



FUNDAÇÃO GETULIO VARGAS

FGV/ EPGE - Escola Brasileira de Economia e Finanças

FGV EPGE / WORLD BANK SEMINAR

“The experience with fiscal adjustment in Latin America: lessons for Brazil”

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June 21, 2018

How Much Should Countries Adjust?

General Government

Net Debt/GDP: **0.54**

Effective Real Interest Rate – GDP Growth: **6.6**

Primary Surplus for a Constant DEBT/GDP Ratio ~: **3,6% of GDP (WB Report 4,9%)**

Present Projection: **-2,1% of GDP**

Required Adjustment ~: **5,7% of GDP**

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A time-varying fiscal reaction function for Brazil

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$$b_t = -s_t + \frac{(1+i_t)}{(1+\theta_t)} b_{t-1}$$

$$s_t = \rho b_{t-1} + \gamma X_t$$

$$b_t = \left(\frac{1+i}{1+\theta} - \rho \right) b_{t-1}$$

Long – Run Net Debt Sustainability

	01/2003 - 06/2016	01/2012 - 06/20126	01/2014 - 06/2016	2018 (Forecast)
Nominal Int. Rate Selic and (Effective Int. Rate*)	12.3 (15.7)	10.1 (17.9)	12.8 (20.4)	6.5 (12.1)
Nominal GDP Growth	10.8	8.2	6.7	5.5
Int. Rate – GDP Growth	1.5 (4.9)	1.9 (9.7)	6.1 (13.7)	1.0 (6.6)
Fiscal Reaction	5.7	4.7	4.3	4.3
Debt Sustainability:	Sustainable Whatever Int. Rates Are Considered	Selic Sustainable Effective Interest Rate - Not Sustainable	Not Sustainable Whatever the Int. Rate Considered	Selic Sustainable Effective Interest Rate - Not Sustainable

*The Effective Interest Rate is Defined as the Interest-Rate Bill Over the Net Debt Stock

Figure 5.1 - Estimated Fiscal Reaction Coefficient by the Three Methods

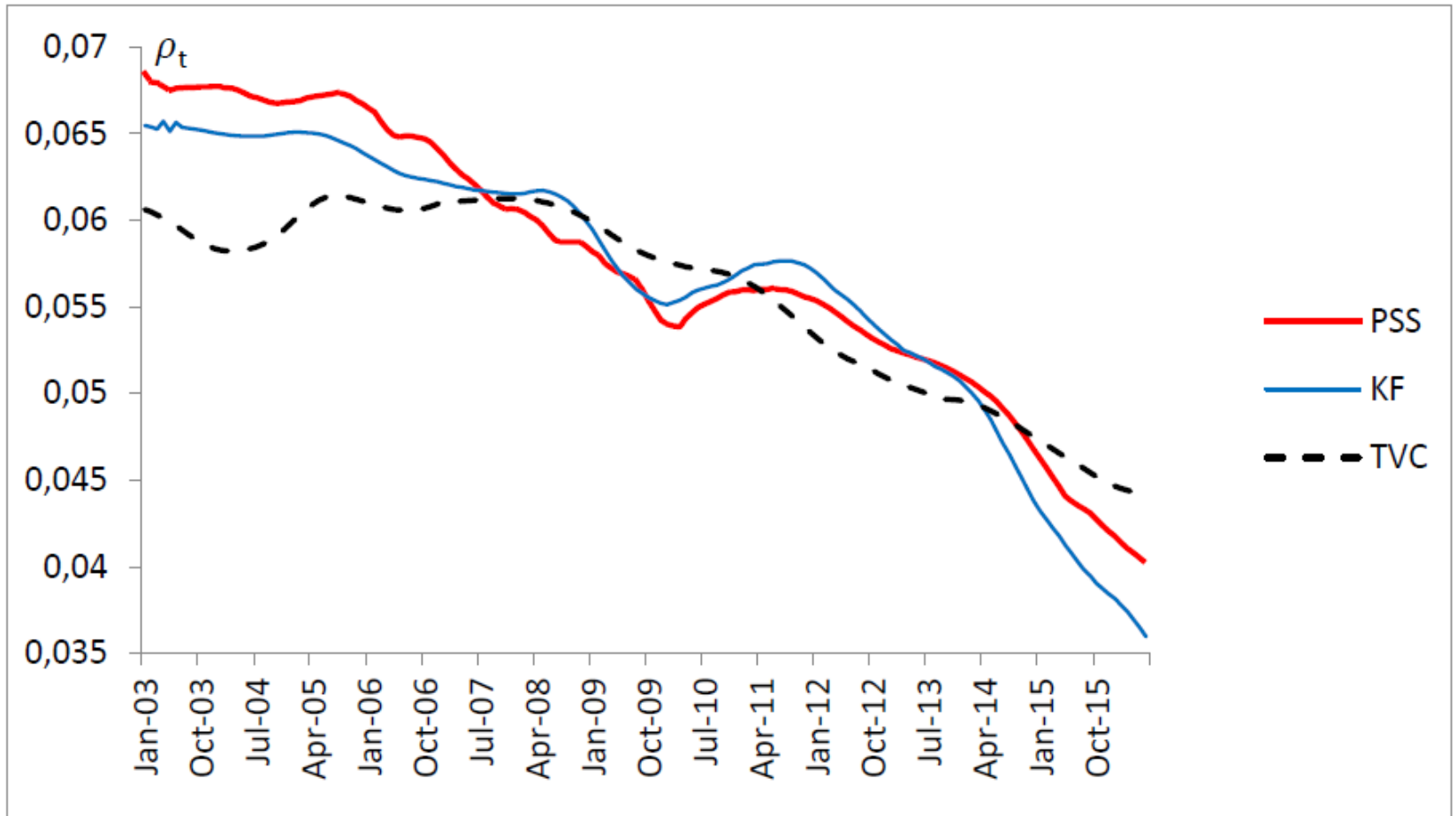
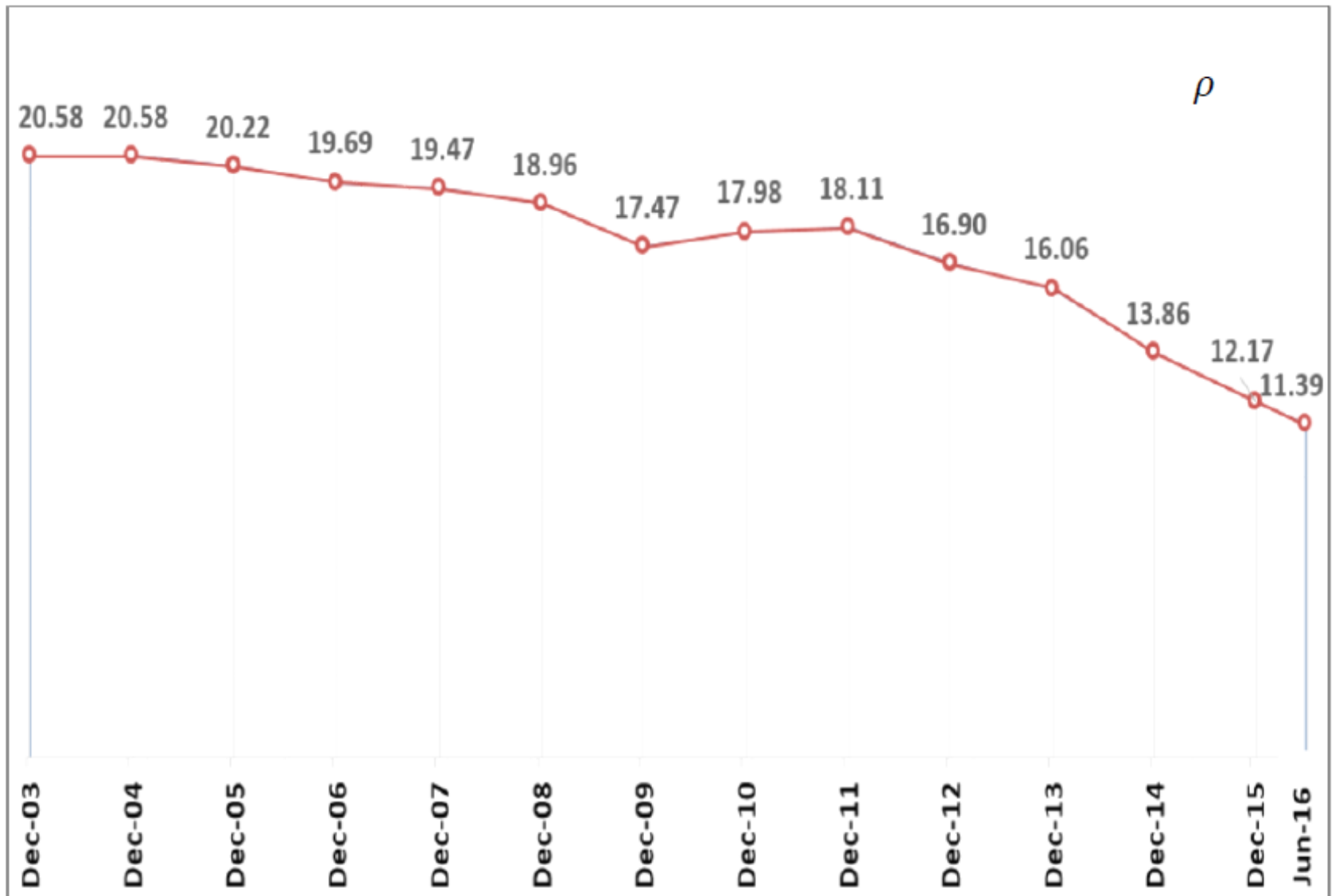


Figure 5.4 - Fiscal Reaction Over Time, in Reais of 2016



FISCAL DOMINANCE IN BRAZIL: AN
APPROACH BY SIMULATED
METHOD OF MOMENTS

Eduardo Lima Campos
Rubens Penha Cysne

The Results Here Displayed are Preliminary
and Subject to Usual Statistical Uncertainties

$$\pi_t = 0,711h_t + 0,496\Delta e_t + 0,707(E_t\pi_{t+1} - \pi_{t+1}^m)$$

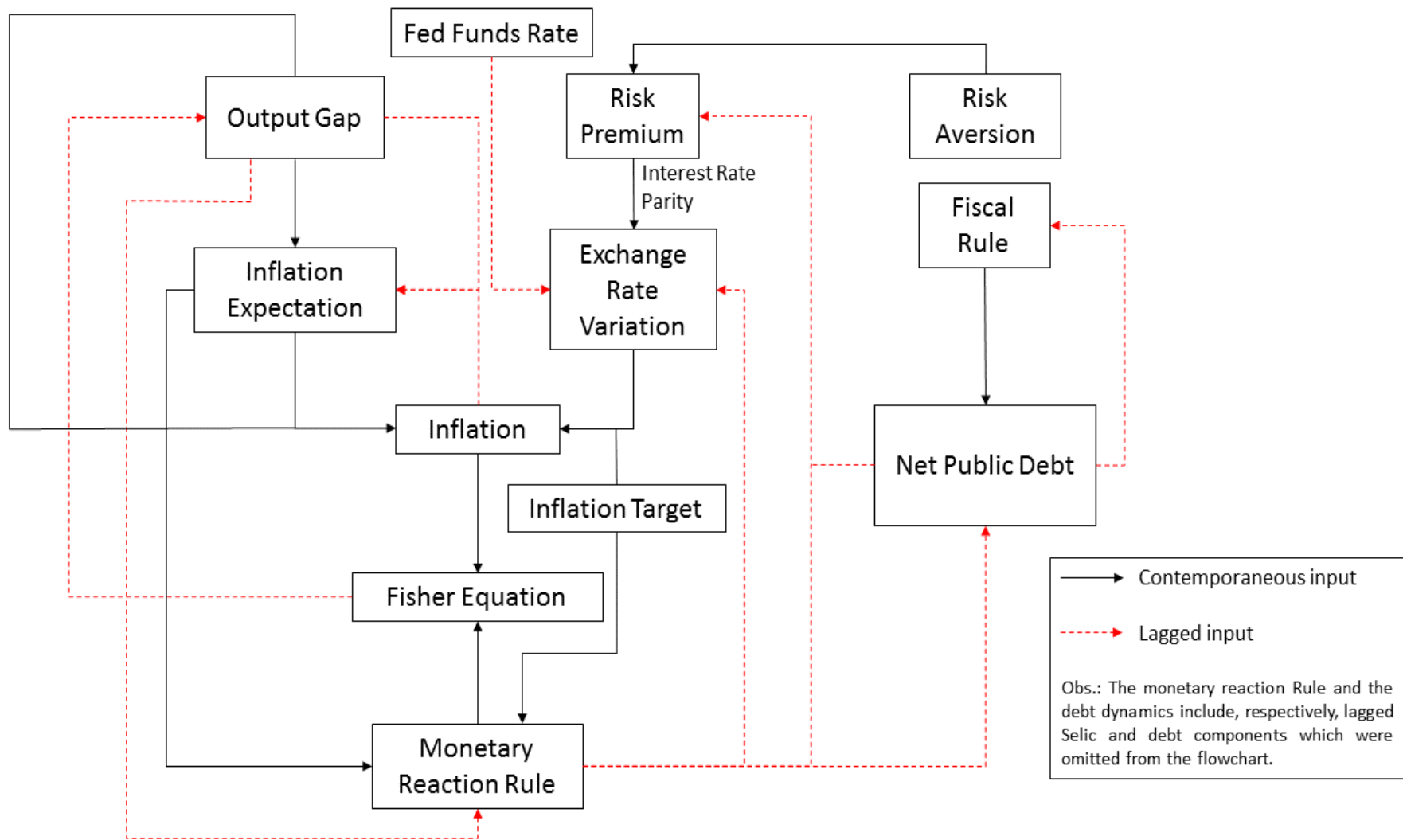
$$i_t = 0,873i_{t-1} + 1,281(E_t\pi_{t+1} - \pi_{t+1}^m)$$

$$E_t\pi_{t+1} = 0,623\pi_{t-1} + 0,18h_t - 0,05h_{t-1} + 0,24h_{t-2}$$

$$h_t = 0,647E_t h_{t+1} - 0,062r_{t-1} - 0,041r_{t-2} - 0,072r_{t-3}$$

$$E_{t-1}\Delta e_t = -0,611(i_{t-1} - i_{t-1}^*) + 0,0849rp_t$$

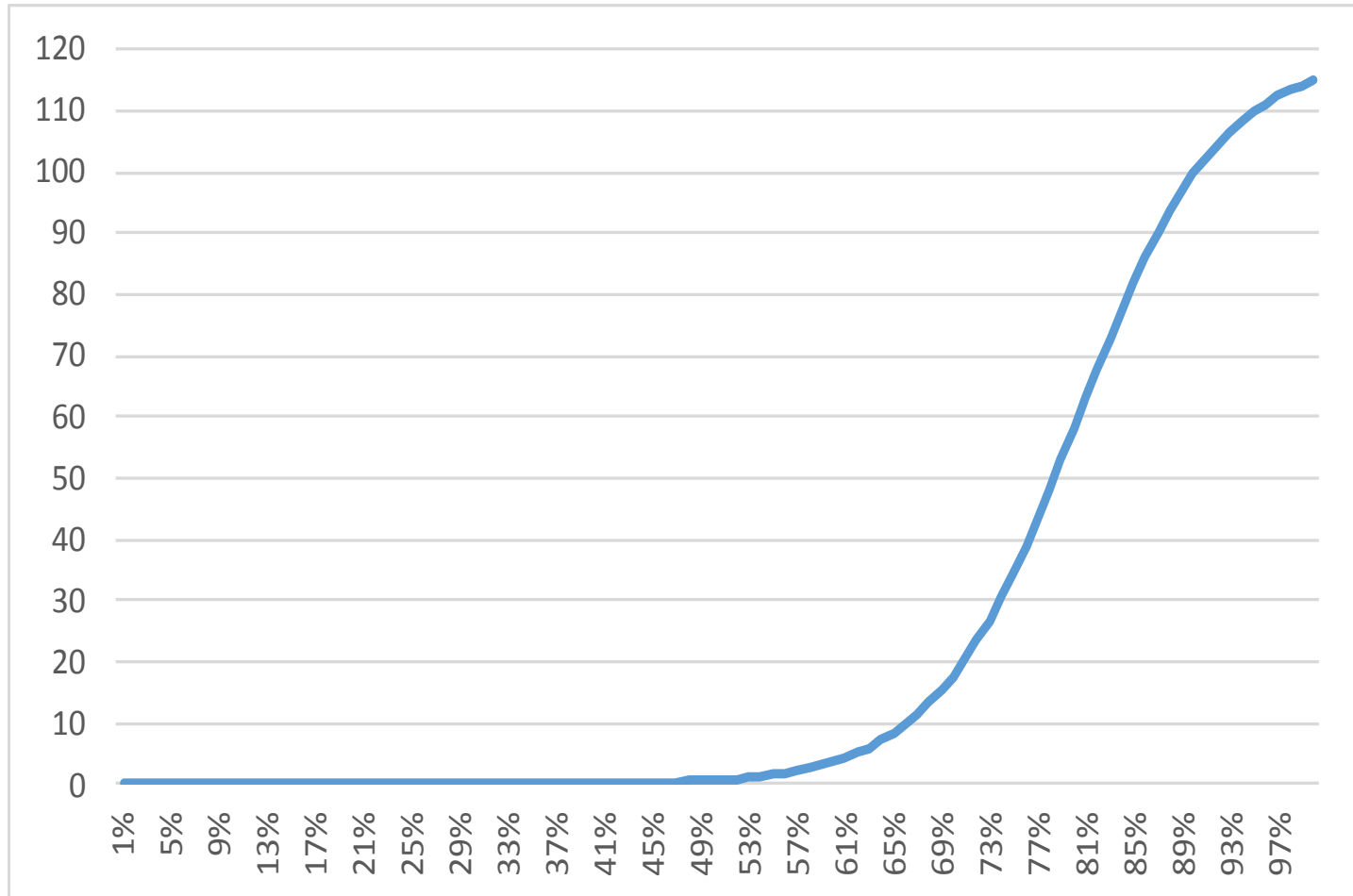
$$rp_t = \frac{237,941}{1 + e^{-16,91(b_{t-1} - 0,803)}} e^{i_{t-1}} + 5,624ra_{t-1}b_{t-1}$$



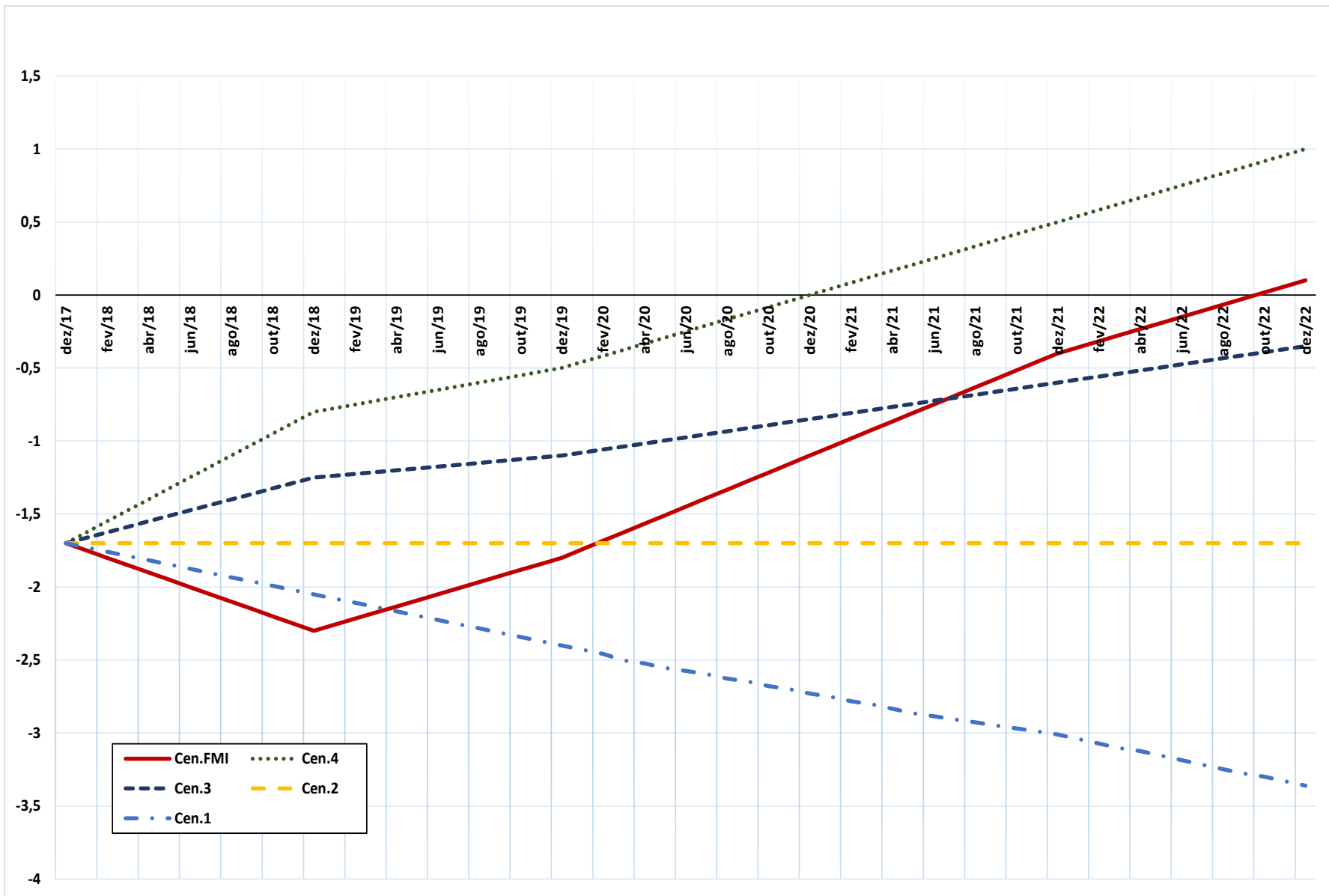
0,5 Points of Selic Increase: Decomposition of Effects over Inflation and R.P. Variation that Cancels the Overall Effect

	1 mês à frente	5 meses à frente
E.R. Pass Through	-2,09%	-3,68%
Aggregate Demand Effect	-0,36%	-1,93%
Total Conventional Effect	-2,45%	-5,61%
Variation of R.P. Necessary to Cancel the Overall Effect	60,08%	NA

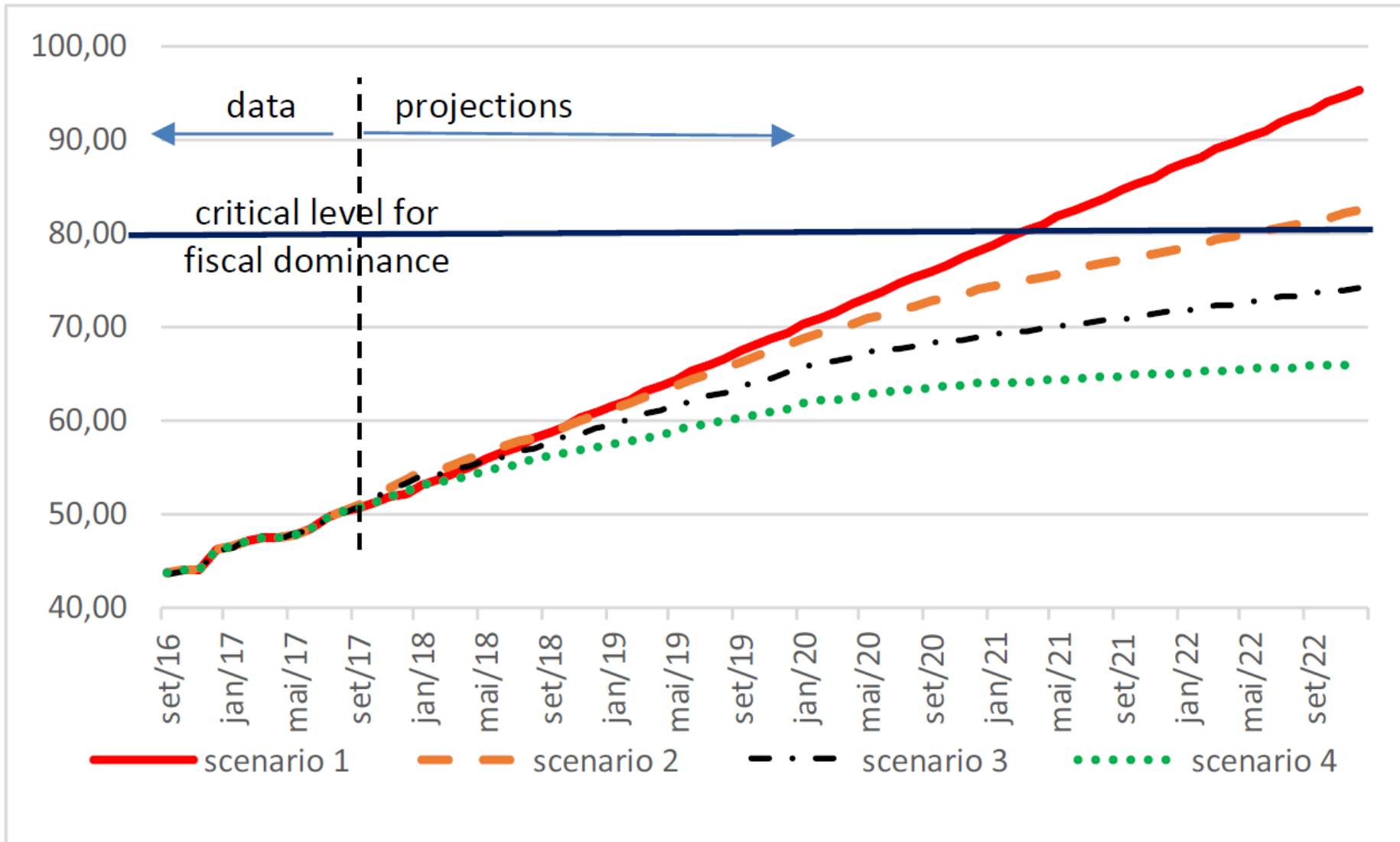
0.5 P.P. Selic Increase: % Variation of Risk Premium as a Function of Net Debt/GDP Ratio



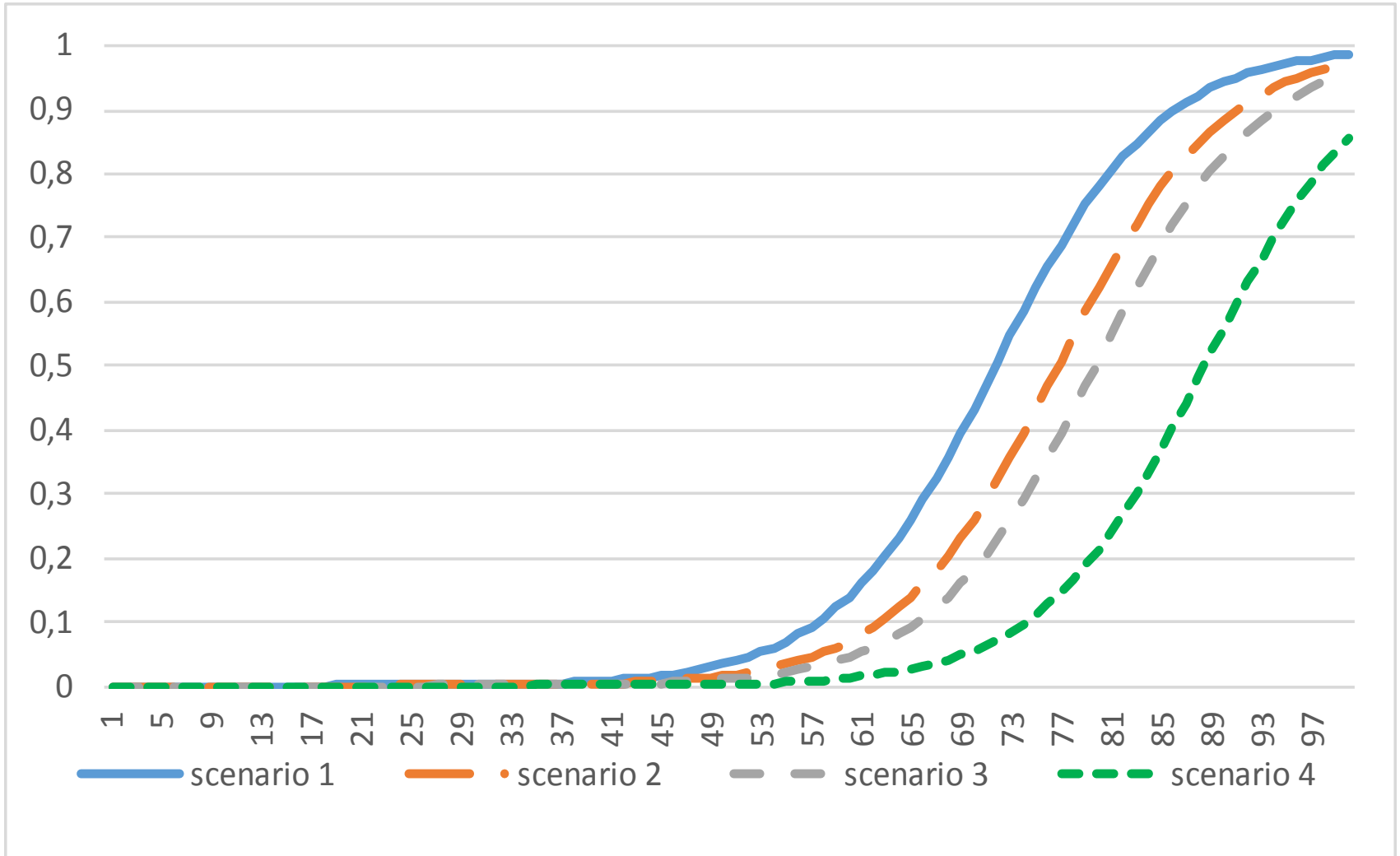
Primary Surplus Projections under Different Scenarios



Projections of Net Debt/GDP Under Different Scenarios



Probability of (Temporary) Fiscal Dominance



Thank You for Your Attention