Many economists have considered Brazil's unbalanced Fiscal accounts to be the most significant reason for inflation acceleration since the early sixties.

Mario Henrique Simonsen, one of the most prominent economists in Brazil history, is frequently cited as having said: Inflation cripples but the balance of payment (Exchange rate) kills - "Inflação aleija mas o Balanço de Pagamentos (câmbio) mata." In the late 70s, Brazil's main problem was a shortage of international reserves to pay all the external obligations, resulting in Brazil's 1982 moratorium.

The correct quote from Simonsen took place on two occasions in 1977, the first in a lecture and a congress speech: Inflation is irritating, but external impasse would be deadly - "a inflação é irritante, mas o impasse externo seria mortal."

Every attempt to stabilize Inflation from the early '70s until the Real Plan (1994) never solved the fiscal problem. The Real Plan in 94 managed to tame the hyperinflation but did not address the budgetary accounts. This imbalance was the leading cause of the 1998/1999 currency crisis.

The first practical attempt to stabilize the fiscal accounts started in October 1998, but it was too late. At that moment, Brazil began to aim for primary budgetary surpluses. Soon after that, Brazil shifted from a Peg to a floating exchange regime and has adopted an inflation target as a base for Monetary Policy goals.

For the first time, an established framework encompassed fiscal responsibility, inflation target, and floating exchange rate. This economic policy framework became known as the Economic Policy Tripod ("Tripé da política econômica." And the trilemma of Economic policy was finally resolved (reference trilemma).

From 1998 to 2014, Less than two years later, Brazil approved the Fiscal Responsibility Law and delivered all the promised targets set at the Budgetary directives law, where the fiscal result target is declared. Brazil has better results than the proposed law and for the two initial years were also part of IMF agreements.

From 1999 - 2013, 1999 - 2006 ( second FHC mandate and Lula's first mandate, second Lula ( 2007-2010 ) In 2008 Brazil became Investment Grade, and Inflation was under control. The average fiscal surplus was. Then came Dilma's Government (2011-2013).

<<<<<Grafico de superavit primario, 99-2013>>>>>>

In 2014 Brazil changed this behavior. To stimulate the economy and prevent an unavoidable recession, President Dilma opted for a permanent increase in expenditures and decided to run fiscal deficits.

<<<<<grafico superavit primario 99 ate 2021 com linha vertical (2013) - 2019>>>>>>>>

This resulted in sequenced downgrades, the loss of the investment grade, and a steep deterioration in fiscal risk. Debt to GDP was 52 in 2013, coming from 67 (?) in 2002 (2001). In only two years, the result was Debt to GDP increased to 70% in 2016 compared to 56% in

Federal Tax collection increased from 14% in 2000 to 21% in 2003, and total Taxation went up to 35%, coming from 27.5%.

After the Temer Government, the essential stabilization aspect introduced the spending cap in constitutional amendment 95. And some months later, the approval of the social security reform.

Those two efforts managed the debt/GDP around 75% from 2017 to 2019, and then Covid hit the world, and everything changed. Brazil spent 7% of GDP in 2020 and 1% of GDP in 2021 to minimize the effects on families, which explained 2/3 of the increase in debt to GDP; the rest was a reduction in tax collection.

The first three months of 2021 were paramount in determining if President Bolsonaro was committed to fiscal responsibility or not. After vetoing all the excess in this year's budget proposal, markets became calmer towards their preferred path.

Conclusions and Forecast

We expect debt to GDP to hover around 84 % over the next ten years. To have a declining ratio, Brazil will need to change the expenditures as we advance, so we regard as very necessary another round of Social Security reform AND a comprehensive administrative reform ( to reduce Public worker's wage expenditure).

Only after these reforms could we think of a reduction in Taxation in Brazil.

As the external accounts are in a very positive stance with the floating FX regime and favorable terms of trade, I would paraphrase the misquote about Simonsen.

Inflation is irritating, but the Fiscal impasse would be deadly.