



Brazil

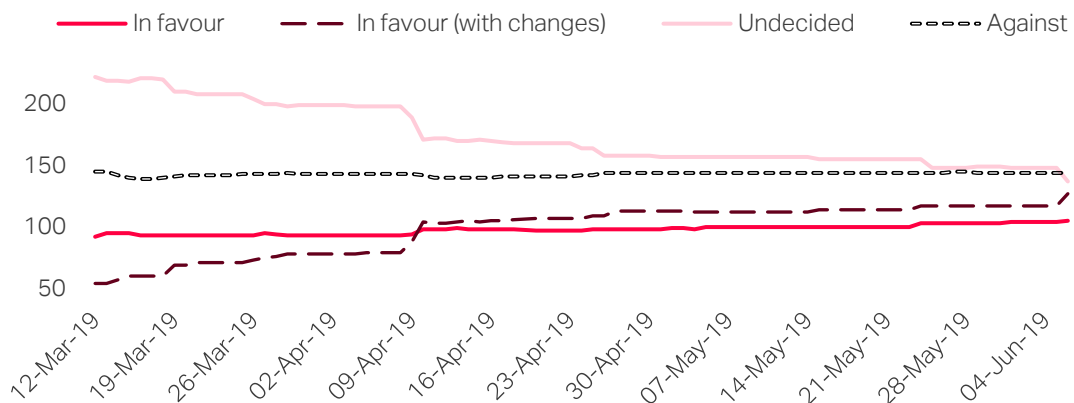
# SLOW PROGRESS IN CONGRESS

Elizabeth Johnson

- The government has scored some important victories in the legislature this week, as tensions eased between Bolsonaro and the Congress
- The government's lack of a base – and its apparent lack of interest in building one – means that it will have to fight to approve every bill
- The rapporteur of the pension reform will release his draft bill by next week, but the government still lacks the votes needed for its approval
- It is increasingly likely that state and municipal workers will be included in the reform after 25 governors showed public support for the reform

## Support for pension reform in the Lower House

No. of votes



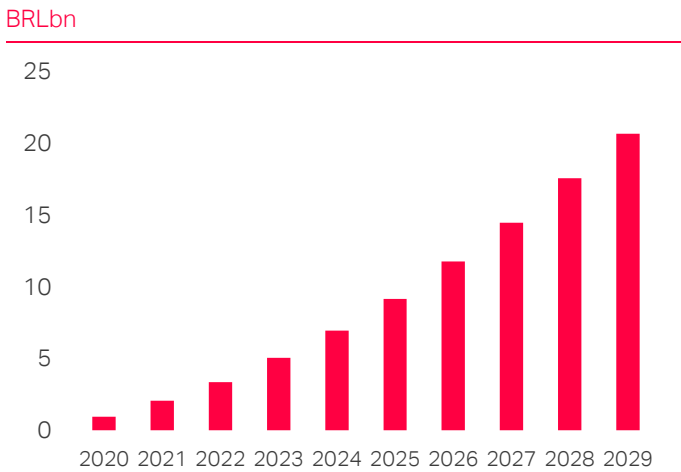
Source: Atlas Politico.

## Ongoing battles with the Congress

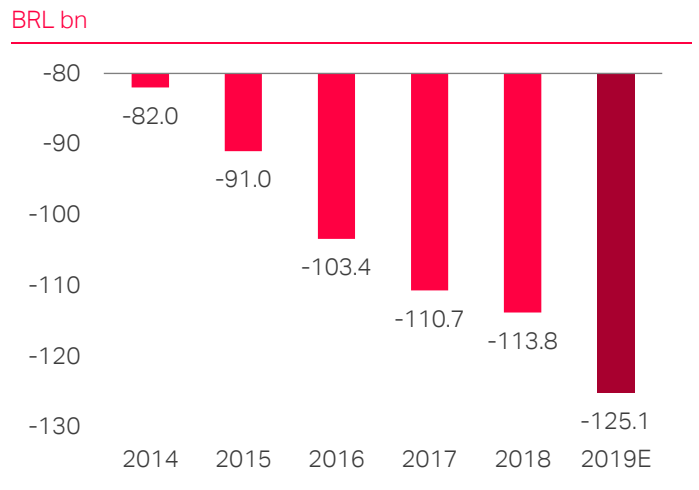
**Despite some important victories in the legislature this week and the improvement of the mood in Brasilia, Bolsonaro's relationship with the Congress remains strained.** The most important victory for the government was the approval of a presidential decree on Monday (3 June) that will allow the Social Security Administration (INSS) to carry out an extensive audit of benefits in a bid to reduce fraud in the system. At the same time, the legislation will tighten the requirements for people to claim rural pensions and widow/widower's benefits – two areas in which there are notoriously high levels of fraud. While the decree was passed just three hours before it would have expired, its approval in the Senate sent a positive message to the market about the willingness of legislators to support the pension reform.

**The anti-fraud legislation will lessen the impact of removing rural pensions from the reform.** Total savings from this measure are estimated at roughly BRL100bn over the next 10 years, equivalent to 10% of the BRL1 trillion in savings target that Economy Minister Paulo Guedes is hoping to reach through the broader reform. The legislation passed this week will stiffen the requirements to claim a rural pension, with the goal of reducing fraud. Over time, this will help reduce the rural pension deficit. The legislation that passed this week will also offset some of the losses in savings with the removal of rural pensions from the broader pension reform bill. As we have highlighted previously, the proposed changes to the rural pension system have been one of the areas that have received the most criticism from the legislature. As a result, the broader reform is unlikely to include any changes to rural pensions.

**Chart 1: Savings from proposed changes to rural pensions**



**Chart 2: Rural pension deficit**



Source: Economy Ministry.

The legislation passed this week will also require medical exams for people who have been receiving disability payments for more than six months. It will also increase the requirements for domestic partners to claim pension benefits. The legislation will also make it more difficult for families to collect pension benefits when a head-of-household is incarcerated, which plays well to Bolsonaro's base.

**Although there was solid support for the anti-fraud legislation in the Senate, with 55 Senators voting in favour of the bill and only 12 voting against,** its approval just three hours before expiring highlights the problematic modus operandi of the Bolsonaro administration. The lack of both a solid congressional base and a coordinated strategy means that the administration has been more engaged in crisis management than in crisis prevention with respect to getting key legislation passed. We expect this to continue to be the case in the future, and the government will be forced to negotiate legislation on a case-by-case basis rather than be able to count on a sound base of support allowing it to move ahead with its agenda. This is in part because the administration does not appear to believe that it needs to build a coalition in the Congress. As a result, the government will likely have limited success in passing unpopular legislation in the future, especially if Bolsonaro's approval rating continues to erode.

**The lack of political coordination was apparent on other fronts this week as well.** Most damaging to the government was the approval of a constitutional amendment that will further reduce the government's discretionary spending. The legislation, which had been stuck in committee since 2015, was revived at the end of March, when the relationship between Bolsonaro and the Congress took a turn for the worse. The legislation will guarantee the disbursement of 0.8% of the total annual federal budget for parliamentary amendments starting in 2020 and 1% from 2021 onwards. This will make it even more difficult for the administration to comply with the spending cap and the golden rule, because it will reduce its ability to cut spending.

**Further, legislation that will limit the use of presidential decrees was passed in the Lower House and should be approved next week in the Senate.** In addition to limiting the federal government's flexibility to allocate budget, the Congress is seeking to reduce its ability to legislate by decree. With the likely approval of this constitutional amendment, presidential decrees will lose their validity if they are not approved in 40 days by a joint committee of the legislature. If approved by the joint committee, the decree would need to be approved by the Lower House in 40 days. Once a decree is approved in the Lower House, the Senate would then have 30 days to approve the legislation. If any of these deadlines are missed, the decree would lose its validity. Currently, a presidential decree goes into effect immediately and needs to be approved by the Congress in 120 days. This means that the President would have much less time to negotiate the approval of these decrees, which have been a common means of legislating in recent administrations. The legislation is part of a broader trend that we have highlighted recently – namely, of the Congress taking a more active role in presenting and passing new legislation in order to fill the power vacuum left by the weak executive branch.

**Meanwhile, the vote that would require Congressional approval for the government to issue additional debt was postponed until next week.** As we highlighted last week, because of weaker growth and lower revenues, the government runs the risk of failing to comply with the so-called "golden rule", which prohibits it from issuing debt for purposes other than capital investments or debt refinancing unless it has Congressional approval for such deficit spending. Although we expect the Congress to approve the additional debt issuance to avoid a government shutdown – in part because failure to do so would force the government to suspend the payment of key social benefits – the lack of political coordination has kept this issue from being resolved quickly.

The rapporteur of the bill in the Lower House, Hildo Rocha, argued that the government ignored this issue. Rocha also blamed the government's lack of organization for the failure to secure approval of the legislation in committee. But because this issue still has not been resolved, the administration will need to continue to focus its attention on gaining the green light for the

additional spending. This will further detract attention from the pension reform. According to Treasury Secretary Mansueto Almeida, the bill needs to be approved by 15 June if delays in the July payments for rural credit and disability payments for impoverished seniors are to be avoided. In an indication of the potential problems created by the lack of congressional approval for the additional spending, the government was forced to delay its farm bill for the 2019-20 season, originally scheduled to be released this week.

**But the administration is now closer to being able to share revenues from the pre-salt mega-auction with state and municipal governments without violating the spending cap.**

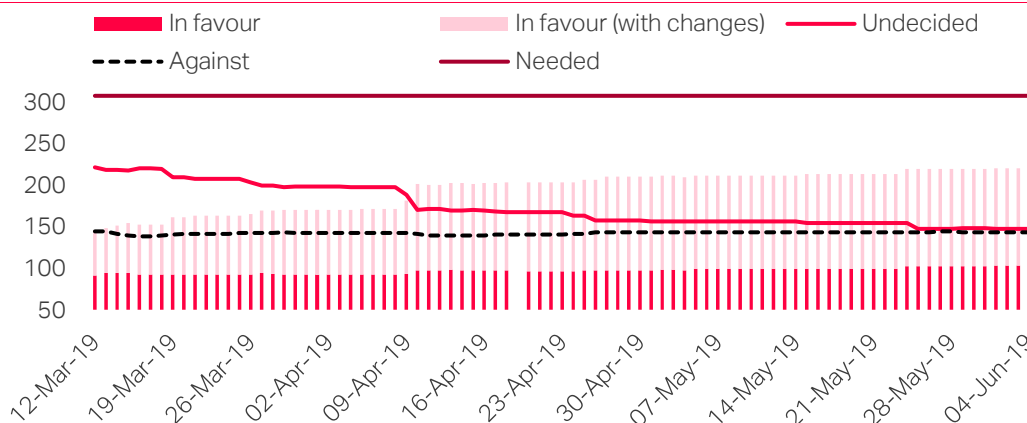
This issue has been a thorn in the Bolsonaro administration’s side since last November and resolving it would bring some relief to the government. Although the Congress did increase the amount of such revenues to be transferred to state and municipal governments to 30%, up from the 20% originally suggested by the administration, the fact that negotiations are advancing is positive. And the likely approval of this important piece of legislation would be a key development because it would clear the way for the mega-auction to take place on 28 October, as scheduled. It will also help to reduce the fiscal deficit this year, while helping to increase investment in Brazil’s oil and gas sector.

## Pension reform debate enters the home stretch

While the government continues to focus on short-term issues, the rapporteur of the pension reform, Samuel Moreira, is working on finalizing his draft of the legislation. Moreira has been holding meetings with party leaders and members of the Lower House to reach a consensus regarding the final draft of the reform. Currently, the government lacks support for the reform in the Lower House, where it needs support from a minimum of 308 of the 513 members. Still, in recent days, support for the reform has increased and 232 members of the Lower House are now in favour of the reform as it was presented by the government and an additional 127 Congressmen say they support it with changes, according to a survey by Atlas Político.

**Chart 3: Support for pension reform in the Lower House**

No. of votes



Source: Atlas Político.

**While Moreira had initially indicated that his draft would target savings of roughly BRL1 trillion over the next decade, his total is likely to be less.** Moreira received a total of 277 amendments to the reform and is now sifting through these suggestions to decide which he will include in his proposal. More importantly, he is engaged in discussions with party leaders to

finalize a draft of the legislation that will be acceptable to three-fifths of the lower legislature. In addition to removing changes to the rural pension system and to disability payments for the elderly, he is reportedly considering the removal of teachers from the reform as well as possible changes to the transition period to the minimum retirement age. In this context, we believe that there is a growing chance that the 10-year savings from the reform will be in BRL700-800bn range. While this is not the ideal reform, it would nonetheless satisfy markets and help put Brazil on a more stable fiscal trajectory.

**One key remaining issue is whether state and municipal workers should be included in the reform.** This has been at the centre of debates in Brasilia over the past week. Governors from the market-friendly Brazilian Social Democrat Party (PSDB) were in the capital this week to show their support for the reform and to demand that state and local government workers be included in it. This sentiment was echoed by the president of the National Mayor Caucus (FNP), Jonas Donizette, who has been a staunch supporter of including municipal workers in the reform. For his part, the president of the National Municipal Confederation (CNM), Glademir Aroldi, has threatened to file a lawsuit if municipal governments are not included.

**In response, 25 governors issued a document on 6 June in favour of the reform, requesting that the Congress keep state and municipal workers in the reform.** The threat of removing states and municipalities appears to be working and governors are starting to lobby their representatives in the Congress to support the reform. A case in point is the Brazilian Democratic Movement (MDB) party. Governor's including Helder Barbalho of Pará state and Governor Renan Filho, of Alagoas states have been meeting regularly with the party's 34 congressmen in an effort to convince them of the importance of voting in favour of the reform and of including state and municipal governments in the reform. As we argued back in [February](#), the support of state governors is yet another element that will contribute to the approval of pension reform this year.

One possible solution suggested by the FNP's Donizette is to include a provision that would require mayors and governors to issue a decree ratifying the reform once it is passed by the federal government. This would require them to express their public approval of the reform and thus share the onus with members of the legislature.

**Maia continues to push for the reform to be passed before the July recess.** Indeed, as part of his efforts to continue to grow his political capital, the Lower House Speaker remains a leading supporter of the reform. Earlier this week, Maia announced that he will not approve travel plans for members of the Lower House after 20 June in a bid to guarantee the necessary quorum for the reform. Similarly, Senate President Davi Alcolumbre has promised that the Senate will vote on the reform as quickly as possible. Still, the president of the Special Committee has warned that because of the 20 June Corpus Christi holiday and the festivals in late June in northeastern Brazil, a vote might not be possible until early July.

## Conclusion

**Tensions in Brasilia have eased, in large part because Bolsonaro himself has been working to improve his relationship with the Congress.** He has gone out of his way to commend Speaker Maia and other members of the Lower House for working to approve legislation that will help improve the country. He has also avoided references to "old-style" politics, which has been a source of irritation, particularly for politicians from centrist parties (Centrão). But it is clear that members of the legislature do not trust the President and are

seeking to curtail his power. Furthermore, it remains to be seen how long Bolsonaro will maintain his peace-and-love approach to dealing with the Congress.

**The legislature will continue to fill the power vacuum that has emerged because of Bolsonaro's lack of a clear agenda.** The upside to this is that the legislature is taking an active role in pushing important reforms. This was evident this week, when the Senate passed its own bill aimed at increasing private investment in the water and sanitation sector after the government failed to secure support for the presidential decree which expired on 3 June. While the recent congressional activism is a far cry from a parliamentary system, we believe that the increased role of the legislature is a positive trend.

**Positive momentum continues to build in favour of pension reform.** Despite Bolsonaro's limited role in gaining approval for the pension reform, by taking a back seat in discussion with the Congress, he has given key members of the legislature the opportunity to take the lead on the reform. Because there is a growing consensus of the need for pension reform, members of the Congress are more willing to support this legislation. Furthermore, because of the dire fiscal situation that the country currently faces, the Congress can also count on strong support from state and local politicians. In this context, it is increasingly likely that the reform will pass sooner rather than later, and that the savings over the next decade will reach BRL700-800mn. While this is not the ideal reform, it will satisfy the market and will also help put Brazil on a more sustainable fiscal path.