Assessing the Impact of Fiscal Consolidations on Unemployment and Growth in the Brazilian Economy

Topic: Multiplier & Linkages Regional
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Since the great recession of 2008/2009, the role of fiscal policy for both economic growth and income distribution has been back to the academic debate. The more expansionary fiscal policy in the aftermath of the crisis did not last long and, a few years after the crisis, several countries implemented large fiscal consolidations in response to the sudden increase on public debt. As a consequence, many of these countries have faced an increase in inequality and a depressed economic environment, which imposed even larger fiscal adjustments. In Brazil, since 2015, based on the same assumptions of the European case, the so-called expansionary austerity, a major fiscal consolidation was implemented with huge impact on unemployment and public finances. The results of this paper support the view of a self-defeating austerity. The decrease on public investment, imposed by expenditures cuts, has actually contributed to the economic downturn leading to a continuous decrease on tax revenues. In order to identify and quantify this phenomenon, in this paper we apply the same methodology presented for the Portuguese case in Amaral and Lopes (2015). We derived, based on input-output relations, an unemployment rate/budget balance trade-off equation, as well as the impact of a strong fiscal consolidation based on social transfers and the notion of neutral budget balance. The data used is a series of I-O and Fixed Capital Matrices valued at constant prices constructed by the GIC-UFRJ for the period 2000-2015. Besides the analysis of the current fiscal consolidation, we also try to simulate the consequences of the â€œNew Fiscal Regimeâ€• with an emphasis on the expected impact of the expenditure ceilings on the trends of growth and income distribution. The paper confirms the huge costs of a strong and permanent fiscal consolidation, both in terms of unemployment and social policy regress.