

Poverty, Inequality and Stability



The Second Real



**Poverty, Inequality and Stability:
The Second *Real***

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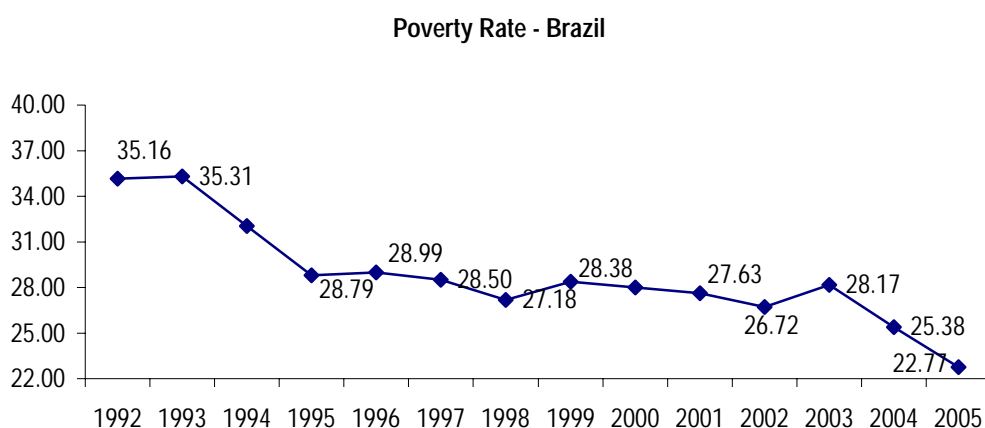
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Poverty, Inequality and Labor Dynamics

The Second *Real*

Since 1992, when the new PNAD survey was established, the figures for poverty indicate two significant changes in its status. Firstly, the proportion of the Brazilian population below the poverty line decreased from 35.3% to 28.8% between 1993-1995. In 2003, when poverty reached 28.2% of the population, a new period of descent began, leading to the figure of 22.7% in 2005, based on the new PNAD. This adds up to an overall decrease of 19.18% between 2003 and 2005—this magnitude being comparable to the 1993-1995 decrease of 18.47%. The graph below shows the parallels between these two periods that occurred 10 years apart.



Source: CPS/FGV processing PNAD/IBGE microdata.

OBS: 1994 and 2000 are averages of adjacent years, since in those years PNAD did not collect field data.

* Defined as the share of the population with per capita income below 121 reais, in today's prices in São Paulo metropolitan área, adjusted for regional differences based on living standard costs. See section on Methodology.

According to an analysis done by administrative periods, poverty fell 21.8% in both Cardoso administrations and 15.16% in the first three years of the Lula Administration. Given the differences in timeframe, poverty decreased an annual average of 3.2% in the Cardoso administration and 5.2% in the Lula administrationⁱ, similar to that observed in the first Cardoso government (5.1%).

As it is known, changes in the poverty rate occurring in the 1993-1995 period are associated to the implementation of the *Real* Plan. What are then the characteristics that can be associated with the shift in poverty observed between 2003 and 2005? In particular, how did growth and inequality interact in these two periods? Which public policies—such as changes in the macroeconomic regime (*Real* Plan, inflation targets, among others) and changes in social policies (Bolsa-familia, minimum wage adjustments, etc.)—explain these shifts in poverty? What are the specific channels that enable these policies? These are some of the questions addressed by the present research.

In broader terms, Brazil was the country that displayed the highest inflation worldwide, from 1960 to 1995. Since the start of the eighties, controlling inflation became the focus of public policies in Brazil. Throughout the last 25 years, changes in these social indexes have captured the volatility of the Brazilian macroeconomic environment: until 1994, the sources of instability were the successive attempts of stabilization and their failures, while from 1995 onwards, the main source of instability was the arrival and departure of external crises. Similarly, Brazil has been notoriously known as one of the countries that has the highest income inequality in the world. Following its steep ascension in the sixties, Brazilian inequality has been persistently high, but it had remained stable between 1970 and 2000. However, in recent years, particularly after 2001, inequality has been declining, which has brought the inequality rate to the lowest levels of the past 25 years, more specifically since 1976, when the PNAD series started to be processed. Affirming that the former decade was one of inflation stabilization, we can likewise state that—until this time—the current decade is one of income inequality reduction. The main theme in this study is the moments of inflection for both inflation and inequality, where Brazil occupies an unique spot in international statistical series and in the analysis of poverty and social welfare.

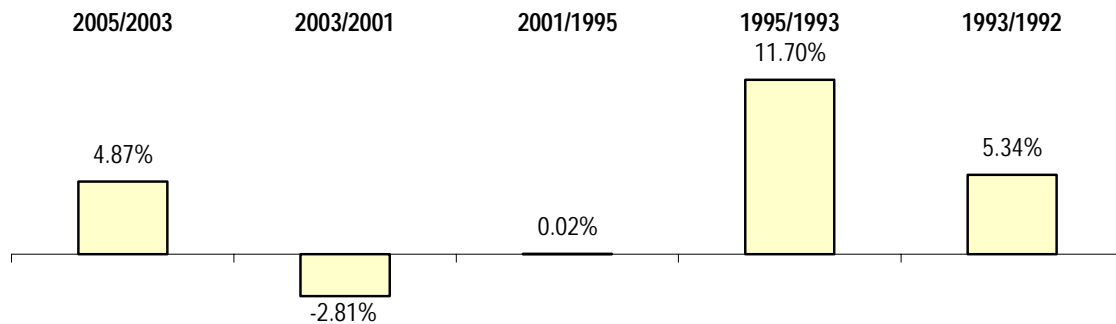
The Distribution Dance

We work here with the concept of income distribution in the statistical sense, including changes in inequality as well as movements in income growth (household income per capita—that is, the sum of all income from all household members divided by the household population).

The main feature of this approach is its level of decomposition according to three groups of income: the tenth richest who withholds almost half the 2005 per capita income (more precisely, 45,1% mean income R\$ 1877); the half poorest who has a little bit more than a tenth of the national income (14,1% R\$ 123); and the 40% intermediate one whose share of the population and of the income virtually coincides (40,8% R\$ 440 mean) – which makes Brazil an average income country, like Peru, halfway between wealthy Belgium and poor India. This approach by income groups (Belindia or Belperdia) contrasts with the one based on per capita GDP where the weight is proportional to each person's income - individuals implicitly "are worth what they earn". The marked inequality of income in Brazil does not allow a reliable calculation of its average and for a sound social welfare, hence the importance of this aspect for the discussion of the Brazilian case.

We are proposing here a timeframe that divides the 1980-2005 period in five phases: a) institutional uncertainty and chronic inflation pre-1995 (July 1994); b) post-inflationary stabilization boom 1993-1995); c) critical uncertainty from external shocks (1995-01); d) uncertainty in relation to the external situation and internal political changes (2001-2003); and e) post-"confidence shock" boom (2003 onwards).

Annual Variation of Mean Income - Brazil



Source: CPS/FGV processing PNAD/IBGE microdata.

There is a period, before the *Real* Plan, of chronic uncertainty, when the population was used to living with the instability caused by persistent high inflation rates and the successive implementation of economic plans. Agents and institutions developed a series of mechanisms to hedge against inflation, whose main collateral effect was to perpetrate inflation. This phase encompasses various periods that are marked by successive economic and stabilization plans. A reverse “economic miracle” occurred during the Collor administration at the beginning of the 1990s. Income fell sharply but affected, mostly, the richest 10% (-11,8% against -4,4% of the 50% poorest, per year). The Collor administration reduced inequality by equaling incomes according to its lowest levels. The second period (1992-93) as shown in the graph is marked by growing inflation rates and a meaningful increase in income only for the richest (12,3% and -1,6%, per year, of the poorest) resulting in a strong rise in income concentration.

The next phase (1993 a 1995) can be classified as the honeymoon with the *Real* Plan. The income from all segments of the population was raised by 12% per year, in a real “economic miracle” fashion. Chronic uncertainty was very quickly removed from the economy – creating important welfare gains – being replaced by a period of euphoria and an economic and social boom.

Afterwards, the country plunged into a phase of exposure to external shocks. This period presents an uncertainty of a different nature to that of the high inflation period. It is instead a critical uncertainty regarding an upcoming acute crisis. Figures show that the poorest were spared, but the remaining groups presented income falls of 1.1% between 1995 and 2001.

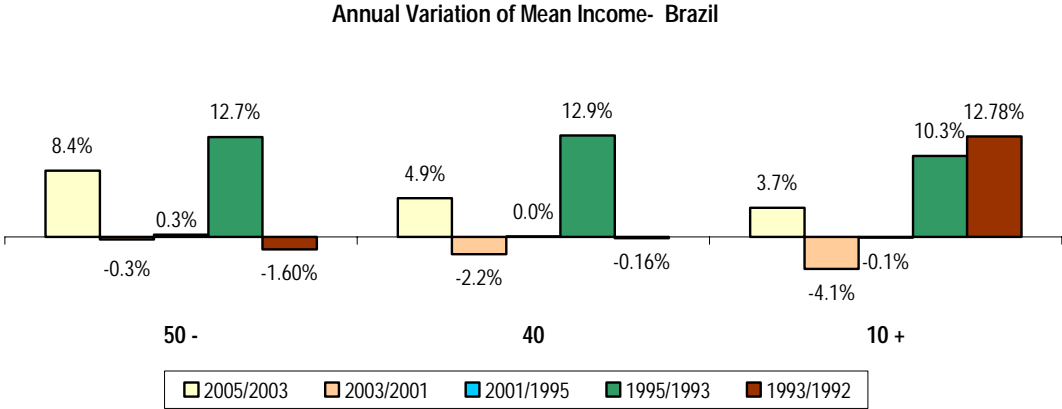
A great economic deterioration similar to the Asian and Russian crisis (1997 and 1998, respectively) became a possibility in Brazil. In aggregate terms, there was the possibility of a shock of considerable proportions. Long-term unemployment became a possibility for many citizens. These were not micro or macroeconomic shocks as in the chronic inflation period, but instead of atypical shocks of an unknown nature. In 1999, Brazil was hit by the crisis whose impacts were not as devastating as expected. Rises in inflation and unemployment that followed the currency de-valuation were not as high as general expectations.

On the other hand, the analysis of the income distribution during the external crisis period (1995-03) is very heterogeneous in Brazil, depending upon the indicators. The crisis was serious, for instance, when observing only labor income in the greater metropolitan areas. It is less serious though if all sources of income and geographical areas are analyzed, thus approaching a wider welfare concept.

The dissolution of the critical uncertainty in 2000 contributes to an increase in direct domestic and foreign investments and an increase in formal employment, which are hit by the internal successive energy crisis, the Argentina crisis and the American recession in 2000 – but that is a different story.

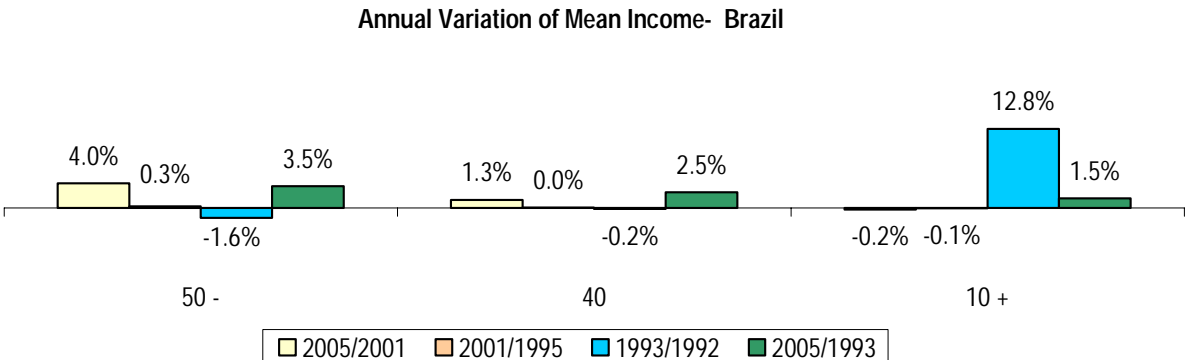
The 2001-2003 period was marked by losses in income with a reduction in inequality. Despite affecting all the segments from the population, these losses were more pronounced for the lowest income groups - -0.3% against -4.1%, of the richest (-0.6% and 7.9% accumulated in the period).

In the more recent period (2003 to 2005), the total annual growth was 4.8%, spread unequally amongst the segments of the population. The poorest sectors gained more, with annual increases of 8.4% in income (as opposed to 3.7% of the richest tenth and 4.9% of the intermediate group).



Source: CPS/FGV processing PNAD/IBGE microdata.

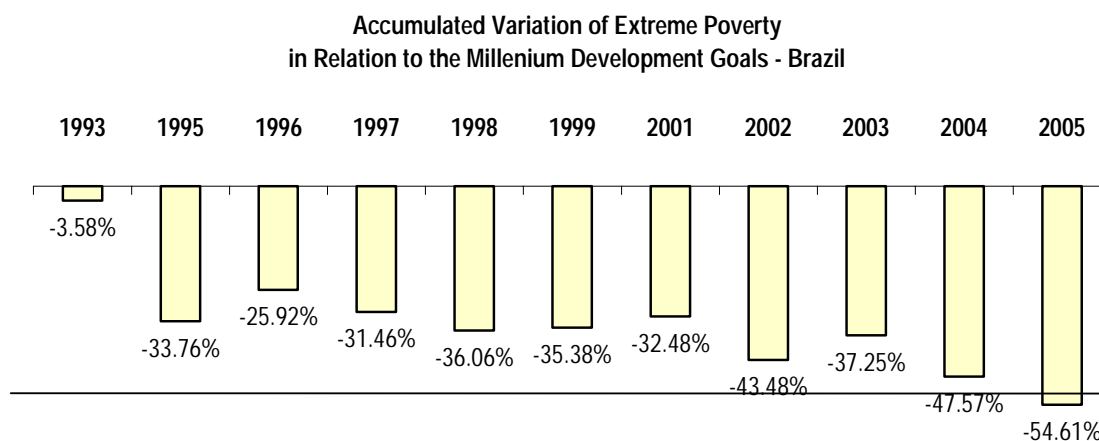
Other periods can also be analyzed in the graphs below. The richest 10% were the only losers from 2001 and 2005 (a decrease of 0.2% vis-à-vis a 4% gain for the poor). In the last 12 years, all groups have experienced gains of 1,5% to 3,5% per year for the richest and the poorest, respectively.



Source: CPS/FGV processing PNAD/IBGE microdata.

Accomplishment of the Millennium Development Goals

Apart from the Poverty Gap by the Center for Social Policies at the Fundação Getulio Vargas, we have monitored poverty according to the line established by the first Millennium Goal to reduce poverty by half between 1990 and 2015: US\$ 1 per day, adjusted by differences in living costs among countries and within Brazil (in this case, we have also used the deflation rates from POF 2003). In 2005, extreme poverty also reached its lowest level: 5,32% of the Brazilian population with per capita household income below this amount. Data show that the accomplishment of the first goal in half the foreseen time (25 years), that is 12 or 13 years counted since 1992 in order to maintain the methodological consistency of the PNAD questionnaires, as opposed to the 1990 benchmark. Since 1992, the accumulated reduction of poverty until 2005 was 54.6%. In three years, (1992-1995) there was a total reduction of 33.76%, but in ten years (1992-2002) this only increases up to 43% of total poverty. The last boom went beyond the accomplishment of the Millennium Goal with an accumulated decrease of 54.6%. That is, the lifetime of extreme poverty in Brazil should have been 25 years, according to international agreements, but lasted approximately half this time. The graph below shows the accumulated reduction year on year.



Source: CPS/FGV processing PNAD/IBGE microdata.

Future Scenarios

The research creates some scenarios about the poverty in Brazil: if the economy grows 4.5% per year for consecutive years, without any changes in inequality, the proportion of extreme poor people in Brazil (individuals who earn less than R\$ 121 a month) will fall from 22.77% in 2005 to 19.74%, a 13.28% decrease. This means that millions of Brazilians will cross the poverty line this year, if the country changes its current expansion into a process of sustained growth, which has not been seen in Brazil since the last economic miracle. But the real social miracle would happen if all the growth came hand-in-hand with a reduction in inequality. For instance, if in the next four years Brazilian inequality keeps its descent trend of the last four years (since 2001) the proportion of extreme poor would fall by 34%.

Poverty Scenarios

		Per Capita Household Income	% Extremely Poor	Variation
Brazil 2005		437,44	22,77	
<i>Growth Effect*</i>				
	3%	450,56	21,94	-3,62%
	12%	489,93	19,74	-13,28%
<i>Inequality Effect (RJ) **</i>				
	<i>growth rate*</i>			
	0%	437,44	21,82	-4,18%
	3%	450,56	20,85	-8,44%
	12%	489,93	18,23	-19,94%
<i>Inequality effect (BA) ***</i>				
	<i>growth rate*</i>			
	0%	437,44	18,14	-20,33%
	3%	450,56	17,40	-23,58%
	12%	489,93	15,01	-34,05%

Source: CPS/IBRE/FGV from PNAD/IBGE microdata

* Per capita income growth

** We have replaced Brazilian inequality rates by Rio de Janeiro inequality rates in 2004 (Gini drops from 0,568 to 0,561)

*** We have replaced Brazilian inequality rates by Bahia inequality rates in 2004 (Gini drops from 0,568 to 0,548)

The Two *Reais*: Poverty, Inequality and Growth

The two episodes of poverty reduction that occurred in 1993-1995 and 2003-2005 present similarities and differences. We begin with the approximate causes of poverty and social welfare, whose measure is based on the concept of per capita household income, namely: growth and equity. The concept of per capita household income summarizes a series of effects that happen both in public policies and in private life (labor market, capital gains, etc.) including also employment and self-employment, pensions, benefits, social programs, rents, private transfers (child support allowance, etc.) interest gains, etc.

Per capita household income is interesting as it provides a synthesis upon which we calculate the average and the inequality by a most popular index—Gini, which varies between 0 and 1, 1 being the closest to inequality. Gini's lowest limit refers to a perfect equity case, where everybody would have the same income; in its highest limit, we would experience the perfect inequity where one person would hold all the income from society, while the rest would have zero income. In order to understand the seriously high level of inequality of the Brazilian income distribution, which is 0.568%, it is fair to say that we are closer to perfect inequity than to a situation where everyone is the same.

In our calculations, we have considered all people with null income—which can cause some detachment from the IBGE series referring to the average and the revenue inequality, as these series only consider the occurrence of positive income for each concept. Implicitly, the Gini index gives more weight to those people with lower income and the greatest weight to those with zero income.

Sen's Social Welfare Measure

In order to provide a final synthesis, we have included the effects of the mean income and inequality in a social welfare function proposed by Amartya Sen, who won a Nobel Prize in Economics. For instance, the mean income of 437 reais per Brazilian would be the value of social welfare according to Sen's simple measure if there was total equity, but it corresponds in reality to 43.2% of this amount, or 189 reais, given Brazil's extreme inequality nowadays. The table below shows the

Household Income Per Capita			
	Mean Income	Gini	Welfare
1992	320.1	0.58	133.4
1993	337.1	0.61	132.6
1995	420.7	0.60	168.5
1996	427.3	0.60	170.1
1997	430.8	0.60	172.1
1998	437.7	0.60	175.0
1999	412.9	0.59	167.8
2001	421.1	0.60	170.2
2002	422.3	0.59	173.8
2003	397.8	0.58	165.9
2004	410.2	0.57	175.7
2005	437.4	0.57	189.0

Source: CPS/FGV processing PNAD/IBGE microdata.

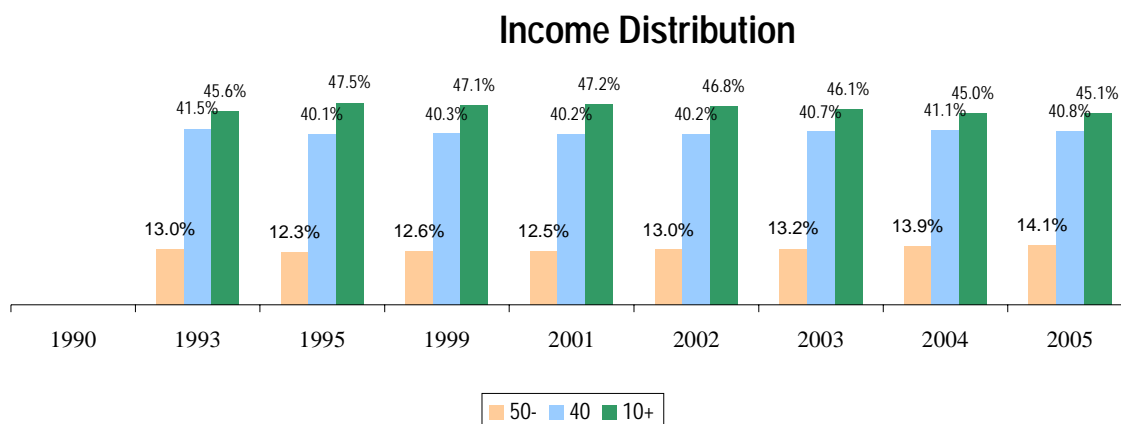
evolution of the mean income, income inequality per year and the combination of both, as given by the welfare measure proposed by Sen.

The table shows the mean income and Sen's welfare synthetic measure growth from 1993 to 1998, both at 2005 constant prices, with special emphasis on the 27% growth observed between 1993 and 1995, when the mean income has a substantial increase while inequality decreases to a lesser extent. In the following period, mean income goes through serious oscillations, finally recovering its 1998 value in 2005. Income increases after the 2003 recession and inequality presents a marked reduction after 2001. This redistribution rarely predominates in Brazilian historical social series. The reduction in the inequality of household per capita income that occurred in 2004 is approximately equivalent to that one from the 2001-2003 period, when the Gini index decreased from 0,596 to 0,583, pacing it down in 2005. In the last year, the rhythm of income de-concentration é less than a third of that in 2004, but it is still atypical for the Brazilian historical series that used to point to a chronic case of inertial inequity.

Inequality

Brazilian internationally infamous inertial inequality, which remained fairly stagnated in the previous decade - hence justifying its name - then changes and begins to fall consistently since the beginning

of the millennium. The 50% poorest share increases from 12,5% to 14,1%. The 10% richest share, in turn, falls from 47,2% to 45,1%. We can see the variation in various sectors of distribution.



Source: CPS/IBRE/FGV processing microdata from PNAD/IBGE

Focusing solely on the last year: the graph shows that the share of the 10% richest in income falls one percentage point (from 45,7% in 2003 to 44,7% in 2004). The share of the 50% poorest increases 0.6-percentage point (13,5% to 14,1%). The 0,4% difference is explained by an increase in the share withheld by the 40% intermediate (from 40,8% to 41,2%). That is, the middle-class in the statistical sense – i.e. those with mean income, 40% who receive 40% of the income – have also gained income.

Who's in whom in income distribution: the PNAD data show those who were the main winners and losers in the distribution dance. Between 2004 and 2005, all won, since the Brazilian mean income, as per PNAD, increased 6.6% in 2005 vis-à-vis 1% GDP per capita growth in the same year. However, inequality decreased meekly—0.6%, well below the drop in the previous three years –1.9% in 2004, -1% in 2003 and –1.2% in 2002. In 2005, the income of the 50% poorest increased 8.56%, the share of intermediary 40% increased 5.74% and the income of the wealthiest 10% increased 6.89%. In 2005, the poor did not experience their loaf of bread falling with the butter face down, nor did the rich witness their croissant with imported jam fall either.

The table below captures the distribution dance for these groups in a yearly fashion throughout the current decade.

	GDP per Capita	Household Income per Capita	Poorest 50%	40% Middle	Wealthiest 10%
2002	0.45%	0.30%	3.65%	0.34%	-0.68%
2003	-0.91%	-5.81%	-4.15%	-4.67%	-7.32%
2004	3.43%	3.14%	8.34%	4.13%	0.68%
2005	0.83%	6.63%	8.56%	5.74%	6.89%

Source: CPS/FGV - PNAD/IBGE and National Accounts

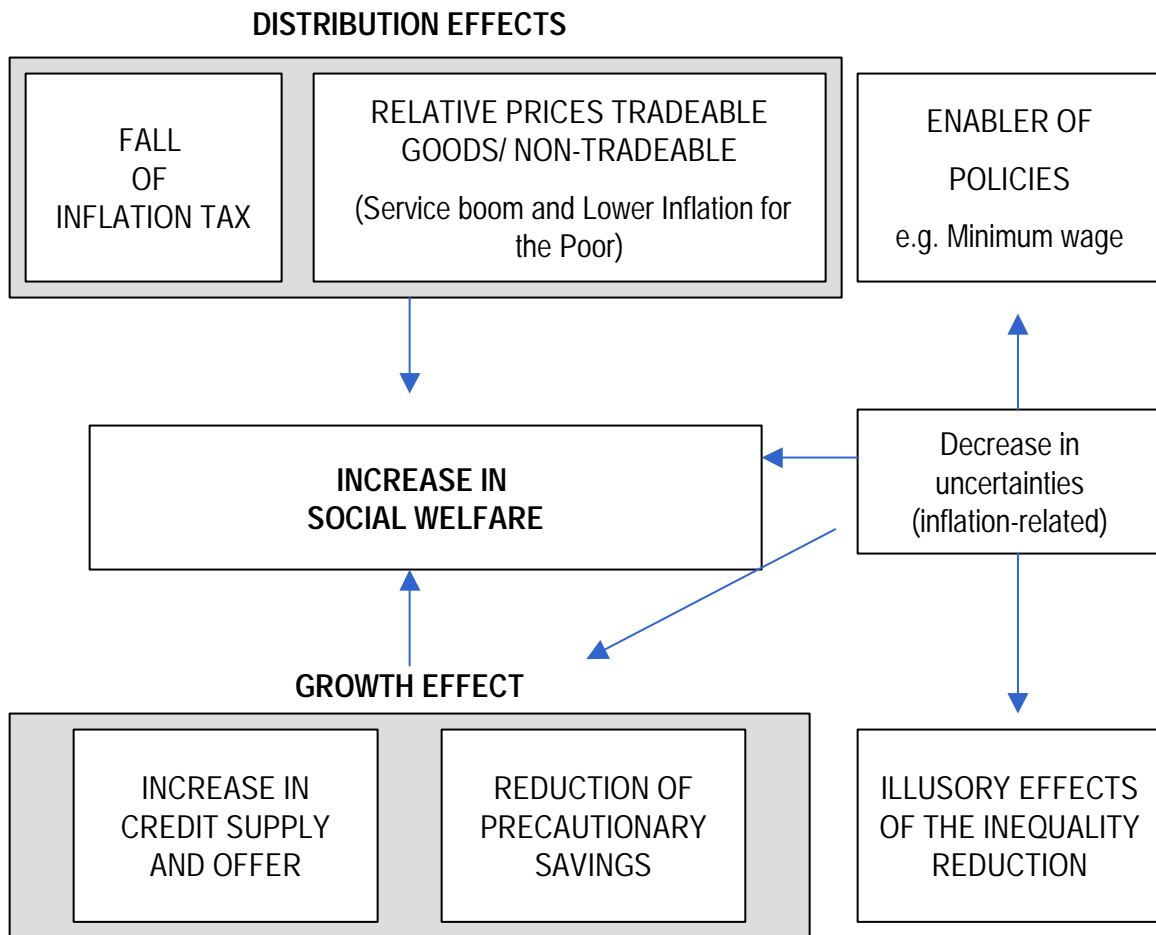
The Two Reais: Determining Factors

As in marriages, the relationship between Brazilian society and its policy makers has its highs and lows. We have analyzed these fluctuations, according to a distributional perspective.

The *Real*/Honeymoon (1993-95)

In the period leading up to stability, and contrary to what has been affirmed, *Real* had a relatively small impact in the reduction of inequality. The research that supported the Real Plan and the stabilization plans which preceded it sought to reduce inflation by maintaining the status quo of income distribution at fairly constant levels. The URV period, between February and July 2004 – a kind of “engagement” with the new currency – intended exactly that. Real was conceived – and successful – to fight inflation. The great gain of social welfare that resulted from the stabilization was not a fall in inequality, but – as the name itself suggests – an increase in the stability of individuals income. This reduction in uncertainty led to illusory effects of reduction in the differences between incomes, but more importantly, it improved the conditions for social policy planning and implementation, as well as conducing to a post-stabilization economic boom. The scheme below presents the effects of the Real Plan on poverty (and social welfare) and the respective channels of growth, equity and associated stability.

REAL EFFECTS



After the launch of the Real Plan we had, alongside a reduction of the inflation, a welfare gain associated to the lower incidence of the inflation tax, especially on lower income groups' income. Simulations of this effect show an increase of 10% in the income of those who do not have access to sophisticated financial mechanisms and a reduction of 5% in poverty. This is one feature of the stabilization, but it explains only a small share of the social gains observed after the Real.

A second effect refers to the type of stabilization. It set the exchange rate, opened up the economy and a consumption boom occurred. The measures benefited the non-tradable goods sector, as services, whilst it worsened the tradable goods sector, as manufacture. It is indeed the service sector that employs the greatest number of poor people. There was thus a great impact in reducing poverty. This explains why some regions, like Rio de Janeiro, benefited more than others, such as São Paulo.

The third and main effect, directly linked to the stabilization, is the reduction in uncertainties. There are direct social welfare gains in this transition from chronic uncertainty to a stability period, as it becomes possible to plan for the future. Stabilization also increases the families demand for credit (negative savings), which can in turn become less careful towards the future and feel free to

consume and ask for credit. On the other hand, banks and finance companies tend to feel more confident about monitoring their potential debtors. The market of direct credit for the consumer flourished after the Real Plan, be it for supply for demand reasons.

Real's main gain was to bring stability to everyone's income. We have calculated that based on the PME-IBGE data that follow families through time and have concluded that the volatility of the monthly household income fell around 40% with stabilization.

The effect of this reduction in volatility is contagious to other inequality measures. It seems that inequality fell more because the economy is more stable, monthly income inequalities – which is what is measured in Brazil – are inflated by this fluctuation. If the mean income in a given economy is the same through time – an egalitarian economy by definition – but where incomes fluctuate at different moments, then inequality will appear to be greater than what actually is. The reduction in these fluctuations produced an illusory redistributive effect of the Real Plan. The inequality in monthly incomes falls three times more than the income inequality during consecutive four months. This difference corresponds exactly to the effect of the reduction in income instability. To sum up, it appears that inequality has fallen, but in effect the instability of individual income actually fell.

The direct redistributive effects of the Real Plan were not great, but its stability created the possibility of making social policy in a much better fashion than before. Governments and private agents, including companies and workers, could plan further down the future. It also became easier for governments and for families to implement their respective budgets, with the increase in stability and the end of inflation tax.

The Real Plan enabled social policies, but it is not in itself a great social policy. It is necessary to differentiate the necessary conditions from the sufficient ones. Real's objective was not to redistribute income, but it ended up enabling the implementation of distributive policies. In this sense, it does not make much sense to argue over who is the "father" of the Real's immediate distributive benefits, because they were still to come.

According to the PME, the bulk of the liquid reduction in poverty (55%) from the post-Real period occurred exactly in May 1995, nine months after the stabilization. It may have been just a long pregnancy until the stabilization benefits could be born. In a more realistic way, the 10,56% reduction in poverty would relate more strongly to the 43% adjustment of the minimum wage, from the same date. The mistake seems to be the emphasis placed on Real's direct distributive effect. The greatest gains was the reduction in uncertainties and the associated growth boom, without mentioning the improvement in the implementation of distributive policies as the increase of the minimum wage illustrates.

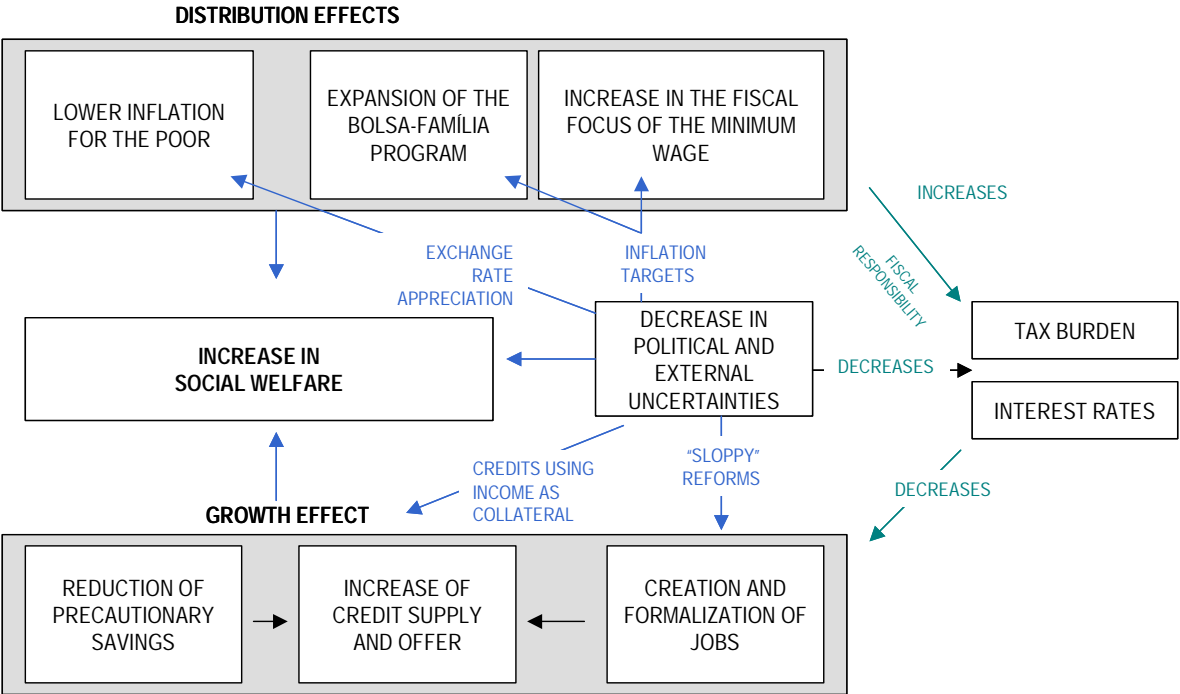
The Second Honeymoon (2003-2005)

As we mentioned before, since its recovery from the 2003 recession, Brazil has lived a period of poverty reduction of similar magnitude to that of the Real Plan. Next, we present a systematic look at the main effects of the poverty reduction and the increase in social welfare, observed in recent periods.

The new administration gave markets a “confidence shock” at the beginning of 2003, mainly by keeping intact the three pillars of the macroeconomic regime, relying once more on high real interest rates. The launch of Fome Zero program at the beginning of this administration meant an initial break with the income transfer policies that were gradually implemented. The results of what could be perceived as a lack of adjustment in social policy combined with the social costs from the macroeconomic adjustment led to the 2003 stagnation and an increase in poverty.

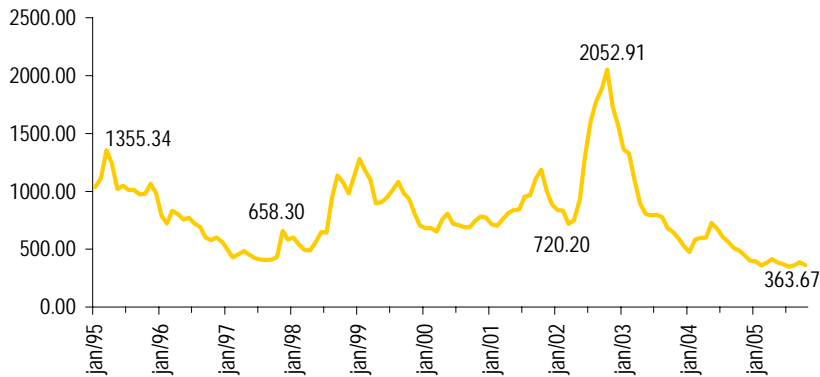
The analysis of this reduction in income instability in both episodes draws considerable attention in the current economic and social debate. Here we argue that the existence of a number of effects that resulted from the reduction in uncertainties between 2003-2005, although of a different nature from the stabilization case. The last one is related to the reduction in the critical uncertainties during the rapid and persistent transition towards lower inflation rates. In the recent case, we have observed the effect known as Lula’s administration “confidence shock”, whose main idea was conveyed by the “Letter to Brazilian Citizens” written before the 2002 elections. In reality, Lula’s great economic plan was that he did not have a plan. Several indicators that capture risk, such as the exchange rate and the so-called “Brazil Risk” measured by C-Bond spread, pointed in that direction.^v

THE “SECOND REAL” EFFECTS



* Loss of labour effectiveness

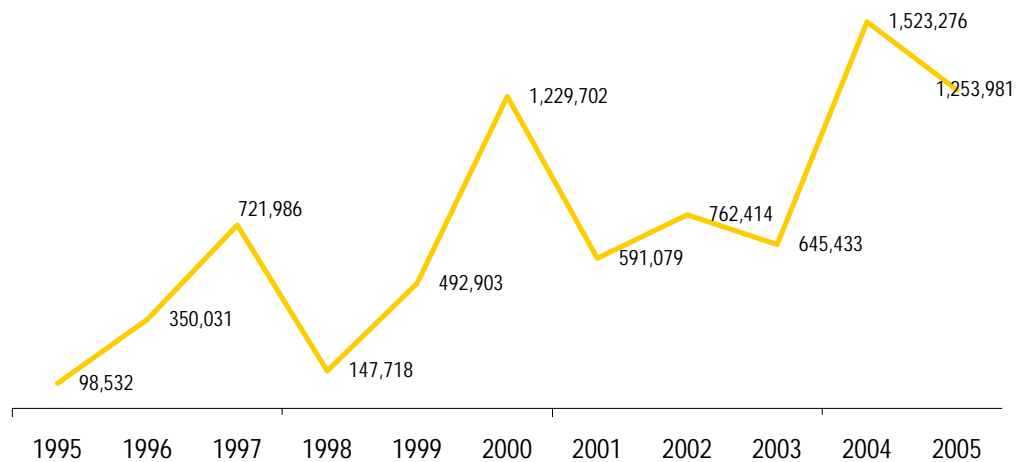
C-Bond Spread - Monthly



Source: CPS/FGV - Bacen

The fall in these risk-related indicators was not the only one observed, but also the increase in formal employment between 2004 and 2005 is one of the main features of this period – which could be mean an improvement in the perception of risk by entrepreneurs^{vi}. Only sustainable expansions translate into formal employment, in view of the inherent redundancy costs. One of the main pieces of this puzzle, associated with recent social changes, was the doubling of formal employment from 600.000 in 2001-03 to 1.2 million in 2004-06, as the graph below shows.

Formal Jobs Created - Annual



Source: CPS/FGV processing CAGED microdata.

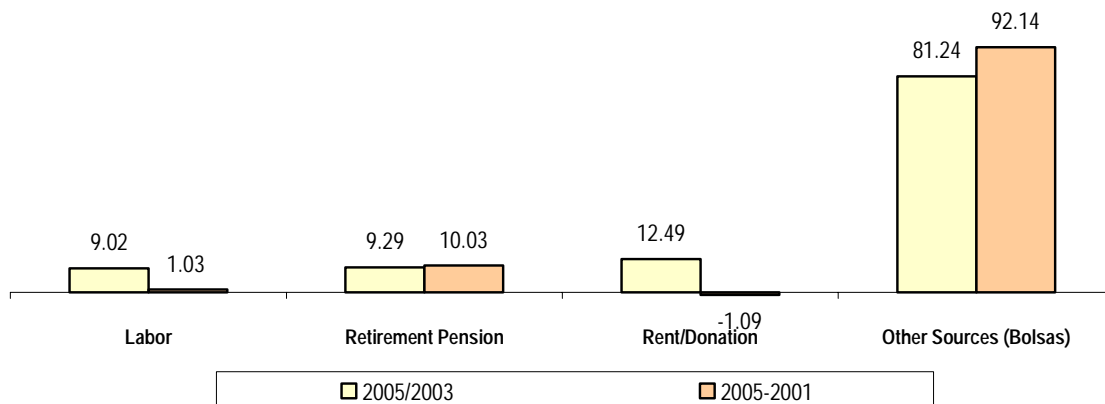
Other risk-sensitive indicators range from an increase in the provision of personal credit to an increase of 8% in the number of marriages in 2004 – although in these cases it is necessary to also observe the institutional determinants of these changes. The abrupt reduction of risk in models of precautionary savings caused a definitive leap in the consumption series with the lowest growth rates in the following periods.

In October 2003, the government launched the Bolsa-Família, which followed the same pattern as previous governments' social programs, only expanding the number of beneficiaries and the average size of the benefit itself, plus additional improvements, namely: increased benefit to the poorest; unifying the beneficiaries records into one system, thus ensuring more transparency and credibility before society. In 2004, Brazilian economy experienced good improvements, as the GDP grew at 4.5% and poverty kept falling. It is important to note that, despite the instability in GDP growth in the 2001-2004 period, inequality fell during this period, especially between 2003 and 2004.

On the social front, the minimum wage increased effectively by 75% from 1995 to 2004 – and 94% until 2006. The minimum wage is also used as the basis for various income transfer policies, particularly indexing social security benefits and influencing eligibility criteria. In 1995, social programs expenditure had already reached 50% of all the social expenditure in Brazil and 11% of the GDP. In 1998, there were progressive adjustments to income transfer benefits – which were not, however, particularly noted, since no legislative reform or constitutional change enabled them. Since 2000 when the Poverty Eradication Fund was created, there has been a gradual implementation of federal government programs by those municipalities with the lowest Human Development Index. The expansion of these focused and conditioned income transfer programs, like *Bolsa-Escola*, and now *Bolsa-Família*, have helped to combine compensatory and structural components. The availability and expansion of social safety nets since 2000 have generated a pro-poor impact in many instances. The social impacts of this new generation of income policies have not yet been validated because (i) changes in the social program benefits and (ii) the knowledge about programs targets have been gradual and relatively recent.

In the graph below, it is possible to observe some changes in the share of different income sources in the total household per capita income, during the "Second Real". Even with real increases of 9.02%, labor income's share in the total amount. Conversely, the Bolsa-Família effect is evident in the income gains from this period, since in 2005 *Bolsa*-related income represents 1,77% of the Brazilian citizens' total income (opposed to 0.95% in 2001). It has had a real variation of 92.14%, of which 81,24% occurred in the last three years (when income grows from R\$ 4,29 in 2003 to R\$ 7,78 in 2005). Finally, social security keeps its share of 19% in the total income, with increases of 10% in income in this period.

Variation (%) According to Income Source - Brazil



Source: CPS/FGV processing PNAD/IBGE microdata.

It is important to bear in mind that the adoption and expansion of a new regime of income policy (without ending the old regime) based on the expansion of new targets for the income transfer programs financed by Federal Government leads to an expansion of public expenditure, which in turn has led to an increase in the tax burden of 10 percentage points of the GDP since 1995, reaching around 38% at the end of 2005. High real interest rates also contributed to an increase in the Brazilian public debt up to more than half of its GDP.

Conclusions

Brazilian macroeconomic policy has been extremely successful in controlling inflation. A good share of this success is due to a pragmatic attitude, which focuses on tangible objectives. The adoption of inflation targets performs a fundamental role in this current process: firstly, by coordinating the design of public policies within the government; and secondly, by informing society about the government's priorities. These commitments helped to reassure financial markets and the formation of prices on the real side of the economy. The potential benefits of a well-informed economic environment should not be underestimated. Nevertheless, this macroeconomic success in the making has not resonated among the Brazilian citizens. The ordinary citizen, contrary to the markets, is less sensitive to the financial deficits than to the "repayment" of the social "debt".

It is suggested then that the government uses the credibility that resulted from the accomplishment of macroeconomic targets in its social policy. The government would then define its own targets in relation to long-term social indicators. The objective is to rationalize the public debate by adopting budgetary restrictions for social priorities. The greatest failures in the social area are the lack of mechanisms for dialogue.

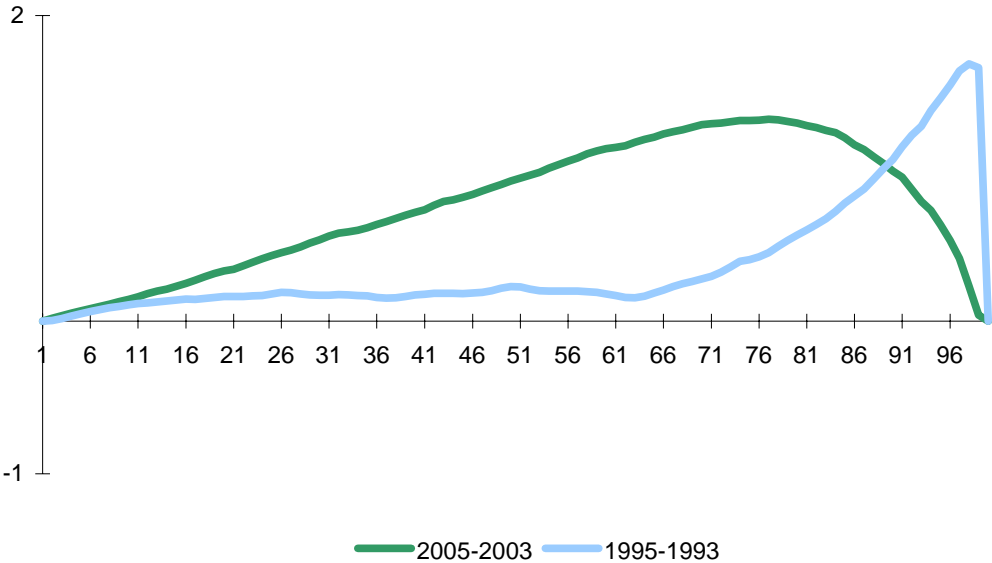
It is reasonable to affirm that just as the previous decade referred to economic stabilization (and of the wide access to primary school) the present one has referred – up to now – to a reduction in income inequality (and the creation of formal employment). In this sense, it does not make much sense to argue over who is the "father" of the recent distributive benefits. Stability, in itself, does not

ensure the achievement of sustainable human development - just as a couple's fidelity does not lead to a happy marriage. It is necessary to differentiate the necessary conditions from the sufficient ones.

How encompassing are the results?

Could it be that the social indicators presented here are also valid in view of other poverty lines and indicators of inequality? In relation to the latter, despite the discrete improvement in 2004 and 2005 inequality indicators as Gini and Theil, the distribution of per capita income in 2005 is not necessarily more egalitarian than in 2004. The decrease in some inequality indicators is not the same for all inequality indicators that can be used. The per capita family income distribution in 2005 prevails in the Lorenz curve the 2003 distribution, boosted by the marked reduction in inequality in 2004. Similar qualitative results are obtained when comparing the income inequality in 2005 and 2002, and in 2005 and 2001. In fact, the difference in the curve tends to increase as we move towards the end of the decade, but the greatest move in distribution occurred between 2004 and 2003. The comparison, which interests us the most refers to the distances between Lorenz curve of 1995-1993 and 2005-2003, respectively. The graph shows that the greatest move occurred in the second period.

**Distance of the Lorenz Curves - 2003 to 2005 and 1993 to 1995
Household Income Per Capita**



Source: CPS/FGV processing PNAD/IBGE microdata.

Mean

Data for per capita household income growth from PNAD information and the per capita GDP are markedly different in terms of growth rates in several periods, with a special emphasis on those

periods of greatest interest namely 1994 and 1995 – the latter captured by cross-data. What interests us most, however, is the last bi-annual period, in particular 2005. In this year, per capita GDP grew at Haiti-like rates (0.83%) whilst PNAD-based per capita household income growth was 6.6%, closer to emerging countries rates, such as India.

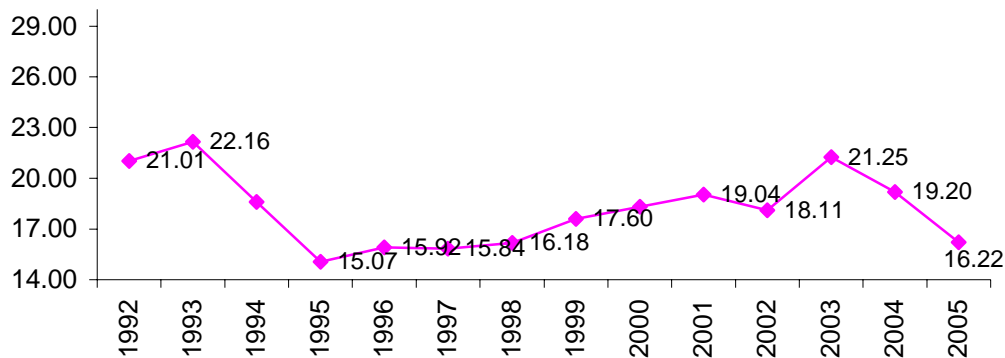
	Household Income per Capita	GDP per Capita
1993	5.34%	3.26%
1994	12.38%	4.20%
1995	11.02%	2.62%
1996	1.59%	1.10%
1997	0.82%	1.72%
1998	1.59%	-1.36%
1999	-5.66%	-0.71%
2000	0.99%	2.82%
2001	0.98%	-0.17%
2002	0.30%	0.45%
2003	-5.81%	-0.91%
2004	3.14%	3.43%
2005	6.63%	0.83%

Source: CPS/FGV - PNAD/IBGE and National Accounts

Rural, Urban and Metropolitan Trends

The metropolitan areas (compared to urban and rural) are the places that present the greatest relative growth in poverty between 1995 and 2003 – 41% - reflecting the metropolitan crises. In the following periods, however, metropolitan areas had the best relative performance, falling 23.7% in 2003 and 2005 and 32% between 1993 and 1995. In fact, except for the 1993-95 and 2003-05 periods, poverty in big metropolitan areas increased in all the years. After a steep fall during the Real Honeymoon period – when poverty fell from 22,16% to 15,07% - poverty increase again in 2003 to 21,25%, in an uninterrupted trend up to 2005, when it reaches 16,22%

Metropolitan Poverty Brazil



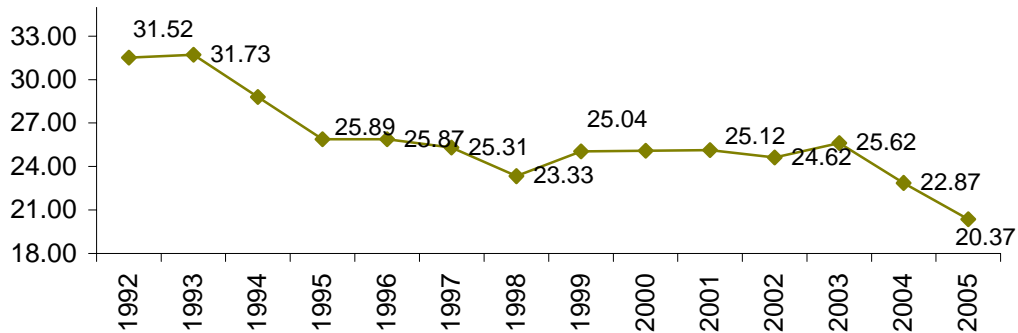
Source: CPS/FGV processing PNAD/IBGE microdata.

OBS: 1994 and 2000 are averages of adjacent years, since in those years PNAD did not collect field

* Defined as the share of the population with per capita income below 121 reais, in today's prices in São Paulo metropolitan área, adjusted for regional differences based on living standard costs. See section on Methodology.

Urban areas – which reflect the good performance of intermediate sized cities – presented the greatest accumulated reduction in poverty from 1993 to 2003 of 35.8%, outperforming metropolitan and rural areas, whose reduction rates were 26.8% and 27.2%, respectively. Both in its level as in its annual variation, urban poverty follows the same pattern as in the rest of the country, including the reduction pattern for election years, as in 1998 and 2002. From 1993 to 2005, there was a systematic fall in urban poverty from 31.52% to 20.37%.

Urban Poverty Brazil



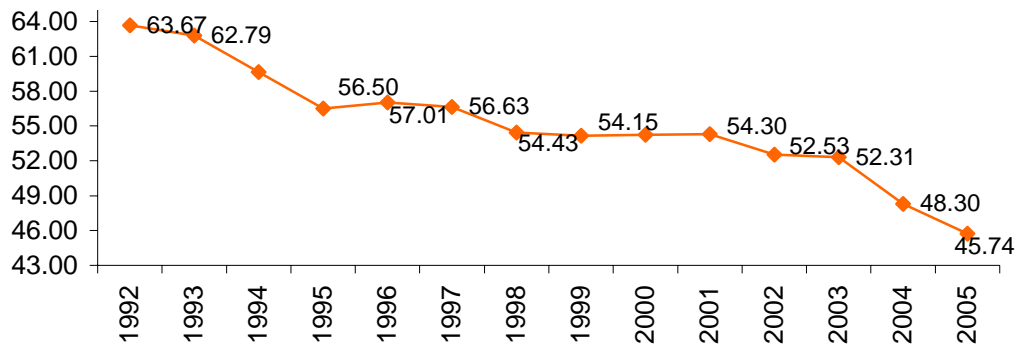
Source: CPS/FGV processing PNAD/IBGE microdata.

OBS: 1994 and 2000 are averages of adjacent years, since in those years PNAD did not collect field

* Defined as the share of the population with per capita income below 121 reais, in today's prices in São Paulo metropolitan área, adjusted for regional differences based on living standard costs. See section on Methodology.

Rural areas performed more constantly in the various sub-periods. Rural poverty falls systematically in almost all the years in the series, including droughts in the Northeast that happened in 1998 and 2001. This pattern was influenced by rural-focused public policy in particular income transfer programs.

Rural Poverty Brazil



Source: CPS/FGV processing PNAD/IBGE microdata.

OBS: 1994 and 2000 are averages of adjacent years, since in those years PNAD did not collect field

* Defined as the share of the population with per capita income below 121 reais, in today's prices in São Paulo metropolitan área, adjusted for regional differences based on living standard costs. See section on Methodology.

The PANORAMA Description

General Information

It is a tool used to measure the annual evolution of poverty and income (mean and medium) since the beginning of the 1990s. It displays this information based on per capita household income by different population groups.

It selects the type of analysis:

- Poverty (CPS /FGV Line)
- Poverty (U\$\$ 1 – PPP line)
- Mean Income
- Medium Income

The screenshot displays the 'Panorama da Miséria Nacional' web application interface. The header features the FGV logo and the title 'Panorama da Miséria Nacional - Todas as Fontes de Renda - 1992 - 2005'. Below the header, there is a dropdown menu for 'Análise' set to 'Miséria CPS'. Three buttons are visible: 'Gerar Tabelas', 'Limpar seleção', and 'Selecionar todas'. The interface is divided into three sections: 'Características Demográficas' (with checkboxes for Population Total, Years of Study of the head, Immigration, Sex, Color or Race, Age Group, and Position in Family), 'Características Sócio-Econômicas' (with checkboxes for Position in Occupation, Time in Company, and Maternity), and 'Características Espaciais' (with checkboxes for Type of City, State, Local of Residence, Metropolitan Region, and Geographical Region). At the bottom, there are three more buttons: 'Gerar Tabelas', 'Limpar seleção', and 'Selecionar todas'.

The Cardoso administration begins in January 2005. It would be natural to use October 1994 data, when PNAD was implemented. As there was no survey in 1994, we have chosen to use 1993 data as the beginning of the term – once PME data indicate that the greatest reduction in labour poverty between 1993 and 1995 occurred in 1995

ii The Cardoso administration begins in January 2005. It would be natural to use October 1994 data, when PNAD was implemented. As there was no survey in 1994, we have chosen to use 1993 data as the beginning of the term – once PME data indicate that the greatest reduction in labour poverty between 1993 and 1995 occurred in 1995.

iii In other words, beyond its real channels, inflation also affects the measurement of inequality in a spurious way. That is, the coincidence between inflation and inequality peaks is not casual in Brazil in 1989 and 1994, but measurement errors. As nominal income is received in different moments this would require deflation with distinct timing for different income types (for more details, see Néri: 1995).

iv Technically similar to Cagan classic definition, monthly rates above 50% for at least 6 months. The inflation in the semester preceding the Real was on average % a month, with relative stability, opposed to the European classic hyperinflations of the 1920s of a more explosive nature..

v

vi

vii For instance, all the FGT indicators such as proportion of poor people (P0), Poverty Gap Index (P1) and Poverty Severity Index (P2). We are not implementing a spatial deflation in this dominance analysis – see Appendix.

viii The same poverty dominance occurs in 2001 and 2002, and consequently from 2001 to 2004. When PNAD 2002 figures were released in 2003 they received little attention. Poverty reduction and an increase in employment are some of the observed achievements at the termination of the Cardoso administration.

ix This is calculated based on the concept of the dual inequality indicator. The computation of the household income per capita considers the weight given to the poorest whose families are, in general, larger.

^xxx Technically similar to Cagan classic definition, monthly rates above 50% for at least 6 months. The inflation in the semester preceding the Real was on average % a month, with relative stability, opposed to the European classic hyperinflations of the 1920s of a more explosive nature..

xi Only sustained expansions translate into formal employment, because of the inherent costs of redundancy. One of the main pieces in this puzzle related to social changes was that formal jobs increased from 600,000 in 2001-03 to 1.2 million in 2004-06.