››› Brazil: investment suffers strongly during recession

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South America's most populous economy is in a deep recession. Real gross domestic product is expected to shrink by around 7.5 % overall in the two-year period of 2015/2016. The Petrobras scandal and the impeachment of President Rousseff have paralysed the country's economic policy, and inflation is significantly above the central bank's target. In this environment it is all too understandable that consumers and businesses are in a bad mood.

Investment is plummeting

The decline in gross fixed capital formation has put particular downward pressure on growth since the second quarter of 2014. It recently fell 18 % in real terms year-on-year. In the construction sector, expectations for new infrastructure contracts dropped at the same time. This is all the more dramatic as Brazil's poor infrastructure poses a severe structural problem. This is reflected in its infrastructure ranking in the Global Competitiveness Index, where Brazil comes in at 74 out of 144 countries.

Olympic Games unlikely to boost the economy

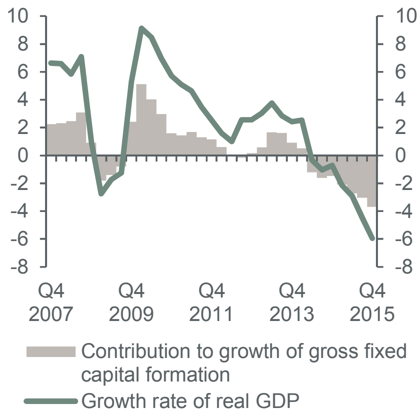
After the 2014 FIFA World Cup, the 2016 Summer Olympic Games is the second major sporting event to be hosted by Brazil in a short period of time. It will be one of the very few countries since the Second World War to host the Olympics in a year of recession. That would make it all the more desirable for rising investment or at least higher tourism revenues to boost the economy. However, expectations that hosting such events generates positive effects are usually disappointed. The positive effect Brazil's bid to host the Games and the actual award had on investment and economic growth, which research has identified, also does little to help Brazil in its current situation. This is because the maximum effect of the decision to bid and the award typically manifests itself five years before the event itself. Besides, public infrastructure expenditure on the 2014 FIFA World Cup and the Olympic Games is very modest in comparison with the expenditure on transport infrastructure under the general growth and employment programme.

Investment weakness with potentially long-term impacts

Declining investment means slower growth of capital stock, which reduces long-term growth prospects. It also means that the technological progress contained in new capital goods spreads more slowly. A significant impulse from the government to mitigate the current investment weakness can hardly be expected. The indebtedness and budget situation is forcing the finance minister to cut spending. Constitutionally prescribed links between public revenues and expenditure leave little scope, so that discretionary investments suggest themselves for spending cuts that can be implemented relatively easily and quickly. Last year public transport infrastructure investment already declined by some 30 %. Private investment activity will pick up when the business climate not only stabilises, but when enterprises' actual business prospects improve substantially. In any case, overall investment is currently not expected to recover disproportionally in the years ahead, with the IMF forecasting a constant investment ratio of 19 % up to the year 2021. ■

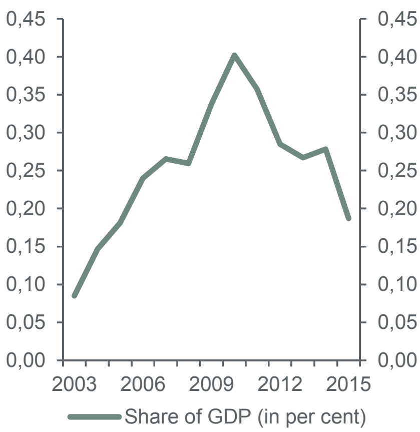
Figure 1: Economic situation

(in per cent and percentage points)



Source: OECD

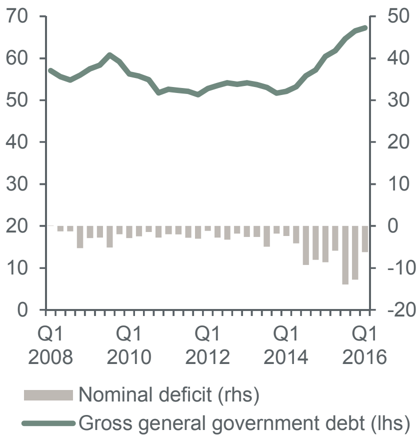
Figure 2: Public investment in transport infrastructure



Source: OECD, IBGE.

Figure 3: Public debt

(in per cent of GDP)



Source: Banco Central do Brasil