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LATIN AMERICA

Brazil Senators Approve Pension System Overhaul

The passing of the legislation is a political victory for President Jair Bolsonaro

Brazilian senators celebrate after a revision of the country's social security system was approved. PHOTO: BRUNO ROCHA/FOTOARENA/ZUMA PRESS

By Paulo Trevisani and Jeffrey T. Lewis

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BRASÍLIA—Brazilian senators overwhelmingly approved on Tuesday a revamp of the country's insolvent social-security system, which will sharply lower spending and serve as a pillar for President Jair Bolsonaro's overhaul of a sluggish economy hamstrung by bureaucracy and protectionism.

The legislation, which is projected to save taxpayers as much as $200 billion over 10 years, is a political victory for the president, who has been distracted by clashes with foreign leaders and lawmakers in the capital, even from his own party.

Markets have been rallying on the prospect of approval of the bill, with the Ibovespa stock index reaching a new high on Tuesday. The president is expected to sign the legislation into law in the next few days.

“The Brazilian Congress has dealt with a very hard but very important issue,” the Senate’s President Davi Alcolumbre said as he announced the result, capping months of often fiery debate. “This is the broadest pension reform ever” in Brazil, he said.

The bill, approved by 60 of 80 senators, raises the minimum retirement age to 65 from 60 for men and to 62 from 55 for women. It also plugs loopholes that allowed many workers, mostly in public service, to retire as early as in their late 40s, often with a full salary.

Retired police chiefs, judges, politicians and other state employees currently receive monthly payments as high as $9,000, nearly 20 times what most private-sector retirees get. That has led to a shortfall, which is expected to reach $60 billion this year. It is the main reason why Brazil has been living on borrowed money since 2014 and its sovereign debt rated as junk.

“Future generations of public servants won’t have this prospect anymore,” said Maria Luiza Machado, 70, a former central bank economist who retired at 48 with a full salary that allowed her to travel the world. She supports the legislation, saying, “We must think about the nation as a whole.”

Nearly all of Mr. Bolsonaro’s predecessors tried unsuccessfully to make meaningful changes to Brazil’s pension system—one of the world’s most generous—but stopped in the face of strong popular opposition. Mr. Bolsonaro’s supporters, however, bought into the administration’s argument that retirement perks bestowed mainly on well-paid public servants should be erased for Brazil to prosper. Many took to the streets in rallies to demand pension overhaul, rare in a country trying to rollback coveted benefits.

Brazil’s pension costs eat up to 45% of the federal budget. With much of the remaining funds going to pay salaries, only about 3% is left to build and maintain much-needed hospitals, schools and other infrastructure. The pension overhaul will keep the country’s debt under control, the administration says, allowing policy makers to focus on growth-spurring measures.

Pedro Zevallos, co-portfolio manager of emerging markets strategy at Dalton Investment, which has $250 million under management in emerging markets, said that the legislation had to be approved for Brazil’s government to cut costs and modernize the economy.

“Unless you address the root of the problem, the problem just gets worse, and it’s a ticking time bomb,” said Mr. Zavallos. “That’s why pension reform was their main project.”

Brazil’s economy could use a jolt as it recovers slowly from the crippling 2015-2016 recession. It is forecast to grow less than 1% this year. Unemployment is close to 12% and has been above 10% since the start of 2016.

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The overhaul of the pension system creates momentum for other economic changes spearheaded by Economy Minister Paulo Guedes, including slashing import tariffs, a drastic simplification of the country's complex tax code and a significant reduction in the federal government's 600,000-strong, $2 billion-a-month workforce. Details of the proposals are yet to be announced.

Central bank independence, a proposal economists say could help lower borrowing costs and spur consumption, is moving slowly through congress. Currently, the central bank president can be hired and fired by the country's president.

The legislation passed Tuesday will serve as a pillar for President Jair Bolsonaro's overhaul of the economy. **PHOTO:** ADRIANO MACHADO/REUTERS

"There is a huge pipeline of reforms meant to let markets work more freely," said Luiz Fernando Figueiredo, founding partner of the Mauá Capital, an investment firm with around $1.6 billion under management. "This agenda has been held back for too long."

Even with the tailwind, though, the administration still faces difficult and extensive negotiations to get congressional approval for the next item on investors' wish list, a simplified tax structure.

The administration's capacity to win support for politically delicate legislation like the tax overhaul has been hurt by an investigation by federal police of members of Mr. Bolsonaro's right-wing Social-Liberal Party, or PSL, for alleged electoral fraud. The scandal raised tensions between the president and the party’s leadership, with PSL lawmakers threatening to vote against the administration.

“I think nothing will be approved short-term,” said economist Fernanda Consorte, a foreign-exchange analyst at Ourinvest brokerage, referring particularly to changes in taxation. She said the government itself is indicating any revision might not be as deep as markets hope for. “They are already talking about going piecemeal on tax reform.”

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