financial Institutions. According to Oliveira (2011, p.144), the internationalization of the subnational political units implies an important political role for states and municipalities in forming a new development strategy for the country.

However, when states and municipalities are internationally integrated, there is a risk that the federal government will be unwittingly giving up its exclusivity in the formulation and implementation of Brazilian foreign policy. Nonetheless, the Brazilian framework, in the case of the relationship with Multilateral Institutions, provides a minimum guarantee of compliance with national priorities, mitigating this risk. And yet, if it were not for this framework being put in place, the probability of concurrent and costly initiatives would be even higher, since the subnational governments would manage their relationships with the Banks directly.

3.1.3.1 Overview on the lending program to states and municipalities

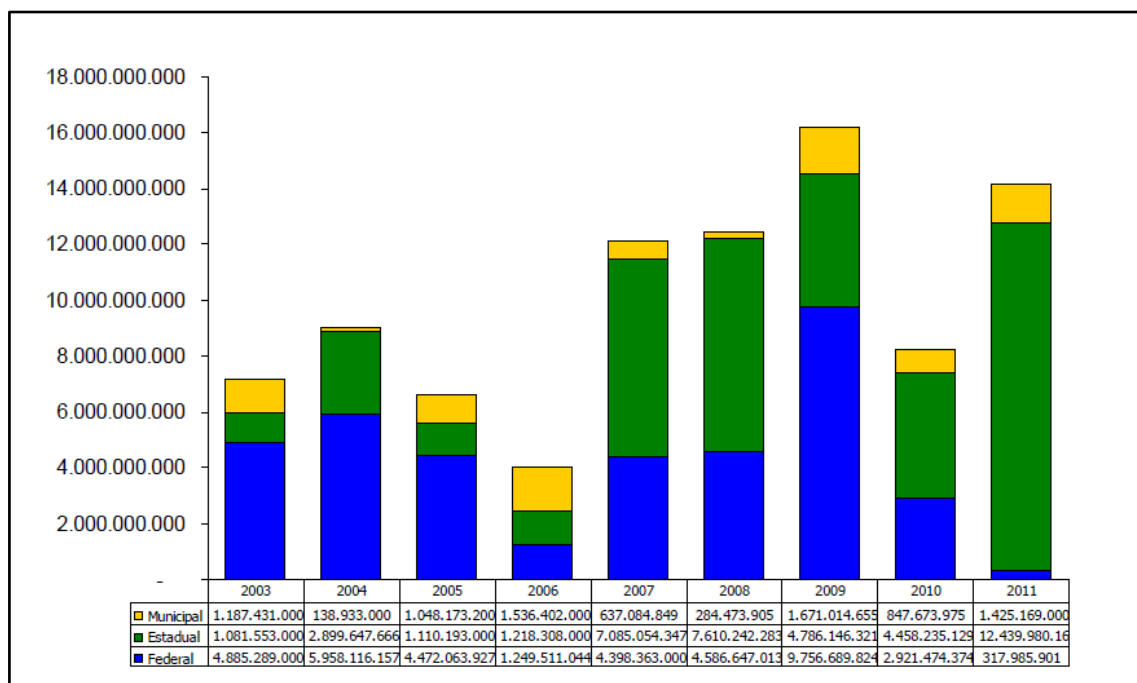
In the period from 2003 to 2011, the majority of requests (70%) for external loans presented to COFIEX (figure 6) came from the subnational governments. States presented 40% of the requests and municipalities presented 30%. The value of the projects (figure 7) presented by the states amounted to 47% of the total amount of the projects presented to the COFIEX in the same period, while the total value of those presented by municipalities amounted to 10%.

Figure 6 – Number of requests for external loans presented to COFIEX – 2003/2011



Source: International Affairs Secretariat, access at http://www.planejamento.gov.br/secretarias/upload/Arquivos/seain/downloads/2012/120127_apresentacao.pdf in Feb 11, 2012

Figure 7 – Total value (US\$) of requests for external loans presented to COFIEX – 2003/2011



Source: International Affairs Secretariat, access at http://www.planejamento.gov.br/secretarias/upload/Arquivos/seain/downloads/2012/120127_apresentacao.pdf in Feb 11^h, 2012

The figures indicate a trend that emerged in the 2000's: the proactive role of the subnational governments in designing projects with bilateral and Multilateral Financial Institutions to finance regional and local development.

This trend was in fact adopted by the Multilateral Institutions as a strategic approach. An assessment made by the Operations Evaluation Department of the World Bank in the early 2000's identified the necessity "to deal directly with Brazilian states and municipalities, given their responsibility for the provision of public services mandated by the 1988 Constitution" (World Bank Operations, Evaluation Dept. et al, 2004, p.5).

In the case of the World Bank it is important to mention that the focus on the state level had been initiated in the end of the 90's. In an effort to help sanitize the finances of Brazilian states, the Bank supported the privatization of banks and infrastructure companies owned by the states.

The position stated by the World Bank in regard to the focus on states and municipalities supported the transfer of knowledge and technical assistance to the subnational levels. This transfer occurred mostly during the design and execution of projects financed by the Bank. According to the World Bank Operations, Evaluation Department (2004, p.37), the loans provided the path for technical assistance to the states, which have a much weaker institutional capacity than the central government, and are responsible for basic public services.

In tables 12 and 13, the distribution of projects of the IDB and World Bank is plotted, according to status (phase) and level of government (federal, state and municipal levels) that is accountable for each project.

In the case of the IDB portfolio, 82% of the total number of projects (in all phases) accounting for 81% of the total portfolio value, is currently managed at the state or municipal level.

For the World Bank portfolio, 77% of the projects (in all phases), accounting for 79% of the total portfolio value, are run by subnational governments.

Table 12 – Distribution of IDB active projects in Brazil

Phase of the Operations	Value (US\$ 1,000)	% Value	Number of projects	% Nr of projects
In preparation	4,799,144.9	32,88%	66	31,13%
Federal	484,464.6	10,09%	14	21,21%
State	3,639,108.3	75,83%	36	54,55%
Municipal	675,572.0	14,08%	16	24,24%
Contract Negotiation	354,408.4	2,43%	12	5,66%
Federal	94,000.0	26,52%	3	25,00%
State	141,793.9	40,01%	6	50,00%
Municipal	118,614.5	33,47%	3	25,00%
Signature	2,454,670.0	16,82%	19	8,96%
Federal	93,600.0	3,81%	3	15,79%
State	2,162,330.0	88,09%	11	57,89%
Municipal	198,740.0	8,10%	5	26,32%
In Execution	6,987,735.5	47,87%	115	54,25%
Federal	2,044,314.0	29,26%	18	15,65%
State	3,947,756.1	56,50%	66	57,39%
Municipal	995,665.4	14,25%	31	26,96%
Total	14,595,958.8	100,00%	212	100,00%

Source: elaboration of the author, based on data from the International Affairs Secretariat

Table 13 – Distribution of World Bank active projects in Brazil

Phase of the Operations	Value (US\$ 1,000)	% Value	Number of projects	% Nr of projects
In preparation	5,499,162.5	32,29%	29	26,36%
Federal	720,666.5	13,11%	7	24,14%
State	4,778,496.0	86,89%	22	75,86%
Contract Negotiation	1,335,695.0	7,84%	7	6,36%
Federal	950,000.0	71,12%	3	42,86%
State	385,695.0	28,88%	4	57,14%
Signature	779,879.1	4,58%	4	3,64%
Federal	49,604.1	6,36%	1	25,00%
State	730,275.0	93,64%	3	75,00%
In Execution	9,414,066.2	55,28%	70	63,64%
Federal	1,784,551.4	18,96%	14	20,00%
State	6,368,967.7	67,65%	43	61,43%
Municipal	1,260,547.1	13,39%	13	18,57%
Total Geral	17,028,802.8	100,00%	110	100,00%

Source: elaboration of the author, based on data from the International Affairs Secretariat

It is noticeable that the upcoming portfolio (projects that are in the phases of “signature”, “contract negotiation” or “in preparation”) of the World Bank is concentrated at the state level, and the IDB has a prospection effort clearly addressed to the municipalities.

3.1.3.2 Risks associated with the increase of operations at the subnational level

One of the main concerns in regards to the focus of the Multilateral Institutions on the subnational level seems to be the same reason that justifies the approach of the banks with the states and municipalities: the lack of institutional capacity at other levels to manage and execute the projects financed with external loans. The IDB (IDB, 2009, p. 26) concluded in its evaluation of the Country Strategy for Brazil relative to the period from 2004 to 2010 that the projects that were supposed to benefit the municipalities had an heterogeneity and a scale that made it difficult to find public officials with the capacity to successfully implement the expected public policies.

The domestic execution of an external loan by the government requires technical and managerial competencies that do not necessarily differ from those that would be expected to exist in the staff of the governments. However, there are details concerning the financial and bidding specific rules that have to be observed and sometimes matched with the national legal framework.

Most subnational government levels in Brazil (mainly in the municipalities) face scarce human resources and the needed competencies to manage and execute the projects financed in a timely manner.

In local governments, namely states and municipalities, it is usual to observe a lack of administrative continuity due to the renewal of governors and mayors who take office every four years. The politicians at the local level are more inclined to establishing their own agenda and therefore manage sluggishly the projects and initiatives of a former administration. The IDB (2009, p.28) exemplifies this constraint in the case of the National Program to Support Modernization of Public Administration and Planning in the States and Federal District (PNAGE). In this program the start of execution was delayed due to the complexity of conditions placed on the states prior to the first disbursement. By the time of this disbursement, new governors had been elected who appointed political teams that had not participated in the genesis of the program. Due to this kind of instability, programs financed by Multilateral Institutions with states and municipalities may not comply with the schedule and planned outputs.

Another risk related to the trend of concentration of the Multilateral Institutions' loans with the subnational governments is related to the mandatory procedure for states and municipalities to request a sovereign guarantee from the Finance Ministry. The risks include the formalities of detailed analysis and strict

compliance with the LRF, which can result in unexpected delays (mainly from the Bank's standpoint) or even the denial of the sovereign guarantee.

The World Bank (2011a, p.37) recognizes other important operational risks related to the execution of the projects, when they involve multiple implementing agencies from different sectors, Ministries and/or Secretariats. To address these risks, the Bank intends to design appropriate implementation frameworks and provide training and other capacity building activities. Such initiatives might have a major importance in the case of state and local projects.

3.2 The Multilateral Institutions' "Country Strategies" for Chile

3.2.1 World Bank Strategies for Chile

The strategy of the World Bank for Chile relative to the Fiscal Years 2011-2016 is detailed in the report Nr. 57989-CL (January 2011) and focuses on a flexible program to be carried out predominantly through demand-driven joint studies related to the commitment of the Government of Chile to eradicate extreme poverty by 2014 and become a developed country by 2018. The result areas and main outcomes and outputs designed under the strategy for the period are detailed in table 14.

The so-called Joint Studies Program (JSP) originated from an agreement between Chile and the World Bank formalized in 2008. According to this agreement, the Government, through its National Budget Office, periodically prioritizes areas for specific studies under the JSP. The selected studies must concentrate on topics where the Bank has a comparative advantage in knowledge and reflect public policies at a broader level related to institutional development.

For the period from 2011 to 2016 the World Bank and the Government of Chile agreed to negotiate the Joint Study Program on a yearly basis. The Bank will fund US\$400,000 per fiscal year and the Government will contribute up to US\$ 800,000 to ensure that the demand for studies is fully met. The strategy considers the possibility that Fee-Based-Services can be used for additional studies requested by the Government of Chile (outside the Joint Study Program framework).

Table 14 – World Bank Country Partnership Strategy for Chile – Fiscal Years 2011-2016

Result Areas	Outcomes
Public Sector Modernization	<ul style="list-style-type: none"> • Improving performance and public financial management, including the debate on a new model of performance management incentives, including an assessment of management tools to improve institutional performance accountability mechanisms • Increasing transparency, including implementation of the Access to Information legislation and the strengthening of the oversight role of the Council for Transparency • Strengthening monitoring and evaluation systems, including the design of scorecard methodology for selected social programs. • Strengthening financial system and capital markets regulation, including discussions on pension funds incentive structure, SME financing, and bank and insurance regulation and supervision • Boosting the efficiency of resources in the public sector, including review of procurement management and information systems in the health sector
Job Creation and improving Equity	<ul style="list-style-type: none"> • Improving quality, financing, and equitable access to tertiary education services • Improving the social protection system for the poor, including the assessment and strengthening of the design and implementation of social protection policies and programs such as “Chile Solidario” and “Chile Crece Contigo” • Increasing the access of rural population to basic public services and markets, including effective and productive use of sustainable infrastructure services by rural communities
Promoting Sustainable investment	<ul style="list-style-type: none"> • Strengthening regulations and further development of productive infrastructure, including the improvement of regulatory and institutional framework for concessions, strengthening of public investment planning to facilitate foreign trade and improvement of foreign trade logistics and competitiveness • Support to private sector investment, including increased innovative renewable energy investment and support to Chilean companies operating in advanced fields or innovative business models. • Sustainable use of natural resources, including the impact assessment of economic incentives and subsidies on water resources sustainability and the development of a national incentive program for mainstreaming sustainable land management planning and practices in order to combat land degradation, conserve biodiversity of global importance and protect vital carbon assets

Source: elaboration of the author, based on data from World Bank (2011b, pp.29-31)

The Bank evaluates that the JSP has helped to better coordinate the knowledge and advisory services, which results in an increase in the amount of resources offered for these studies and in their efficiency, since there has been a reduction in the transaction costs related to carrying them out (World Bank, 2011b, pp.46). Concerning effectiveness, the Bank believes that the non-lending technical assistance has provided Chile with access to the knowledge and global experience that it requires to better manage the policies and institutional reforms.

The following studies are examples of issues that were covered by the Joint Study Program in 2009 and 2010 (World Bank, 2011b, pp.56-57):

- ✓ Comparative study on the international experience in agencies responsible for evaluating public policies;
- ✓ Evaluation of the Government’s “Programas de Mejoramiento de La Gestion en los Servicios Públicos” (PMG);

- ✓ Analysis of management of information technology in the reform of pension administration;
- ✓ Design of a strategy that combines positive incentives and enforcement mechanisms to ensure an adequate adherence of key productive sectors to environmental priorities and regulations;
- ✓ Review of the Public Technological Institutes attached to the Ministry of Agriculture;
- ✓ Definition of the medium-term strategy for higher education in Chile;
- ✓ International comparison of the institutional framework for early childhood education in Chile and in México, New Zealand and Sweden;
- ✓ Development of a monitoring and evaluation system that will support impact evaluation for the newly established preferential school subsidy introduced for students from socioeconomically disadvantaged backgrounds;
- ✓ Design of a new institutional structure for the educational sector that will address challenges such as improving quality and ensuring an efficient use of the increased funding for primary and secondary education, and in-depth analysis at the design and implementation of quality assurance systems in selected OECD systems;
- ✓ Survey of international experience with programs to increase access to computers;
- ✓ Diagnostic of the equality of opportunity conditions at the national and sub-national level in Chile;
- ✓ Gap analysis of the various medical specialties to ensure a proper supply of specialists in the public health system and analysis of implicit and explicit incentive in the health system, their coherence and consistency with the policy objectives, and their sustainability in light of the market conditions in the short and long term.

The World Bank assistance to Chile is outlined basically through knowledge activities put in place by means of the Joint Study Program and Fee-

Based-Services. Only a small portfolio of new lending operations is planned in the current strategy, in a total amount of US\$ 600 million for the period between 2011 and 2016.

3.2.2 Inter-American Development Bank Strategies for Chile

The Inter-American Development Bank (IDB) established its Country Strategy for Chile to take effect from November 2011 to June 2014. The IDB recognizes that Chile would not need multilateral financing to achieve its development goals, considering the level of its fiscal savings and the access of public sector to capital markets at competitive prices. Consequently, following the same trend already discussed in regard to the strategy outlined by the World Bank for the country, the demand on the part of the government is for an agenda based on knowledge products.

The strategic areas for cooperation were jointly defined by the IDB and the Government of Chile and can be viewed in the summary contained in table 15. While the strategy defined by the World Bank focus on the social theme of equity and the economic approach of sustainability, the strategy prepared by the IDB also covers the issues of innovation, security, transportation and trade development.

In August 2001 the IDB and the Government of Chile signed a Memorandum which establishes the terms and conditions for the fee-for-service Advisory Services Program, a tool only implemented by the Bank in Chile. For the period between 2011 and 2014, the Bank will focus its participation on supporting the above referred priority areas based on technical assistance under the “fee-for-service” program.

Additionally, there is an expectation that non-reimbursable technical-cooperation operations will focus on identifying loan operations, pilot programs, and evaluations that help to boost economic productivity and contribute to accelerate the convergence of the Country towards OECD standards.

Table 15 – IDB Country Strategy with Chile – 2011-2014

Strategic Areas	Outcomes
Labor markets: Equity and productivity	<ul style="list-style-type: none"> • Improve the quality and relevance of publicly funded training programs • Improve labor market regulatory policy
Climate change	<ul style="list-style-type: none"> • Expand knowledge about climate change adaptation and mitigation at the national, local, and sector levels • Increase institutional capacity to implement climate change adaptation and mitigation programs • Define strategy or public policy instruments to support development of nonconventional renewable energy for Chile • Reduce greenhouse gas emissions
Innovation, science and technology	<ul style="list-style-type: none"> • Foster business innovation through increase in total investment in Research and Development, in scope of promotion instruments and in labor productivity • Stiffen the protection of intellectual property • Disseminate information and communication technologies in small and medium enterprises
Public sector management	<ul style="list-style-type: none"> • Increase accountability and citizen participation • Improve service to users • Improve strategic planning systems at core of government and evidence-based decision-making • Improve the instruments for fostering productivity • Improve the business climate, through implementation of a new bankruptcy procedure
Citizen security	<ul style="list-style-type: none"> • Reduce crimes in households • Increase efficiency of the judicial system
Transportation and road safety	<ul style="list-style-type: none"> • Improve the public transit service in Santiago • Enhance road safety and reduce number of traffic accident deaths
Trade and integration	<ul style="list-style-type: none"> • Increase the range of exportable offshoring services • Diversify exports both by product and by destination • Reduce times and costs associated with export and import transactions and obtain greater efficiency in foreign trade management

Source: elaboration of the author, based on data from IDB (2011, pp.i-iv)

4 Conclusion: trends for Brazil in the relationship with Multilateral Financial Institutions

The role of Multilateral Financial Institutions in countries like Brazil and Chile is not supposed to be a “one-size-fits-all” solution. There are historical aspects that have shaped the Multilateral Banks’ operations since their creation. It is illustrative to mention, for instance, the analysis made by Elson (2011, p.118) concerning the shifts identified in the World Bank’s lending addressed especially to the developing countries.

In the post-World War II period the Bank had an important role in promoting public investment in infrastructure projects, due to “market-failure” in coordinating private investment. In the late 1960’s and 1970’s the focus shifted to agriculture in light of the challenge to alleviate poverty in the rural areas and emphasis on employment. As the debt crisis emerged in the 1980’s, the Bank’s policy emphasized macroeconomic adjustment according to the recipe prescribed by the Washington Consensus, and based on the idea that “government failures” were an obstacle to development. Throughout the 2000’s the World Bank’s policy lending has been focused on good governance and sound institutional framework as fundamentals both to attract private investments and to deliver basic social services. More recently, the promotion of human development has been the driver of World Bank policies.

Elson (2011, p.124) questions whether the Bank’s focus should be on conventional lending in countries which are among the largest developing economies of the world (such as Brazil, China, India and Mexico), or solely on poverty reduction programs. In his opinion, the Bank should refocus its presence in these countries, by: i) coordinating bilateral and other multilateral development assistance; ii) integrating its funding with local-based lending in global programs (disease-eradication, environmental protection); iii) shaping debate through research, advisory and training functions.

The effectiveness of the assistance of Multilateral Institutions has led to an academic and political debate over two distinct and opposite approaches of international institutions like the World Bank and the IDB (Elson, 2011 p.117):

- a) Top-down or “planners” approach, that can be exemplified by assistance addressed to poor countries, to support improvements in

health and education based on the United Nations Millennium Development Goals; in this case, the criticisms focus on the fact that recipient countries do not always assume a “leading role” to achieve an upper level of development;

- b) Bottom-up or “searchers” approach, which implies more limited support from the Bank and strong empowerment of local entrepreneurs in low-income countries, enabling them to improve their livelihoods.

The top-down approach is severely criticized by Boas and McNeill (2004, p.214) who believe that there is an enforcement mechanism in the relations of Multilateral Institutions, through nuanced procedures that discipline the “weak” (recipient of the aid) using the leverage of the “strong” (the donor). According to this standpoint, the development advice of institutions such as the World Bank would not necessarily be neutral, considering that “the production of knowledge in Multilateral Institutions is...produced within a frame of reference that embeds certain cognitive interests”.

4.1 Similarities and distinctions between Brazil and Chile

Brazil and Chile shared similar paths towards stabilizing their economies, managing social inclusion and preserving democratic institutions. Nonetheless, as previously discussed in this paper, and despite the flaws and difficulties that are still faced by its government, Chile has slightly overtaken Brazil in overall socio-economic development, which certainly was determinant to its acceptance as a country-member of the OECD.

The Multilateral Financial Institutions, namely those which are discussed in this paper (IDB and World Bank) have developed in the last decade a notably different approach to Chile compared to Brazil, based in non-lending technical assistance initiatives, covered in a fee-based services delivery.

In Brazil, the Multilateral Institutions have been gradually inclined to a similar orientation, due to the fiscal consolidation of the central government, which led to a significant reduction of the lending program at the federal level and a significant shift of the loans to the subnational governments.

From a thematic perspective, the latest strategies designed by the IDB and the World Bank for Brazil and Chile cover a somewhat similar set of core issues, although there are some distinct approaches, as can be seen in table 16.

Table 16 – Similarities and particularities of the strategies designed by the Multilateral Institutions for Brazil and Chile

Area	Similarities between strategies for Brazil and Chile	Aspects highlighted for Brazil	Aspects highlighted for Chile
Public Management and Modernization of the State	<ul style="list-style-type: none"> • Improvement of procurement systems and procedures • Improvement of performance management • Fiscal consolidation and improvement of tax enforcement 	<ul style="list-style-type: none"> • Focus on subnational governments 	<ul style="list-style-type: none"> • Improvement of Capital Markets regulation • Implementation of Access to Information Legislation
Social Policies	<ul style="list-style-type: none"> • Consolidation of social protection systems, notably the income distribution programs targeted at the poverty reduction 	<ul style="list-style-type: none"> • Support to subnational governments to improve quality of basic education and health programs addressed to low-income households • Support to effectiveness of housing subsidies 	<ul style="list-style-type: none"> • Equitable access to tertiary education • Access of rural population to basic public services and markets • Improvement of labor market • Citizen security
Infrastructure, sustainability and environmental issues	<ul style="list-style-type: none"> • Research and Development on the realm of clean, renewable and efficient energy • Sustainable management of natural resources, namely water • Climate change adaptation 	<ul style="list-style-type: none"> • Improvement of disaster-risk management procedures • Integration and governance of transport sector and development of multi-modal solutions • Use of Public-Private Partnerships 	<ul style="list-style-type: none"> • Support to innovative business models in the private sector • Dissemination of Information, Communication and Technology tools among the Small and Medium Enterprises • Efficiency, competitiveness and diversification of exports

Source: elaboration of the author

The strategies for Brazil have a strong focus on the subnational level and on basic education and health assistance to the poorest households, as a part of the major outcome related to the reduction of poverty. On the other hand, the strategies built for Chile touch on themes like tertiary education, fostering of innovation in the private sector and competitiveness of exports.

Both countries share the desired outcomes related to social protection systems, environmental issues and improvement and modernization of public management, notably in procurement procedures and performance management.

With regards to the instruments used by the Multilateral Institutions, the “country strategies” for Chile clearly and explicitly mention the Advisory Services Program (IDB) and the Joint Study Program (World Bank), both executed as a fee-based service, unattached from the traditional lending programs and taking

advantage of the experience and capability from the Banks to jointly produce and develop knowledge.

Although the “country strategies” for Brazil mention the non-lending products related to advisory services and knowledge building as a possibility, these approaches are in most cases still bundled to the lending operations, despite the broad range of possibilities of partnership that can be developed, in areas where the Multilateral Banks can add value to the country policies.

4.2 The importance of knowledge-intensive services in Brazil

Spotlights are on Brazil in the early 2010’s. The success of social inclusion programs like the “Bolsa Familia” has become a case study in the developing world. The efficient and quick recovery from the economic crisis, which still hurts Europe and the United States, has helped the country to overtake the United Kingdom in 2011 and become the world’s 6th largest economy³⁴. Millions of Brazilians have overcome the poverty threshold in recent years, due to the increase in real wages and the efficient operation of conditional cash transfers.

Last, but not least, the country will host the 2014 FIFA World Cup and the 2016 World Olympic Games, events that have the potential to attract investments and generate a lively economic environment in the upcoming years. The Multilateral Financial Institutions have an important role in helping the country to keep the pace of an inclusive, sustainable and steady development, in which monetary stability has already been embedded as a non-negotiable value.

Vinod Thomas (2006, pp.134-135), former director of the World Bank’s program in Brazil (from mid-2001 to mid-2005) asserts that the macroeconomic stability and growth remains essential, but policy makers should pay greater attention to social and environmental sustainability, with a focus on the quality of the development. Among the points that should be addressed in this “quality” agenda for Brazil, the former World Bank director mentions the importance of an efficient monitoring and evaluation of public spending and a greater focus on the quality of human development, including in education, health, and social assistance. Hence, prioritization of investments in human capital should not be neglected.

³⁴ <http://www.cebr.com/wp-content/uploads/Cebr-World-Economic-League-Table-press-release-26-December-2011.pdf>

To reach higher levels of productivity, Brazil requires more investments in infrastructure, reforms in the regulatory framework and the labor market. The requirements to guarantee productivity are in the realm of either “nontraditional” issues like knowledge economy, science and technology, arts and culture, and ecotourism, and also “nontraditional” instruments such as public–private partnerships and civil society participation.

The World Bank and the Inter-American Development Bank, jointly with the Brazilian government, have gradually adapted the framework of the respective Multilateral Institutions’ programs in Brazil. Following the conclusions from Thomas (2006, p.136), the current IDB and World Bank strategies for Brazil ultimately cover the shift in the agenda from a focus on quantity to a focus on quality, with value-added projects that take advantage on the Banks’ capacities.

Nonetheless, there is room for improvement. Following the trend already consolidated in Chile, the Brazilian government and the Multilateral Financial Institutions can now go the extra mile and progressively advance in the design of a more specific and qualified non-lending services portfolio that is more adequate for the complexities and possibilities of the country at its current level of maturity.

Domestically, Brazil was historically self-proclaimed as the “country of the future” in the second half of the 20th century. The future has arrived, and brought with it a complex, interconnected and unstable “brave new world”. With its more than 5.500 municipalities, 26 states, and almost 200 million inhabitants, Brazil has “continental” challenges related to tying together the maintenance of sustainable economic growth, social equity, competitiveness of the private sector, integration with the subnational levels, and governance of public policies. The country has, therefore, the potential to turn into a unique case study for the multilateral approach that goes beyond “Bretton Woods” and the “Washington Consensus” guidelines.

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