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The One Country That Might Avoid Recession Is...

By Tim Padgett and Andrew Downie / Sao Paulo

Brazil is no stranger to economic crises. In the 1970s and '80s, Latin America's economic giant turned financial mismanagement into an art form. The current global turmoil has not left Brazil unscathed: stock prices, exports and growth are all down. But something interesting is at work this time around, and the best place to see it is in one of Brazil's favelas, the vast urban slums that are desperate even in the best of times. Walk through São Paulo's sprawling Brasilândia, though, and you don't sense the relentless doom and gloom gripping other cities in the world. Take Efigênia Francisca da Silva, who exudes middle-class expectations and remains positive despite the tsunami of bad news. Thanks to a government scheme to encourage entrepreneurs, the once dirt-poor housewife has received some \$8,000 in low-interest bank credits in recent years and now owns three shops that sell everything from shampoo to public-transit tickets. "I didn't have a bank account before," says Da Silva, 37, standing beneath graffiti-covered walls and pirated power lines. "I never had a car. I bought a Fiat Palio." Does she fear the global recession will quash her dreams? "I trust Lula. I don't think we'll be hit that hard."

"Lula" is President Luiz Inácio Lula da Silva (no relation to Efigênia), and most Brazilians believe he's the reason their country is surviving the current downturn better than other places. In past crises, Brazil was usually the nation in need of the largest life preserver. If it wasn't drowning under fiscal recklessness, it was being held under by draconian austerity plans. Brazil, the old joke goes, is the country of the future — and always will be. Now, in the middle of the worst global downturn for decades, Brazil could finally be the country of the moment. According to a recent study by the Paris-based Organization for Economic Cooperation & Development (OECD), Brazil may be the only one of 34 major economies that avoids recession in 2009. While the U.S. debates whether to nationalize its crippled banks, Brazil's remain comparatively sound. Oil companies worldwide are slashing investment, but Brazil's state-run Petrobras is going ahead with a four-year, \$174 billion expansion plan. "Brazil," Lula boasted to TIME, "is riding the current crisis better than many developed countries."

To be sure, the boom — years of 5% growth and soaring exports — is over. Industrial production has plunged. Even Embraer, the aircraft maker whose jets sell to scores of airlines, and which has become a symbol of Brazil's newfound confidence, recently announced plans to lay off 4,000 employees, almost one-fifth of its workforce. Commodity exports — soybeans, steel — are weak. The main stock market is down 25% since September. But Lula, a former shoe-shine boy who heads the leftist Workers Party (PT), has so far kept the good times from becoming a hellish bust. In Brazil, that's nothing short of miraculous.

There may be another miracle in the making. Because unfettered capitalism is widely blamed for the global meltdown, economists and laborers alike say Brazil has become an example of what Lula likes to call "the financial strategy of the future." By that he means a postideological approach that is equal parts wealth creation for corporations such as Embraer and wealth redistribution for underdogs like Da Silva. All this under the kind of prudent financial regulation that seems to have gone missing in the developed world of late.

Brazil still faces huge challenges; its education system is dysfunctional, its political system squalid, corruption endemic. But consider: 53% of Brazil's 190 million people now occupy the middle class, up from 42% in 2002. This increased social mobility happened at the same time the country's main stock index soared some 480% before last fall's downturn. Lula seems to have cracked Latin America's chronic conundrum: how to expand underachieving economies while reducing epic inequality. In so doing, he's created a model that's "an insurance ticket, not a lottery ticket," says Marcelo Neri, head of the Center for Social Policies in Rio de Janeiro.

All Change

In an interview last fall at the Planalto presidential palace in Brasilia, Lula, 63, told TIME that he wants to "change the world's political and economic geography" before he leaves office in December 2010. It may be futile to stump for a permanent Brazilian seat on the United Nations Security Council, but the developed world's financial shambles has made Lula's campaign to challenge U.S. and European hegemony in global trade talks less quixotic — and enhanced Brazil's leadership role among developing nations. "Capitalism will be a different animal once the turbulence is over," Lula told TIME. "Developing countries will be responsible for a major percentage of world economic growth."

Twenty years ago, when Lula was a firebrand unionist, that sentiment might have been dismissed as dreamy rhetoric. Not today. However the crisis ends, there is widespread agreement that developing economies such as Brazil, China and India will be crucial to ensuring that demand remains buoyant. Lula, too, has changed. These days he's a pragmatist who is as popular inside corporate boardrooms as he is in the favelas. On March 17, he will meet new U.S. President Barack Obama — a fellow moderate liberal who shares Lula's passion for green-energy ventures — in the White House. He will be the first Latin American leader to meet Obama since he took

office, a sign, perhaps, that the new U.S. Administration sees Brazil as a key partner in forging a new policy for the Americas.

That too would mark a change. Brazilian officials have long wanted to make a mark outside their neighborhood, but until recently, the world rarely noticed what went on there — unless it involved beaches, soccer or Carnaval. "Brazil always suffered externally because of its internal poverty," says Lula's foreign-policy adviser, Marco Aurelio Garcia. The nation's founding monarchy, which lasted until 1889, insulated the country from the region's 19th century upheavals but also spawned a quasi-feudal class system that led to the inequalities that persist today. In 2000, fewer than 3% of Brazilians still owned more than two-thirds of the arable land, and the divide between the rich southeast and destitute northeast, where Lula was born, was as stark as ever.

Lula's predecessor, Fernando Henrique Cardoso, was the first President to recognize that change was needed. He restored fiscal sanity by slaying hyperinflation, but his attempts at social reform were timid. Lula's victory in 2002 panicked Wall Street and the Brazilian elite. But instead of defaulting on Brazil's foreign debt or busting the budget, as they feared he would, Lula embraced one of the few positive legacies of Brazil's royalist roots: deliberate, negotiated consensus-building. It's a hallmark of Brazil's widely respected diplomatic corps — and it tempered Lula even when he was a metal-workers union boss in the 1970s. Unlike more radical Latin leftists, such as Venezuelan President Hugo Chávez, Lula "was always a negotiator," says union pal and former congressional Deputy Djalma Bom, who recalls Lula telling him to stop reading Lenin 30 years ago. Even rivals like Rubens Ricupero, a former finance minister and Cardoso ally, agree. "The danger with Lula is that he can be rather messianic," says Ricupero. "But he's one of the world's most intelligent politicians."

He does not like admitting it, but once in the presidency, Lula embraced Cardoso's macroeconomic orthodoxy. He then used that as a base on which to weld social programs, such as *Bolsa Família*, a grant scheme that has paid out more than \$20 billion in aid to poor families in return for parents getting their children vaccinated and making sure they attend school. Brazil's business leaders insist record profits during the 2005-2008 boom allowed Lula to aid the poor; Lula argues his antipoverty crusade fueled the economic growth. It's a chicken-and-egg debate, in which both sides are right. What matters is that social stimulus programs like *Bolsa Família* have been matched by fiscal measures like a reform of Brazil's engorged civil service pension system. "It's called doing things right," says Lula. "Allowing the rich to earn money with their investments and the poor to participate in economic growth."

A Better Life

Whatever the explanation, the philosophy has done the President well. Two years into his second and final term, Lula has an 80% approval rating. This suggests that despite the recession, most Brazilians still feel they're winning. "It was very difficult to change social class in Brazil 10 years

ago, or even four years ago," says Luis Minori of the market-research firm Ipsos. "Now people have access to microcredit and computers and other means of social mobility." In that sense Brazil has outperformed even China and India, Neri claims, because "poverty is falling [in those places] but inequality isn't."

Easier credit fueled a rush of small business start-ups and car sales (admittedly the last thing São Paulo's insufferable traffic needed). Even the wine market, once a purely upscale domain, has been democratized. São Paulo wine retailer Expand has seen sales of its mid-priced bottles jump 25% each of the past few years, and it has opened new stores in provincial cities like Fortaleza, where beer and cachaça (cane liquor) were once the only tipples. Expand's owner, Otávio Piva de Albuquerque, says he spends as much time helping secretaries find \$12 Concha y Toros as he does stockbrokers \$75 Chambertins. "So many things Brazilians used to think of as unessential," he says, "are suddenly part of life here."

The downturn has slowed growth, but it has not stopped it. To make Brazil even more business-friendly, the government is spending \$263 billion on tax breaks and infrastructure. Like Lula's social projects, the Growth Acceleration Program, which began in 2007, was funded largely by high commodity prices, most of which have now plummeted. But Brazil seems to have invested the windfall smartly. Exports have been diversified so as to reduce reliance on commodities, and before the downturn the nation socked away a record \$208 billion in foreign reserves. The banking system has remained well regulated, and so far seems to have been less exposed to the toxic assets that have wrecked many U.S. and European banks. All this has "buffered Brazil quite a bit against the global downturn," says Paulo Leme, emerging-markets director at Goldman Sachs.

Then there's oil. In 2007 and '08, state-controlled Petrobras discovered up to 12 billion bbl. beneath the Atlantic floor about 155 miles (250 km) off the coast of Rio de Janeiro. The oil lies almost 3 miles (5 km) below sea level and is covered by a thick layer of salt, so extraction will be a massive undertaking. And while the discovery promised a windfall when oil was \$140 per bbl., at today's price of \$40, profitability will be a challenge. Nor is oil always the blessing that it appears; in nations from Nigeria to Saudi Arabia, its promise of easy money has crowded out other sectors of the economy, and fed corruption, too. But Lula, who keeps a jar of oil from the recent find by his desk, along with others filled with exotic beans and plants developed for biofuels, sees the oil as another resource to help end poverty. "God," the President crowed after the discovery, "is Brazilian."

If he is, of course, others will want to listen to him. Lula was one of the few leaders with whom both U.S. President George W. Bush and Venezuela's Chávez had decent relations. Lula told TIME he has "high expectations" that Obama will turn "a new page" on Latin America and "put aside traditional U.S. insistence on a narrow, one-sided approach that focuses almost exclusively on free trade and the drug war." Like most Latin leaders, Lula wants Obama to lift the U.S. trade embargo against Cuba. And he is keen (he may be disappointed) to see the U.S. throw its weight behind a

last effort to save the Doha round of world trade talks, which could offer farm-export nations such as Brazil new opportunities.

For all the new confidence that Brazil is showing abroad, there's a lot to fix at home. Aside from corruption, Brazil's public bureaucracy is one of the world's most wasteful. Education, despite increased funding and access, is an embarrassment: students consistently score near the bottom of international math, science and reading tests. Exorbitant taxes and violent crime scare off foreign investors, and in the Amazon, deforestation remains a problem.

But Lula, like the brawny, business-minded megalopolis he has made his home, has set a sturdy example. São Paulo's vast, stalagmite horizon of skyscrapers can't match the glamour of Rio de Janeiro, but the city of 20 million people is a truer and smarter reflection of Brazil's *bandeirante* (pioneer) character. This year, work will start on the hemisphere's first bullet train, which will eventually link the two cities. High-speed rail won't mask all Brazil's flaws. But it does show, perhaps, that the country of tomorrow has a brighter future.

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