



Fernando Henrique Cardoso, President, Federative Republic of Brazil

The Cardoso agenda

It is bold and ambitious: Brazil's head of state seeks to build a more democratic society, impose fiscal discipline, assert leadership in Latin America and claim a new role for his country in the global economic order. Can he succeed?

It became a late-20th-century truism: Despite its sheer mass, wealth of natural resources, prodigious industrial and agricultural output, sophisticated financial sector and dynamic people, prosperity and economic stability would elude Brazil seemingly forever.

Decades of import substitution had created an industrial establishment unprepared to compete internationally. Hyperinflation and erratic shifts in government policy undermined investment in the economy. State domination of the economy stifled market mechanisms. Across vast areas of the country, people struggled in poverty and drought. And of perhaps greatest concern to foreign investors, Brazil appeared to be perpetually, and deeply, in debt.

Under the presidency of Fernando Henrique Cardoso, however, Brazil has taken giant strides toward finally

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becoming the country of the future—today. Since Cardoso was elected to his first term in 1994, the country has adopted new laws and practices designed to integrate Brazil into the global economy, including constitutional reforms that open key sectors of the economy to foreign investment and guarantee equal treatment for foreign investors. He also renewed the privatization program initiated by a predecessor in the early 1990s.

Cardoso was reelected in 1998, and the centerpiece of his second term has been an ambitious agenda of fiscal reform aimed at imposing discipline in public finances and overhauling Brazil's tax and social security systems.

These policies are in fact a continuation of those he had authored as finance minister, beginning in 1994 with the introduction of a new currency, the real. Cardoso's Real Plan brought monetary stability, allowed authorities to tame inflation from historic highs of 50 percent per month to annual rates in the sin-

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gle digits, raised the real purchasing power of low-income Brazilians substantially, and fueled investment and consumer demand by opening and stabilizing the economy.

Cardoso—intellectual, urbane, well-traveled, fluent in several languages—slipped easily into the role once occupied by Carlos Salinas of Mexico: that of the industrial nations' favorite example of the modern Latin American leader. During his administration, Brazil raised its profile on the world stage, assuming new responsibility and influence in international bodies like the United Nations and the Basle Committee and leadership in regional trading blocs like Mercosur.

Brazil could not escape the ripple effect from the Asia crisis and Russia's default, however, and the boom, like so many before it, gave way to bust. The real collapsed on January 13, 1999, losing nearly 9 percent of its value overnight and a total of 37 percent by mid-November. In the wake of devaluation, the economy has contracted, boosting joblessness. Popular discontent has been aggravated by IMF-mandated austerity measures;

among the chief casualties: Cardoso's popularity.

Yet it was a robust, charming President Cardoso who received visitors in the spacious, sparsely furnished library of the Palácio da Alvorada, the presidential residence in Brasília, in November. Alternately blunt and self-deprecating but always good-humored and remarkably self-assured, he spent more than an hour with *Outlook* Editor-in-Chief David Cudaback and Managing Editor Letitia Burton discussing his unfinished economic agenda and his vision of a more open society.

He readily acknowledges the paradoxical nature of his quest: In an already fractious political culture, the more democratic the system becomes, the more difficult it could be to reach consensus over essential reforms.

Does the problem lie with the country's notoriously complex constitution? a visitor asks, pointing to a bound copy on the president's desk. "Oh, that's *terrible*," Cardoso says with a laugh and dismissive wave of his hand. "I know: I helped write it."

Outlook: In an interview with former Portuguese president Mário Soares, you said that your "political and intellectual ambition is to open a new era" and to "leave a mark" on Brazil. With one term behind you and three years remaining in your current term, how close do you think you are to achieving these goals?

President Cardoso: When I refer to a new era, I'm referring to an open society, an open economy and a much more active civil society. Not a stateless society, not neoliberal, but something that gives much more room to different groups within society. I believe it is important to go more in depth in that direction, to give society much more freedom.

What role do you envision for the government?

The government is becoming much more accountable. Everyone can know what is happening in government. We are decentralizing the state. Instead of a small state, we are trying to organize an *effective* state, introducing public control in the decision-making system.

You ask me to what extent I think this has been successful. It's difficult to evaluate. But we have come a long way. If you look at Brazil today and compare it to what it was 10 years ago, the results are quite evident.

Your opponents in Congress have not always agreed with your vision of Brazil.

Any process of reform is difficult and involves obstacles. It's enough to see how many deputies in Congress are speaking against our proposals. That's a good indicator of what is happening, and it's very difficult because I need the political support to implement reforms. That is normal in the democratic process, and it gives us greater legitimacy in the results we are able to accomplish.

What tangible results can you point to?

I will give you one highlight: primary education. We have more than 96 percent of children of schooling age enrolled in public schools—37 million students.

Another important contrast with the previous era is the opening of the Brazilian economy and the role of private-sector investment in some public services. I'll give you an example: In my presidential role, around this table, I made an agreement with the so-called barons of Petrobras, which took the form of a constitutional amendment opening oil exploration to foreign private capital.

In the area of telecommunications there is also a revolution under way. Now there are, I don't know exactly, perhaps 12 million cellular phones in Brazil. The cost has been reduced dramatically so that now a worker can have a cell phone. This is also very important in terms of democratization, in terms of access to consumption.

Six years ago there was tremendous debate over how to break the state monopolies. Now no one is discussing if it is possible or not to compete. This is no longer an issue.

Brazil's credibility among foreign investors depends on your government's ability to complete its fiscal reform agenda, which, in turn, would bring meaningful reduction of the country's foreign and domestic debt. What progress are you making in these areas?

First, the government foreign debt is not very considerable. In our reserves we have around \$40 billion. Our foreign debt is \$100 billion. So we have \$60 billion; this is a relatively small sum, given the size of the Brazilian economy.

The private sector in Brazil has around \$200 billion in foreign debt. Providing they can roll over the debt, it's no problem. When we have a financial crisis, and the foreign creditors prefer not to continue to roll over the debt, that's a tremendous problem. But under normal circumstances, this is not a problem. Our GDP is about \$700 billion, so the debt is 40 percent.

What about the domestic debt?

The domestic debt in Brazil is in the hands of Brazilians. It's not like in Mexico, where the domestic debt is in the hands of foreigners as well as Mexicans but not denominated in dollars. In Argentina it is again different, because the Argentineans have 80 percent of the domestic debt denominated

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in dollars. In our case, the internal debt is in reals, the local currency.

Everyone who has money in the Brazilian banking system is a creditor to the Brazilian state. So it is a domestic relationship.

From time to time abroad they said, "Oh, the Brazilians have not been able to pay the internal debt." And of course if the rate of interest goes up and up, this is true. But if the rate of interest is going down, like it is now, this is nonsense.

But there is nonetheless a downside to the public deficit.

What is bad is that the government is competing for funds with the private sector, and that is one of the reasons why it's necessary to reduce the official interest rate.

The internal debt now is approaching 50 percent of the GDP. If you look at the United States, it's 150 percent; in Italy, 110–120 percent. Now we are extending the maturity of the debt. As an average, it's 11 months; when I was finance minister it was two months. So the situation is absolutely under control, in our hands—providing the interest rate is under control and providing Brazilian savers have their money in domestic currency.

How is your fiscal reform agenda faring in Congress?

The Congress has approved almost everything we sent. Of course, every congress is complicated; in a democracy you cannot imagine the congress will just say yes. From time to time, they say no. And even when they say yes, they correct what's been sent. And the corrections are not necessarily good ones. Democracy takes time. So we are negotiating—again and again and again.

What about reforming the social

security system?

I was reading very recently a paper on the social security system modifications in France, Italy and Germany. If you compare Brazil with them, it is clear that we have made enormous progress. The Italian system was perhaps even worse than Brazil's. They have been able to introduce some modifications; we have done the same.

Regarding private-sector pensions, the modifications are enough to provide control in the coming years. The idea is to stabilize and then to reduce the payments as a proportion of GDP.

In practice, our system is in equilibrium if you consider that there are about 6 million people in the rural areas who never paid into the system but are entitled to receive a pension. This is a social program; it is not a social security program. In the current system the deficit is around \$10 million; what is paid to the rural employees is about \$9 million. So the system is around the equilibrium point.

But pensions for public-sector employees is a separate problem.

The situation in the public service is much more dramatic, because in Brazil the public service has been always governed by privileges. Congress approved a modification that would impose mandatory pension contributions on retired civil service employees. Why? Because until 1993 they didn't contribute anything to the system. So they have no right to receive a full pension.

And it's more than a full pension. The day they enter into retirement they receive the same amount of money [as their former salary], plus 11 percent. It's the only country in the world where you get more when you retire than when you are working. In this sense, it's crazy.

Imposing pension contributions was very difficult to get approved. But the Supreme Court decided that the Constitution lacks an article to allow this. So I sent to the Congress a new amendment proposal that would introduce in the Constitution the possibility to charge retired people.

I will win this battle. This will cost my popularity, of course, because it's not popular to be against these kinds of privileges.

Part of the media claims that reform will affect the poor. This is not about the poor: This is about judges of the Supreme Court, generals, professionals in some universities. They are entitled to receive maybe 20,000 reals [approximately \$10,000] per month.

What is the status of the proposed fiscal responsibility law?

This is a very good bill and very important because it puts some limits on expenses by the judiciary and the local assemblies. The bill is being discussed in the House; it has been examined by the Rapporteur. It is now under consideration by the special committee. It will probably be approved, and we will have some limits on extreme cases of bad management of public money.

Tax reform is another key issue, particularly for companies operating in Brazil.

To my surprise, tax reform is making progress. It is about to be approved by the special committee in the House. As you can imagine, tax reform is very difficult.

Brazilians are Iberians—Portuguese and Spanish people. So we like imagination—big transformations, new plans—and, like me, “new eras.” The idea is to reform the whole tax system. This has advantages, but it is very risky. We never know who



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is losing and who is gaining in the federal government, the local government and the states.

I would prefer more modest proposals that introduce reforms step by step. The Rapporteur has presented his views, and he came several times to see me around this table with his people. There are different views and different perspectives. But we are making progress.

When do you expect tax reform to be resolved?

It takes time. Certainly we'll continue to discuss it this year. The schedule was to start by 2001. So we are trying to keep this in mind. What is important from the point of view of the government is to reduce the cascade of taxes on the current system. This is the main task we have.

The federal government has enough money. Right now we have a surplus of about 3 percent of the GDP, so we have room to maneuver; we don't need more taxes. We need to [better] utilize what we already have; we need more flexibility to do this. Of course, those sitting around my table, the ministers, don't like me to say it, but we don't need more money.

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But you do presumably need more growth.

Definitely, definitely.

What will be the sources of sustainable growth?

If the government continues to produce surpluses, this will be positive for our growth because the rate of interest can be reduced. Secondly, we have to produce surpluses in trade.

In our external accounts in 1998, the current account deficit was around \$34 billion. [For the first 10 months of 1999 it was estimated to have been] around \$20 billion. So the necessity of external financing is considerably reduced. Foreigners are investing heavily in Brazil. [In 1999] we didn't need any more foreign borrowing because the level of foreign direct investment was higher than the current account deficit. Foreign direct investment was something around \$26 billion in 1998, and the estimate for 1999 is similar.

Much of the direct foreign direct investment is market-driven—investments companies make to sell goods to consumers in Brazil, rather than export-oriented investment. That's not bad, that's good because

it means that the domestic market is expanding. We are like America was in the past. We are inward-oriented, because we have a big domestic market. We are exporting around \$50 billion—a very, very modest figure compared to GDP. It's only 7 or 8 percent. And we are importing about the same. So we still are domestically oriented. However, we need a more positive trade balance, because we have to continue to import.

How is the Mercosur regional trading bloc likely to evolve?

When I was in Buenos Aires six months ago, I said that we needed a "little Maastricht" for Mercosur. [Argentine president Carlos] Menem was proposing a common currency. But before you have a common currency, you have to have a convergence in your macroeconomic policies.

If Brazil and Argentina and possibly Chile are able to adopt this view, it will help us to negotiate with America like it helped our negotiations with the Europeans. And if we are able to propose a set of feasible targets for economic convergence, this would be good for the region.

Mercosur is not exactly an alliance of equals, however.

Brazil is effectively able to become integrated at the global level in the new order, in terms of industry and technology. We are able to produce planes; we are able to explore for oil in deep waters with our own technology; we have the capacity to produce seeds in agriculture. So we have some advantages.

However, that is not necessarily the case for all partners in Mercosur. Each member has its own advantages and disadvantages. So we have to organize in such a way that capital flows within the region are encour-

aged. And that's the problem. This in effect requires a more open mind in our private sector—not only in Brazil but also in Argentina. There are still people who speak as if the times have not changed. Some business sectors in both countries still seem to believe they are in the 1950s. They believe they need more tariffs, more protection, more banking system assistance. They believe they have to compete with each other.

Will that attitude change under Argentina's new president, Fernando de la Rúa?

I have met him twice—yesterday and six months ago—and I was impressed by his grasp of the challenges facing Argentina and Mercosur. I am sure he will be doing his best to meet these challenges. But these things do not depend entirely on presidents' decisions. Anyway, I believe it is the responsibility of presidents to exercise leadership and pay the price.

How would you characterize the relationship between Brazil and Argentina?

I remember once when I was in Germany, and had a conversation at lunch with [former German chancellor Helmut] Kohl. He said to me, "You know, we made an agreement with the French people. In the past we had wars. I realized it was necessary to put an end to the situation, and we decided to be allies with the French. But we are the strongest. We are 90 million people. So we have a responsibility. We have to make an agreement with the French people, giving them more possibilities than we have. You Brazilians, you are like Germans: You have to do the same with the Argentineans."

And Kohl was right. Integration always involves a certain amount of generosity on all sides, and awareness of this fact is particularly important to Brazil, which, as a large country,

tends to be introspective. This awareness is indeed important for bringing a positive contribution to help the integration process move forward.

Have you persuaded your countrymen that this is the right course?

I try, but it's difficult because it is not easy to understand that you have to be more generous vis-à-vis the Argentineans. They are wealthier than Brazilians, in average terms. So why be more generous? That answer is that if you look to the future, we will have more opportunities together.

What about Brazil's position in the global economy?

Maybe only China, India and Brazil have the possibility to enter the new global order in the coming century in a more competitive way. That is because of our technological advancement and systems at the federal and state level to support research and technology. The federal system grants between 40,000 and 50,000 fellowships every year. If you add to this what exists in the local areas, there is a considerable amount of money going into training. So in spite of the fact that the Brazilians complain day and night about the lack of public support for research and technology, it's just not true.

Is Brazil's political culture changing?

In the past, Brazilian political culture was influenced by European experience. We tried again and again to organize parties like in Europe. We failed, because we are Americans, in the proper sense. There is enormous space and mobility—social mobility and regional mobility. Local institutions will continue to grow stronger. The state will be less strong than in the past. That's not Europe. In Germany or in France or in Italy, the state is still the state. Parties correspond to class structures.

In Brazil there is no correspondence between parties and class structure because class structure is much more flexible than in Europe, again like in America. But we also have some of Africa in Brazil; it's a complex mix. And we have to face the problem of exclusion, in order to incorporate all Brazilians into the political system.

I don't know to what extent the system will move in a more open way toward the American model. This is a question mark. In the European system it is very difficult for a person who is not rooted in the political system and political culture to become the president, prime minister or whatever. In America too, the civil culture has a kind of filter. There are two parties, and they are running around the center of the political spectrum.

Our system is much more open. It is much more difficult to forecast, but it's still today possible for an outsider to enter into the system.

What is your primary goal for what is left of your term?

My main responsibility is to look to the future and to make sure we move on with our policies, in order to guarantee continued economic stability and more equitable opportunities and living conditions for all Brazilians. But we do not take anything for granted, I am telling you very frankly. ■

Additional background reporting was provided by Lucy Conger, a financial reporter in Mexico City and a former São Paulo correspondent for Reuters.

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