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IDB GROUP STRATEGY WITH BRAZIL 2019-2022

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CONTENTS

APPENDIXES

ANNEXES

LINKS

ABBREVIATIONS

BNDES	Banco Nacional de Desenvolvimento Econômico e Social [Economic and Social Development Bank]
BRIC	Brazil, Russia, India, and China [countries]
CAF	Development Bank of Latin America
CBR	Country Office in Brazil
CDC	Country Development Challenges
CGU	Ministério da Transparência e Controladoria-Geral da União [Ministry of Transparency and Office of the Comptroller General]
CNI	Confederação Nacional da Indústria [National Confederation of Industries]
CONFAZ	Conselho Nacional de Política Fazendária [National Financial Policy Council]
CONSOC	Grupo Consultivo da Sociedade Civil [Civil Society Consultative Group]
CRAS	Centro de Referência de Assistência Social [Social Welfare Referral Center]
CRF	Corporate Results Framework
DATASUS	Departamento de Informática do Sistema Único de Saúde [Public health system data repository]
EPE	Empresa Pesquisa Energética [Energy Research Office]
ESF	Estratégia Saúde da Família [family health strategy]
FGV	Fundação Getulio Vargas [Getulio Vargas Foundation]
GCF	Green Climate Fund
IBGE	Instituto Brasileiro de Geografia e Estatística [Brazilian Geography and Statistics Bureau]
IMF	International Monetary Fund
INEP	Instituto Nacional de Estudos e Pesquisas Educacionais [National Educational Studies and Research Bureau]
IPSAS	International Public Sector Accounting Standards
NCB	National competitive bidding
NDC	Nationally Determined Contribution
OECD	Organization for Economic Cooperation and Development
OVE	Office of Evaluation and Oversight, IDB
PISA	Programme for International Student Assessment
PMR	Progress monitoring report
PPP	Public-private partnership
R&D	Research and development
SAE	Special Strategic Affairs Department
SAIN	International Affairs Department
SIAF	Federal government integrated financial information system
SMEs	Small and medium-sized enterprises
SNIS	Sistema Nacional de Informações sobre Saneamento [National Sanitation Information System]
SPE	Sistema Público de Emprego [National job placement system]
STN	National Treasury Department
TFP	Total factor productivity
UNESCO	United Nations Educational, Scientific, and Cultural Organization
WEF	World Economic Forum

EXECUTIVE SUMMARY

Economic and social context

From 2014 to 2017, Brazil's economy suffered one of the deepest recessions in the country's history, with real per-capita GDP shrinking by about 10%. The recession marked the end of a decade of economic growth fueled by credit and consumption, but unsupported by increases in productivity. In 2018, the economic began to recover slowly, sustained by positive changes in the macroeconomic policy framework and expectations of reform. However, structural problems persist that constrain growth and feed uncertainty. The most serious is a structural fiscal imbalance that poses a direct threat to macroeconomic stability and could lead to crisis scenarios. Apart from the fiscal challenge, the country's productive dynamism is sluggish on account of systemic factors such as weak public sector performance and shortcomings in the business climate and stock of infrastructure, which put pressure on production costs and erode economic efficiency. In this context of macroeconomic risks and sluggish productive dynamism, the social scenario is becoming increasingly complicated, as reflected in unemployment, informal employment, poverty, and inequality.

The IDB in Brazil

The Bank's country strategy for 2016-2018 defined three strategic areas: (i) increase productivity and competitiveness; (ii) reduce inequality and improve public services; and (iii) strengthen institutions at the three levels of government. Twenty-nine sovereign-guaranteed operations totaling US$5.083 billion and 105 nonsovereign-guaranteed operations for US$1.793 billion were approved in the period.

Strategic areas

Based on the lessons learned in the previous country strategy, the analysis and proposals presented in the Country Development Challenges (CDC) document, the recommendations of the country program evaluation by the Office of Evaluation and Oversight (OVE), and the government's "Path to Prosperity" plan, the new country strategy has the objective of supporting the country's efforts to achieve sustainable economic growth through increased competitiveness and productivity, with a government capable of efficiently providing public services for Brazilians. Accordingly, the country strategy for 2019-2022 is structured into four strategic areas: (i) improve the business climate and narrow gaps in infrastructure for enhanced competitiveness; (ii) promote national and international integration to boost productive capacity; (iii) build a more effective public sector that promotes fiscal sustainability; and (iv) reduce social inequality and inequality of opportunity by enhancing public policy efficiency. As crosscutting issues, the strategy will address challenges related to: (a) gender and diversity;

	(b) environmental sustainability and climate change; and (c) innovation and digital transformation.
Financial envelope	For the 2019-2022 period, the IDB projects annual approvals of US$1.8 billion. Annual disbursements are expected to be close to US$1.75 billion. If so, the country's debt with the IDB would be US$17.2 billion or 1.22% of total public debt and 25% of external public debt. In the coming years, loans and technical assistance from IDB Invest are expected to account for a larger share of the IDB Group's total exposure to Brazil and facilitate resource leveraging to speed up economic growth and investment. IDB Lab is also expected to develop synergies between the public and private sectors, through high-impact innovative initiatives.
Principal risks	The principal risks to strategy's implementation are: (i) the macroeconomic context, particularly fiscal sustainability and external shocks; and (ii) execution challenges associated with the technical and organizational capacity of some executing agencies, particularly on the subnational level.

I. COUNTRY CONTEXT[1]

1.1 **Brazil is the largest economy in Latin America and the Caribbean.** In 2017, its gross domestic product was US$2.06 trillion, making it the largest economy in the region. With a population of about 209 million, the country's per capita GDP is US$9,821 in current dollars or US$14,103 in terms of purchasing power parity.[2] Brazil is endowed with a broad range of commodities (oil, food, minerals) that provide a solid and diversified production base. The country has a large domestic economy and a sizeable middle class. All these factors generate significant growth potential despite existing challenges.

1.2 **Brazil's economy recently suffered one of the deepest recessions in its history[3] and is currently staging a slow recovery**. Real per-capita GDP fell by nearly 10% between 2014 and 2017. The recession marked the end of a decade of robust economic growth fueled by credit and consumption, which grew at an annual average of 4% between 2000 and 2014. The set of expansionist policies adopted between 2011 and 2014 heightened the vulnerabilities of the domestic economy which, coupled with negative external shocks, led to the 2014-2017 recession.[4, 5] In that period, the country was also grappling with corruption in public enterprises linked to infrastructure contracting. The recovery has been supported by positive changes in the macroeconomic policy framework and reform expectations. However, uncertainty regarding both these aspects constrains the pace of growth, which the IMF projects at 2.2% in the medium term.

1.3 **Brazil presents a serious fiscal imbalance that threatens economic growth and stability.** Without fiscal reforms, the public debt will continue on an explosive path. The 2018 CDC finds that the government needs to significantly increase the primary surplus to stabilize growth of the public debt. That debt grew from 51.7% of GDP in 2014 to 76.7% in 2018. Concrete initiatives have been taken since 2016 to control the rapid fiscal deterioration. In that year, the Congress approved a constitutional amendment to limit real growth in primary expenditure.[6] The measure had an immediate positive impact on market expectations. If compliance with the amendment is forthcoming, the debt path will decline. Nevertheless, the amendment itself is not enough to solve the problem. Specific fiscal reforms are needed to make the amendment workable over time. However the process of implementing underlying reforms is politically complicated. Reform of the pension

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1 An electronic link to the CDC is provided in this document. It contains a more detailed description of the context.

2 Source: World Bank.

3 According to the Getúlio Vargas Foundation's Comitê de Datação de Ciclos Econômicos (CODACE) [Economic Cycle Dating Committee], the recession lasted for 11 quarters—from the second quarter of 2014 to the second quarter of 2017.

4 According to a 2016 study by the European Central Bank, "the most significant factors in explaining the decline in Brazilian GDP since mid-2014 have been adverse commodity price developments and shocks to domestic factors, including domestic demand, monetary policy, and financing costs. External shocks (defined as global uncertainty shocks and shocks to global financing conditions and foreign demand), on the other hand, have been less significant as a cause of the recent slowdown."

5 Deleveraging also contributed to prolonging and deepening the recession.

6 From 1997 to 2015, total government spending increased by 12.9% a year on average in nominal terms, while average inflation over the period was 6.6%, for a real average increase of 6.3% a year.

system[7] is the main topic on the fiscal agenda,[8] but other major challenges exist, such as improving the efficiency of the State and addressing fiscal federalism and budget rigidity. The crisis is not confined to the federal government since the subnational governments are also experiencing serious fiscal deterioration.[9]

1.4 **Apart from the fiscal challenge, sluggish systemic productivity is an additional factor that hampers sustained growth.** Total factor productivity (TFP) has been sluggish since the 1980s, with capital accumulation and labor responsible for most of the growth observed in recent decades.[10] International comparisons confirm the productivity challenges that Brazil faces.[11] Typically, Brazil's periods of economic growth are supported by the large domestic consumer market, temporary leverage of demand, and exogenous shocks such as commodity prices. Scant competitiveness makes efforts to reduce regional inequalities particularly difficult, since the regions with the lowest per capita income present the lowest levels of competitiveness. In this context, policies to promote the country's sustained growth must go beyond temporary virtuous circles of demand to focus on measures that promote high productive capacity and economic efficiency. The 2018 CDC points out that policies to promote market integration, infrastructure development, and a better business climate are essential for sustained pace of growth.

1.5 **In the absence of adequate solutions to the fiscal challenges and increased productivity, social progress is threatened.** Brazil has made significant headway in reducing poverty and inequality and improving other social indicators since the turn of this century.[12] A new middle class with access to better quality goods and services has achieved higher standards of living.[13] However, the 2014-2016 recession revealed that many of these achievements were cyclical in nature

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[7] In 2018, the social security system posted a deficit of 2.84% of GDP, equivalent to R$195.2 billion.

[8] In March 2019, the government sent a social security reform bill to congress as a constitutional amendment.

[9] As of January 2019, seven states had declared bankruptcy and 11 had obtained authorization from the National Treasury to issue debt, since the Treasury considers their fiscal situation to be satisfactory (ratings A and B).

[10] Fernández-Arias (2014). Ferreira, Pessoa, and Veloso (2013) estimate Brazil's TFP based on data from Penn World Tables (PWT) for 1950-2011 and they also conclude that growth in the country's productivity has been driven by the accumulation of production factors with only a marginal contribution by TFP. Barbosa Filho, Pessoa, and Veloso (2010), and Ellery (2014) report similar results.

[11] Ferreira, Pessoa, and Veloso (2013) conclude that between 1960 and 1980, TFP in Latin America grew slightly faster than in the United States, but the trend reversed between 1980 and 2007, when Latin America's TFP growth was negative. Miguez and Moraes (2014) showed that Brazil's productivity plunged in comparison with China. Between 1995 and 2009, Brazil's labor productivity grew by just 13.6%, while it grew by 226.8% in China over the same period.

[12] The percentage of households with per capita income below the extreme poverty line fell from 10.25% in 2002 to 3.52% in 2013, as more than 15 million people were lifted out of extreme poverty. The Gini coefficient fell from 0.589 in 2002 to 0.518 in 2014, for a substantial reduction in inequality. Average life expectancy rose from 69.8 years in 2000 to 75.8 in 2016. The infant mortality rate fell from 25.3 deaths per 1,000 live births in 2002 to 13.8 in 2015. Illiterate adults over the age of 15 fell from 11.86% in 2002 to 8.27% in 2014. The population with access to sewer systems grew from 65% to75% in the period, and the percentage with access to drinking water rose from 87% to 95%.

[13] In 2012, the government classified 53% of the population as belonging to the middle class, for an increase of 35 million people between 2002 and 2012.

and were not attained through productivity that was high enough to generate lasting benefits.[14]

1.6 **The adoption of new technologies, environmental sustainability, addressing climate change, and social inclusion with opportunities—especially with respect to gender and race—should form part of the sustainable development equation.** The global technology wave known as the fourth industrial revolution, is creating challenges and opportunities for Brazil's economic development. Technology can provide the country with the chance to speed up economic growth, boost competitiveness, administer resources more efficiently, and expand services for the poorest and most vulnerable families with better quality and efficiency.[15] Scant use is made of Brazil's natural capital as a driver of resilient, low-carbon economic growth. Its natural capital is threatened by increasing deforestation and contamination of watersheds, among other factors.[16] Climate change challenges will demand efforts to improve systemic territorial planning, mitigate the impact of greenhouse gases, and promote adaptation to the effects of climate change, particularly on infrastructure. The country's vulnerability in this context is apparent in recurrent droughts and flooding that adversely impact the productive sector, infrastructure, the energy sector, and others (CDC 2018). Lastly, social inclusion with opportunities is a pending task in Brazil, which continues to have deep inequities in income, schooling, labor market access, and physical security, which disproportionately affect women, indigenous groups, and Afro-Brazilian communities.[17]

1.7 **The external context adds uncertainty to Brazil's growth and economic development challenges.** Changes in trade relations among the world's largest economies and, more broadly, the underlying geopolitical developments, condition the levels of cooperation and dynamism captured in international investment, technology, and knowledge flows. In this context, Brazil needs to take a pragmatic approach to tapping integration opportunities that can concretely help to boost its productivity and international market penetration. Another uncertainty is the evolution of monetary policy in the advanced countries, which can generate sudden movements in international financial conditions, with an amplified impact

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[14] After a lengthy period of stable low unemployment between 2005 and 2014, the economic decline considerably worsened labor market conditions. The unemployment rate began to rise in 2014, peaking at 13.7% in the first quarter of 2017. After improving steadily for a decade, Brazil's Human Development Index stagnated and according to the World Bank's Per Capita Poverty Rate, the number of people living below the international poverty line increased in 2015.

[15] The CDC 2018 indicates that the country faces serious challenges in adopting new technologies.

[16] Climate Policy Initiative, 2018.

[17] The CDC 2018 provides statistics that indicate significant race and gender inequality in the country. Afro-Brazilians make up about 78% of the population in the lowest income decile and just 24% of the highest decile. While unschooled white workers earn R$9.20 an hour, the average unschooled Afro-Brazilian makes R$6.80 or 26% less. This difference is as high as 30% among workers with a higher education. As for gender, the CDC 2018 indicates that just 53% of Brazilian women are in the workforce compared to 75% for men. In Peru, Uruguay, and Colombia, in contrast, more than 60% of women are in work. The unemployment rate for women fell from 11.5% in 2004 to 8.4% in 2013 but rose again to nearly 13% in 2016. Women are underrepresented in the formal sector and hold just 13.6% of executive positions in the 500 largest Brazilian companies, although female employees in those companies have more years of higher education and are majority participants in training programs.

on countries which, like Brazil, are in the process of implementing reforms to correct severe macroeconomic imbalances.

II. THE IDB IN BRAZIL

2.1 **The IDB Group continues to be Brazil's main multilateral partner.** The IDB Group (sovereign-guaranteed loans) currently accounts for 37% of the country's multilateral financing[18] and 22% of its external financing.[19] The active portfolio of sovereign-guaranteed operations is approximately US$13.2 billion[20] and consists of 93 loans distributed among the country's five regions. It currently represents 15.5% of the number of Bank operations and 24.1% of the Bank's total aggregate portfolio in Latin America and the Caribbean.[21] IDB Invest's active portfolio amounts to about US$1.2 billion.[22]

2.2 **The country strategy for 2016-2018 was based on three pillars: (i) increase productivity and competitiveness; (ii) reduce inequality and improve public services; and (iii) strengthen institutions at the three levels of government.** Considering that Brazil is a middle-income, highly urbanized country of continental dimensions, with limited capacity for public investment in infrastructure and public services, the following three implementation approaches were proposed to guide Bank interventions: (i) strengthening of public-private partnerships for development; (ii) sustainable economic development of the metropolitan areas; and (iii) reduction in regional socioeconomic inequalities. The strategy also considered the crosscutting issues of gender, diversity, integration, and climate change. The strategy was consistent with the strategic priorities of IDB Invest's Business Plan 2016-2019, principally in the priority areas of lending to infrastructure projects and lending to small and medium-sized enterprises (in both cases supporting the strategy's objective of boosting productivity and competitiveness), support for activities aimed at enhancing competitiveness through innovation, support for the provision of goods and services to vulnerable populations, and fostering of green growth by promoting the adoption of sustainable business practices.

2.3 **The lending program approved during the country strategy period[23] consisted of 134 operations, 29 of them sovereign-guaranteed,[24] for a total US$5.083 billion, and 105 nonsovereign-guaranteed, for a total of US$1.793 billion.[25]** Of the sovereign-guaranteed operations, 23 (79.3%) were with

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[18] The CAF has 12 active operations totaling US$983 million. The World Bank has 28 for a total of US$5.974 billion. Data collected on 11 February 2019 from the websites of CAF and World Bank, respectively.

[19] Source: Central Bank of Brazil, 2018.

[20] Source: LMS50 Country Portfolio (31/12/2018).

[21] Source: Active IDB Portfolio (13/02/2019).

[22] At 31 December 2018.

[23] From 30 March 2016 to 31 December 2018.

[24] The number of operations (29) is different from the number of sovereign-guaranteed projects (28) because BR-L1496 corresponds to two lending operations (4723/OC-BR and 4732/OC-BR).

[25] Nonreimbursable technical-cooperation projects are not included.

states, state-owned enterprises, or municípios, maintaining the subnational emphasis. In terms of regional focus, 37.9% of sovereign-guaranteed operations (by number) were in the North (3.4%) and Northeast (34.5%). Ten sovereign-guaranteed operations were also approved in the Northeast (US$627.2 million), four in the South (US$710.2 million), six in the Southeast (US$668.1 million), and two in the Center-West (US$148 million). Six further operations were approved on the federal level for 57% of total approvals (US$2.9 billion). **As for nonsovereign-guaranteed operations,** IDB Invest approved 100 (US$1.780 billion)[26] distributed as follows:[27] 17 loans (US$787.6 million), seven guarantees (US$305.2 million), two equity operations (US$20.3 million), and two debt securities (US$90 million).[28] IDB Lab approved two capital investment operations (US$3.8 million), three equity operations (US$10 million), and 13 nonreimbursable technical-cooperation projects for US$9.6 million.

2.4 **The IDB maintained its position as an important source of technical assistance and knowledge transfers for Brazilian public institutions.** During the strategy period, 40 technical-cooperation projects for a total of US$20.9 million were approved, which focused on boosting efficiency in public resource management (12 totaling US$7.6 million) and improving drinking water and basic sanitation conditions (6 totaling US$1.9 million). A nonreimbursable investment for US$32.6 million was also approved to promote environmental conservation in the country.

A. Main results of the country strategy for 2016-2018

2.5 **In the area of increased productivity and competitiveness,** 28% of the projects in the portfolio were aligned with this pillar and focused on transportation, energy, tourism, innovation, and financial markets. Estimates suggest that the investments in **transportation and logistics** reduced operating costs by 30% and travel times by 40%, and motor vehicle fatalities by 20% in their areas of influence. **In energy,** the useful life of renewable hydroelectric generating plants was prolonged and availability was improved,[29] including a reduction in forced outages from 2.6% to 1%. With the expansion and upgrading of the distribution grid in the south of the country,[30] the quality of the electricity supply was improved, reducing the frequency of outages (from 15.5 to 8.8 outages per user per year) and their average duration (from 21.8 to 15 hours per user per year) in the project areas. The IDB Group also contributed to 11% growth in the country's wind and solar energy sources.[31] **Tourism programs** have contributed to the development of tourist sites in the states of Pernambuco, Bahia, and Ceará.[32] As an example of the results achieved, tourist spending grew by more than 5% in Pernambuco, which has created income

[26] From 30 March 2016 to 31 December 2018.

[27] Considering that a given operation can have a number of outputs.

[28] There were an additional 72 operations under the Trade Finance Facilitation Program (TFFP) for US$577 million.

[29] Operation BR-L1303 financed the rehabilitation of the Itaúba and Passo Real plants.

[30] 146 kilometers of transmission lines have been built/expanded and transformation capacity has been increased to 1200 MVA at substations (BR-L1303 and BR-L1284).

[31] Operation BR-L1442 financed installation of 1131 MW of wind and solar energy in 2017 and 2018.

[32] Operations BR-L1212, BR-L1300, and BR-L1204.

opportunities and a 2% increase in hotel employment. The tourism interventions in the city of Salvador[33] helped to improve ethnic tourism products and train sector entrepreneurs, for an increase in spending by tourists that benefits Afro-Brazilians, particularly women. In terms of **access to financing for small and medium-sized enterprises (SMEs) and support for business competitiveness**, the operations with the Economic and Social Development Bank (BNDES) and Financiadora de Estudos e Projetos (FINEP)[34] expect to reach more than 5,100 SMEs.

2.6 **IDB Invest** made a fundamental contribution to this pillar. Examples include greater competitiveness in the sugar and alcohol industries in the interior of the state of São Paulo; construction of the largest thermoelectric plant in Latin America and the Caribbean in Aracaju (with installed capacity of 1,516 MW, which serves as a backup for renewable energy sources); solar and wind energy projects in the states of Minas Gerais and Rio Grande do Sul, respectively; and the installation and upgrading of 104 power transmission and distribution lines. These operations are intended to promote the sugar and alcohol sector, improve infrastructure, reduce greenhouse gas emissions, and create renewable energy capacity. With regard to financial institutions, IDB Invest helped to leverage resources for SMEs through Banco do Brasil, and to develop the microfinance market through Omni S.A, a financial institution that serves the most vulnerable social classes. These efforts increased access to finance for 76,153 SMEs and offered opportunities for economic empowerment to 25,113 women.

2.7 **IDB Lab** also contributed to this pillar through its support for the entrepreneurial climate in Brazil. IDB Lab has been an important anchor investor in venture capital funds and has invested over US$50 million in a total of 19 Brazilian funds to date.[35] Through these investments, more than 100 startups introduced innovations in financial services (e.g. low-cost loans for SMEs and families), education (e.g. new distance education models), and health (e.g. technologies to lower the cost of private health care and provide diagnostic services for vulnerable groups). Furthermore, IDB Lab supported the creation of Brazil's entrepreneurial ecosystem, which made great strides between 2016-2018, favoring the introduction of new education models for young people and training in the field.

2.8 **The IDB Group provided technical assistance and support for a variety of public-private partnership initiatives**, such as structuring the fourth round of airport concessions;[36] preparing a proposed legal framework to simplify legislation governing smaller concessions in municípios; and conducting joint studies with the World Economic Forum on infrastructure project finance for the Special Department for the Investment Partnerships Program (SPPI).

2.9 **In the area of reducing inequality and improving public services,** 44 projects (47% of the portfolio) contributed to the objectives of this pillar, particularly in water and sanitation, education, and health care. In the **water and sanitation** sector, public access to sustainable basic services was increase by installing more than

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33 Operation BR-L1412.

34 Operations BR-L1442 and BR-L1490.

35 Source: Active Portfolio IDB Lab (31/12/2018).

36 Salvador, Fortaleza, Florianópolis, and Porto Alegre airports.

530,000 new residential sewer connections. This amounts to an additional 1.27 million people connected to a sewer system in urban areas and increased access to drinking water and basic sanitation for 170 indigenous families.[37] In addition, 19,400 families living in areas prone to flooding have been made less vulnerable through relocation.[38] In **education**, the IDB has helped to expand early education by 50% in municípios where it was active, in line with the goal established in the National Education Plan for 2014-2024. Construction of comprehensive secondary schools (administered by the states) offered students in remote areas access to this level. The average secondary school attendance rate in Amazonas rose from 80.4 in 2014 to 83.7 in 2017, while the dropout rate fell from 12.2 to 8.9 over the same period. As well, the use of technology in secondary education has made it possible to reach remote communities[39] and increase enrolment on this level by young people and adults.[40] In **health care and social welfare**, coverage of poor and vulnerable families assisted by public social services was increased by building social welfare referral centers (CRAS) and expanding the network of early childhood centers,[41] providing intensive support for families by social services,[42] and offering additional activities for the inclusion of vulnerable young people.[43] The quality of primary and specialized health services was improved by expanding the coverage of disease prevention and care for

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37 Operation BR-L1314.

38 More than 530,000 residential sewer connections have been built (operations BR-L1297, BR-L1314, BR-L1369, BR-L1216, BR-L1335, BR-L1295, BR-L1166, BR-L1215, and BR-L1405), 17 kilometers of drainage channels (operations BR-L1297, BR-L1216, BR-L1081, BR-L1335, BR-L1006, and BR-L1405), 8.9 hectares of linear parks (operations BR-L1006, BR-L1335, and BR-L1297), 18,375 families removed from areas prone to flooding (operations BR-L1297, BR-L1314, BR-L1216, BR-L1335, and BR-L1006), and 1,410 families resettled (operations BR-L1297, BR-L1314, BR-L1369, BR-L1216, BR-L1335, and BR-L1006).

39 The states of Amazonas and Pará offer three years of in-person secondary school through the use of technology, where the teachers are located in the capitals and students follow their classes by satellite, with the assistance of a facilitator.

40 Development of 819 early education centers and construction of nine new secondary school units, in addition to training for 2,148 lower schoolteachers (BR-L1329 and BR-L1327).

41 Seven new CRAS have been built in Ceará, two assistance centers, nine sports fields and/or sports centers, and four early education centers, that benefit close to 60,000 people (BR-L1053). They are in addition to another 156 units that opened in recent years, with Bank support.

42 In Paraná, the Bank provided support for at least 11,000 families in municípios with lower Human Development Indexes, which were given preferential access to cash transfers, schooling, training programs, and health services (BR-L1372).

43 In the city of Fortaleza, more than 50,000 young people participated in innovative programs that helped them return to the education system, gain access to higher education, and find jobs in the three most vulnerable regions.

chronic and degenerative diseases in the Northeast[44] and Southeast,[45] in addition to increasing secondary and tertiary level service availability.

2.10 As crosscutting approaches, **urban and housing programs** have contributed to the objectives of the second pillar of the country strategy by improving basic infrastructure in the poorest neighborhoods, increasing social service coverage, improving urban mobility, and regularizing property. The main investments have been used to expand drainage and water and sanitation systems,[46] pave streets, provide social, sports, and recreational equipment (schools, sports fields, and squares), and rehabilitate urban parks.[47] In Aracaju, for example, the number of families receiving assistance increased by more than 5,000 or the equivalent of 50% of the municipal coverage target. Better transit management in downtown areas, modernizing and paving of 51.5 kilometers of urban streets,[48] and equipping intersections with smart traffic lights[49] have reduced transportation costs and travel times in the cities of Curitiba, Niterói, and Aracaju. As well, support for including thousands of informal properties in the cadaster has revitalized fringe areas and improved the situation of low-income families living in informal and at-risk areas.

2.11 **Citizen security** interventions have reduced repeat offences by young people discharged from juvenile detention centers by 50% (from 32% to 16.25%) in the program’s three municípios. Homicides committed by young people between the ages of 15 and 24 have fallen by 5% (from 88.8 to 84 homicides per 100,000 population) and robberies by this same age group have been reduced by 10% (from 62% to 56%).[50]

2.12 With regard to **institutional strengthening of the three levels of government**, (21% of the portfolio), the Bank has supported **fiscal management** in states and municípios, contributing to modernization of tax collection systems, management systems, and decision-making processes by the federal public administration. The

44 In Bahia, four polyclinics have been built and equipped and are operating (BR-L1389), benefitting a population of 2.5 million. In Fortaleza, 19 basic health care units were opened, covering close to 85,000 people (BR-L1414).

45 In São Paulo, 47 basic health care units were built, equipped, and are operating, in addition to five psychosocial assistance centers that help 55,000 people a year, and one hospital (BR-L1376) that benefits 2 million. In São Bernardo do Campo, two polyclinics have been equipped to meet the technical specifications of the unified public health system (BR-L1415), providing care for close to 300,000 people.

46 Two kilometers of drainage systems and 3,300 water and sewage connections were built (BR-L1386).

47 Urban parks: Novo Hamburgo (operation BR-L1187), Parque da Gare-Passo Fundo (operation BR-L1163), and Parque Águas–Niterói (operation BR-L1386).

48 20.9 kilometers of road corridors (operation BR-L1163), 27.56 kilometers of streets (operations BR-L1099 and BR-L1187), and 14 kilometers of dirt tracks paved (BR-L1386).

49 An operations control center was installed in Niterói, with 212 cameras for monitoring and a 56 kilometers optical fiber network.

50 Six youth centers were installed in temporary premises (until construction of the permanent buildings is completed) and services have been provided for more than 6,000 young people, 500 of whom found jobs (operation BR-L1343). Sixty-five mobile community police stations (operations BR-L1387, BR-L1331, and BR-L1343) and the public safety observatory in Rio Grande do Sul were installed (operation BR-L1343). In resocialization, interventions and building improvements have reduced the recidivism rate by more than 50% for young people discharged from juvenile detention centers (from 32% to 16.25%) (operation BR-L1343).

introduction of electronic billing in 27 states permitted the recording and storage of about 19 billion fiscal invoices for tax purposes from close to 1.5 million Brazilian companies.[51] This has allowed for: (i) the integration of fiscal data between the state and federal governments which led to an average increase in revenues of 36.6% between 2012 and 2017 in seven of the states evaluated, compared to an increase of 14.7% in a state without the project;[52] (ii) the use of data to establish reference prices which led to savings of 38% in state government procurement operations; and (iii) a reduction in informality in the economy of about 18%.[53] **Financial management** has also been strengthened through progress in modernizing integrated financial management systems (SIAFs) and adapting them to the new accounting rules, in budget management, and in access to fiscal data by citizens, for an increase in transparency. The Bank also contributed to consolidation of the institutional capacity of the Ministry of Transparency and Office of the Comptroller General (CGU) by shoring up its internal operating capacity and its interaction with public managers in the federal administration, expanding civil society's control over the management of public resources, and increasing transparency in public spending at the three levels of government.[54]

2.13 **The country strategy's crosscutting themes and dialogue priorities have been addressed through actions to generate and transfer knowledge, bolster capacity, and promote innovation.** The Bank's technical cooperation played an important role in this area. Support for the federal level during the country strategy period corresponded to 76% of the technical-cooperation projects approved in the period (28 projects for US$15.9 million).[55] The most prominent results include an improvement in the efficiency of public policies brought about by building the federal government's technical and decision-making capacity in sectors such as health, fiscal management labor market, transparency, and sustainable infrastructure. As for climate change, projects approved in the period resulted in an in-depth understanding of the narrative guiding the country in its climate pledge (Nationally Determined Contributions—NDCs) and the Green Climate Fund (GCF). The main results are access to the GCF through more appropriate institutional arrangements and consolidation of an active dialogue between the public and private sectors, cities, and the federal government on investments in infrastructure through the NDCs. As for innovation, the IDB Group has been a

51 Nota Fiscal Eletrônica.

52 Análise da eficiência relativa dos gastos públicos em segurança nos municípios do Rio Grande do Sul usando o método DEA [Analysis of the relative efficiency of public spending on health in Rio Grande do Sul, using data envelopment analysis]. Department of Finance of the state of Rio Grande do Sul, April 2018.

53 Source: Eliminando as barreiras ao crescimento da Economia – uma atualização com foco no varejo [Eliminating barriers to economic growth: An update centering on retail business], December 2014. Instituto para Desenvolvimento do Varejo.

54 Improvement in the index that measures the CGU's organizational climate (from 2.5% to 32.9%); improvement in the percentage of recommendations acted on by audited entities (from 18% to 74.4%); increase in the annual financial income generated by the work of the CGU (from R$2.3 billion to R$4.6 billion); 100% increase in citizen access to the transparency portal (from 921,000 to 1,761,000); 100% of Brazilian states with regulated access to information laws (from 20 to 27 states) (operation BR-L1223).

55 The states received 19.5% (in nine projects for US$4.1 million) and the municípios 4.5% (in three projects for US$900,000) of the total approved in the period.

leading technical player in cutting-edge themes such as digital transformation and innovation, citizen security, solid waste management, plant and animal health, and food safety. In digital transformation and innovation, possibilities have been opened up for regional cooperation with a resumption of dialogue for the sharing of experiences.

Lessons learned in the country strategy period

2.14 **At the strategic level** is it important to: (i) promote fiscal sustainability, supporting structural reforms and processes based on the principals of efficiency, transparency, and technological transformation; (ii) support implementation of policies to boost economic and social development, promoting efficiency and effectiveness in public investment and expenditure in priority sectors with high impact on the public budget; (iii) help to improve competitiveness and the business climate by promoting private investment in productive sectors with the highest potential and creating the infrastructure and logistics conditions to support their development; (iv) continue promoting strategic dialogue on medium- and long-term public policies by defining and implementing agendas that ensure concrete progress and commitments, with active participation by the different social sectors (government, private sector, civil society, and academia) on the federal and subnational levels; (v) support processes to open up regional and global trade and integration through technical assistance and facilitation of relations with other countries and regional blocs; (vi) in the relatively less-developed states, promote participative processes to devise sustainable development strategies with a multisector approach and investment plans to guide the flow of financing from the public budget, federal and regional banks, multi- and bilateral banks, and the private sector; and (vii) deepen synergies and investment coordination between the IDB Group's public and private windows and with other multi- and bilateral agencies, public banks, investment funds, and private financial institutions**.**

2.15 **At the operations level**, during the country strategy period an improvement could be observed in the profile of the portfolio of sovereign-guaranteed operations, with the number of operations rated as "satisfactory" growing in recent years, as measured in the progress monitoring reports.[56] This was achieved through adoption by the Country Office in Brazil of measures such as: (i) comprehensive portfolio reviews with the involvement of the federal government guarantors (National Treasury Department (STN) and the International Affairs Department (SAIN)); (ii) agreements on precise criteria for granting extensions of the timeline for the last disbursement of operations;[57] (iii) cancellation of operations awaiting the signature of borrowers who fail to comply with the criteria for obtaining a Treasury Department guarantee; (iv) improvements in the quality and capacity of executing units in project management, fostering good practices in planning and monitoring, fiduciary management (procurement and financial), and risk management; and (v) strengthening the managerial capacity of the Bank's operations team. As for IDB Invest, the importance of improvements in the

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[56] Progress monitoring reports: 43% (March 2016), 63% (March 2017), and 75% (March 2018).

[57] With some exceptions, the basic criteria for extending the date of the final disbursement are: (a) "satisfactory" rating; (b) maximum extension equivalent to 150% of the original term; (c) for projects on "alert" status or "problem" projects, the extension is conditional on a cutback in resources to ensure execution of the remaining funds within the additional time granted.

strategic tools for development planning and effectiveness, maintain a presence in the field, and innovation in support tools tied to resource leveraging, stand out as central elements in the development and effectiveness of private-sector activities.

III. PRIORITY ISSUES[58]

3.1 **The purpose of the IDB Group's strategy in Brazil for the period 2019-2022 is to promote sustainable development and build a more effective government.** Based on the lessons learned from the previous country strategy, the results presented in the CDC, the recommendations in OVE's country program evaluation, and the proposals of the government's "Path to Prosperity" plan,[59] the new country strategy will support the country in its efforts to generate sustainable economic growth by boosting competitiveness and productivity, with a government capable of efficiently delivering public services to the population. Accordingly, the country strategy for 2019-2022 is founded on four priorities: (i) Improve the **business climate** and narrow gaps in **sustainable infrastructure** to enhance **competitiveness**; (ii) Promote international and national **integration** to boost productive capacity; (iii) Build a **more effective public sector** that promotes **fiscal sustainability**; and (iv) Reduce **social inequality and inequality of opportunity** by enhancing **public policy efficiency**. The strategy will provide crosscutting support for challenges relating to: (a) gender and diversity; (b) environmental sustainability and climate change; and (c) innovation and digital transformation.

3.2 **The IDB Group's proposed actions are aligned with the Update of the Institutional Strategy 2010-2020**, the objectives of which are to strengthen institutional capacity and the rule of law, provide inclusive infrastructure and infrastructure services, develop quality human capital, establish smart institutional frameworks, provide adequate knowledge and innovation systems, and improve urban planning and rural infrastructure. The priorities are also aligned with the priority segments of IDB Invest's Business Plan 2017-2019 and its update, which are to promote infrastructure development, build capacity to support the corporate segment, and use resources through the financial system to support priority areas and crosscutting themes.

1. Improve the business climate and narrow gaps in sustainable infrastructure to enhance competitiveness

3.3 **In comparative terms internationally, Brazil's levels of competitiveness are low.** According to the World Economic Forum's 2018 Global Competitiveness Index, which monitors the performance of 140 countries using 12 competitiveness pillars, Brazil ranks 72nd (59.5 points) and its competitiveness has deteriorated in recent years compared to its 2012-2013 ranking, when it ranked 44th out of 144 countries. In this index, Brazil lags behind all the other BRIC countries.

3.4 **Competitiveness in Brazil is hampered by a business climate that does not promote entrepreneurship, innovation, or productivity growth.** In the 2019

58 All the references can be found in the CDC (Annex I), as well as detailed analyses of the development challenges discussed in this document.

59 Current government's election campaign document.

Doing Business Report, Brazil ranks 109th out of 190 countries in the general quality of the business climate. In the 2018 competitiveness report by Brazil's National Confederation of Industries,[60] Brazil placed last among 18 countries in the quality of its business climate, with poor performance in all of that index's components, including relations with the government, quality of regulation, legal certainty, bureaucratic requirements, labor relations, rule of law, ease of opening a business, and contracting and dismissal practices.

3.5 **Brazil's complex tax system affects the business climate.**[61] The Brazilian government currently collects more than 60 taxes and compulsory contributions mandated by the constitution and different pieces of legislation. From 1988 to 2016, close to 363,000 rules and guidelines were issued on tax matters, at an average of 31 per day,[62] and each Brazilian company is required to comply with an estimated average of 3,000 fiscal directives. A manufacturer spends an average of 1.16% of its annual turnover to comply with the tax legislation, which is equivalent to 10% of its annual spending on wages, in addition to facing costly litigation. For small businesses, this cost represents 3.13% of annual turnover.[63] According to the World Bank, the average Brazilian company spends 1,958 hours preparing and paying taxes, which is more than seven times the world average.

3.6 **Bureaucratic costs are a disincentive for the creation of new companies in Brazil, with negative consequences for growth in productivity and formality.** According to Doing Business 2019, starting a company in Brazil takes more than 20 days, which is higher than the world average.[64] The various steps required to open a business come under the jurisdiction of different governmental and institutional levels, which complicates the process and results in high document rejection rates.[65]

3.7 **The private-sector innovation rate in Brazil's is low and, in general, the indicators have stagnated.** Empirical evidence has shown a positive correlation between innovation and productivity.[66] While investment in innovation as a percentage of GDP is higher in Brazil than in other Latin American countries, it is lower than the levels in the more dynamic world economies, and the private sector's contribution to total investment in innovation is small (CDC 2018). The public sector makes more than 50% of all investments in research and

60 Confederação Nacional da Indústria (2018).

61 Appy (2017) argues that Brazil's tax structure creates serious distortions in the assignment of relative prices, in sector distribution of production, and in the geographic distribution of production, and other areas, that reduce economic efficiency.

62 Instituto Brasileiro de Planejamento e Tributação [Brazilian Tax Planning Bureau] (2017) and Amaral et al. (2017).

63 Federação das Indústrias do Estado de São Paulo (FIESP) [State of São Paulo Federation of Industries], (2011).

64 Considering that many of the steps to open a business derive from state and municipal regulations, there are differences between Brazilian localities, but even in the best localities opening a business is a processes requiring too much bureaucratic red tape. There is a similar problem with paying taxes.

65 Opening a business takes 11 steps, 101 days, and 4.1% of per capita income, compared to 8.3 steps, 31.6 days, and 31.5% of per capita income in Latin America and the Caribbean (World Bank, Doing Business 2015: Going Beyond Efficiency, Washington, D.C.).

66 For a study of the literature, see Bell and Forbes (2012).

development (R&D), similar to levels in other Latin American countries and much higher than other BRIC countries such as Russia (38%) and South Africa (42%). In Japan and South Korea, the private sector accounts for 75% of all R&D investments. The Brazilian private sector's scant in R&D has remained virtually unchanged since the turn of this century, in contrast to growth in private investment in innovation throughout the world.[67] Consequently, Brazilian researchers account for just a small fraction of private sector employees.[68]

3.8 **The scarcity of credit limits private sector development and the financial system does not play a strong intermediation role.** Although Brazil has one of the most sophisticated financial systems in Latin America and the Caribbean, financing for companies and families is scarce and costly. Microcredit makes up just 0.4% of all credit. Most companies invest using their own resources on account of the limited access to credit.[69] Brazil's banking system offers short-term loans to families and businesses, but long-term credit is restricted mainly to public banks. The capital market needs to develop private financing structures for long-term projects, particularly in infrastructure. The BNDES portfolio has provided 80% of total infrastructure financing in Brazil in the last decade. In contrast, private institutional investors assign less than 1% of their assets to infrastructure, due to the absence of suitable instruments that correspond to their risk profiles and time requirements (CDC 2018). In this context, financial sector innovations could be tools for promoting new forms of financing targeted chiefly to families, microenterprises, and SMEs.

3.9 **Although public-private partnerships (PPPs) can be a powerful tool for boosting the country's competitiveness, they need to be more highly developed.** PPPs promote the adoption of new technologies and better processes, while boosting efficiency and transparency in infrastructure and social investment policies in Brazil. PPPs can also contribute efficiency and innovation to the development and management of infrastructure assets. Brazil has made an effort to implement PPPs in the last 20 years and they are used to promote private investment in infrastructure more than in other countries in the region and the world.[70] Weaknesses in planning and management and the absence of projects with feasibility studies limit PPP development. These limitations are particularly relevant at the subnational level.

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67 De Negri, 2010.

68 Mirroring its low levels of investment in innovation, Brazil produces relatively few patents. According to the United States Patent and Trademark Office, between 2000 and 2015, Brazil's patents rose from 98 to 323, for annual growth of 9.6%, far below the rates for China (38% a year), India (28.3%), and Chile (13.2%). According to Pinheiro and Figueiredo (2017), the low production of patents in Brazil probably reflects limited private investment in R&D. The authors show that for every US$1 billion spent on R&D in 2013, Brazil produced 7.4 patents. With the same resources, China produced 20.6 and the developed countries more than 100.

69 Alves and Luporini (2014)

70 Between 1990 y 2016, at least 900 projects in the energy, transport, and water sectors reached their financial close. In Brazil, PPPs accounted for about 60% of total private investment between 1990 and 2017, with the majority of projects concentrated in transport, energy, and telecommunication. Brazil has also been the largest market for PPPs in Latin America in the last two decades. World Bank, 2017.

3.10 **Inadequate infrastructure stands in the way of increased competitiveness.** The poor quality of infrastructure services in Brazil throttles the country's economic potential. In the World Economic Forum's 2018 Global Competitiveness Report, Brazil ranked 81st out of 140 countries in the quality of infrastructure (64.3 points), 112th in the quality of highways, 97th in the efficiency of railways, 105th in the efficiency of seaports, and 73rd in the efficiency of air transport service.[71] Public investment in infrastructure in Brazil is low and has declined in recent decades. In the 1970s, it accounted for 5.42% of GDP, on average, but had fallen to 2.06% in the 2000s.[72] The main infrastructure gaps and challenges are described below.

3.11 **Transportation and logistics.** Transportation costs account for nearly 60% of Brazil's total logistics costs, corresponding to 12.3% of GDP, compared with 7.8% in the United States.[73] Brazil ranked 56th among 160 countries in the World Bank's 2016 Logistics Performance Index. The country relies heavily on highways for its passenger and freight transport. Brazil's paved system is small for a country of its size and suffers from problems related to signage, pavement quality, and engineering. Although the country has one of the longest highway systems in the world, close to 2 million kilometers long, just 12.3% is paved. Only 38% of the paved roads are in good or excellent condition, 34% are in fair condition, and 28% in poor condition.[74] Brazil's heavy dependence on trucking increases transportation costs (CDC 2018). The railway system is limited and suffers from operational bottlenecks.[75] Obsolete equipment, limited multimodal terminals, and shortfalls in capacity reduce the efficiency of Brazilian ports.[76] Despite the country's many waterways, river transport is in its infancy,[77] with poor quality infrastructure and installations.

3.12 **Energy.** The electric power sector needs more capacity and diversification of its energy matrix. Although electrification is nearly universal (99.3%), demand will grow by 4.4% annually between 2017 and 2022, from 624 terawatt hours (TWh) in 2017 to 773 TWh in 2022.[78] Investments of US$75.6 billion in generation, including distribution, and US$28.6 billion in transmission will be needed to respond to this demand between 2018 and 2027. Brazil's energy matrix is highly dependent on hydroelectric energy, which helps to provide renewable, clean, and low-cost power, but increases the country's vulnerability to climate change. Accordingly, the additional generating capacity should mainly come from other renewable sources,

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71 World Economic Forum, 2018.

72 World Bank, 2018.

73 Institute of Logistics and Supply Chain (ILOS), 2018.

74 The average increase in operating costs owing to poor pavement on all public highways and highways under concession is 24.9% (Confederação Nacional do Transporte, 2016).

75 The government estimates that bottlenecks exist on 5,429.7 kilometers of railway track (Plano Nacional de Logística, 2018).

76 World Bank, 2012. Projected demand for Brazilian ports was 1.8 billion tons (Plano Nacional de Logística Portuária, 2015), while total estimated capacity is 1.4 billion. Although Brazilian ports move an average of 34 containers an hour per vessel, Hamburg moves 66, and Singapore 100.

77 The main products carried by river in 2016 were soybeans, for 20.4%, oil for 14.9%, and sand for 12.4%.

78 Plano Decenal de Expansão de Energia 2027 [Ten Year Energy Expansion Plan].

such as wind and solar energy,[79] to comply with the country's NDC goal of increasing renewables (excluding hydroelectricity) in the energy matrix from 28% to 33%.[80] Greater energy efficiency is a pending challenge. Inefficiencies exist in energy consumption, transportation, and distribution. Studies by the American Council for an Energy-Efficient Economy (ACEEE) find that Brazil captures less than 30% of its energy efficiency potential and ranks 15th out of the 16 economies studied.[81]

3.13 **Water and sanitation.** Brazil faces significant shortfalls in sanitary sewerage services, drinking water supply, solid waste management, and drainage. According to the national basic sanitation plan, the country needs to invest R$6.1 billion a year through 2033 to attain universal drinking water coverage, R$9.1 billion in sanitary sewerage services, R$2.3 billion in solid waste management, and R$6.9 billion in drainage. In water, 83.5% of all Brazilians and 93% of the urban population have access to piped distribution.[82] However, these high levels of coverage compared to other Latin America and the Caribbean countries do not reflect the inequality in access. Most of the shortfalls are in the North (57.5%) and Northeast (73.3%). Just 46% of Brazil's urban population has access to sewage collection and treatment services, 12% use individual systems,[83] and 18% have their sewage collected without treatment, while 24% have no sanitary sewerage service. While 98.6% of residences have trash collection service, its adequate disposal continues to be a challenge. About 3,000 open-air dumps are in operation today and receive 41.6% of all trash sent for final disposal.[84] The sanitation sector suffers from problems of governance, uncertainty, and scattered regulations that act as barriers to investment, result in high service costs, and attract political interference. These problems are most serious in water resource management, where the challenge is to achieve consistency between management policies and uses in different sectors (agriculture, energy, sanitation, land use, environment, and ecosystem services).

3.14 **Urban mobility.** Brazil is the eighth most congested country in the world, according to a ranking in which the city of São Paulo occupies sixth place.[85] Congestion-related costs in the city of Rio de Janeiro alone amounted to R$30 billion in 2018.[86] Furthermore, Brazil has one of the highest rates of motor vehicle fatalities in Latin America and the Caribbean, with 23.2 deaths per 100,000 population.[87] The CDC indicates that restricted urban mobility imposes environmental costs and has a negative impact on the climate change goals of

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[79] Impacto de las paradas en la generación hidroeléctrica de Brazil [Impact of shutdowns on hydroelectric generation], Nogueira, Manoel Fernandes Martins, et al.

[80] United Nations Framework Convention on Climate Change (UNFCCC), 2016. Brazil's First NDC.

[81] Removing barriers to financing energy efficiency in Brazil, Conselho Empresarial Brasileiro para o Desenvolvimento Sustentável (CEBDS) [Brazilian Business Council for Sustainable Development].

[82] National sanitation information system (SNIS), 2018.

[83] Plano Nacional de Saneamento Básico [National Basic Sanitation Plan].

[84] Abrelpe, 2017.

[85] INRIX 2018 Global Traffic Scorecard, 2017.

[86] Firjan, 2014.

[87] IDB, 2017. Average for Latin America and the Caribbean: 19.2; the United States: 10.6; and Canada: 6.

reducing greenhouse gases by 37% by 2025 and 43% by 2030.[88] Inadequate planning is the main urban challenge. Above all, poorly integrated urban development policies are a key challenge for improving mobility and strengthening public transportation systems. Uncontrolled urban growth lengthens travel times. By law, all cities with more than 20,000 inhabitants (3,065 cities in all) are required to have a mobility plan but in 2016, just 171 cities (9% of the total) had one,[89] owing to limited technical and institutional capacity.[90]

3.15 **Strategic objectives and action areas.** To improve the business climate and narrow gaps in infrastructure for enhanced competitiveness, the country strategy proposes the following strategic objectives: (i) promote greater economic competitiveness; (ii) increase the role of the private sector by improving the quality of the business environment; and (iii) facilitate public and private investment in infrastructure. The IDB Group will prioritize actions that contribute to a reform of the tax system, including better tax management. To increase financing for the private sector, the IDB Group will support actions to develop and adopt new financial technologies and projects, promote innovation ecosystems, and develop capital markets and long-term financing instruments for infrastructure. As for the development of PPPs, the IDB Group's actions will focus on planning, transparency, use of guarantees, risk management, and bolstering institutional capacity, particularly among subnational governments.

3.16 From a sector standpoint, the IDB Group will support the government in improving the quality of general infrastructure by building institutional capacity for planning and investment. In the area of **transportation and logistics**, the IDB Group will prioritize the development of multimodal transport systems, modernization and expansion of climate-resilient infrastructure, and operating efficiency, to support competitiveness in international trade. In **energy**, the IDB Group will promote policies and investments to diversify the matrix and increase the role of renewable energy sources, encourage the use of innovative solutions, and promote regional energy integration. In **water and sanitation infrastructure**, the IDB Group will focus on improving access to sustainable basic sanitation services, supporting service delivery operating conditions, and creating more climate and environmental resilience with a social inclusion focus in environmental sanitation and watershed protection to safeguard sources. Lastly, in **urban mobility**, the IDB Group will support the implementation of effective mobility plans, promoting a general shift toward more sustainable modes with low emissions and the use of new technologies.

2. Promote international and national integration to boost productive capacity

3.17 **Integration is particularly vital in a country of continental dimensions and great diversity such as Brazil.** Closer international and national integration can enable the country to explore productive synergies and tap competitive advantages, promoting the efficient allocation of productive resources while simultaneously reforming economic relations to support higher productivity.

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[88] Target included in the country's NDC.

[89] Ministry for Cities, 2017.

[90] Nassar, 2018.

Internationally, Brazil presents different barriers to integration with other markets that have a negative impact on productivity and growth. The domestic market is not totally integrated either, with differences between geographic regions. The Southeast accounts for 53.2% of the country's GDP, compared to the North with 5.5%, which translates into a difference in per-capita GDP between the Southeast (R$37,771.26) and the North (R$18,325.33).

3.18 **Brazil's economy remains relatively closed.** The CDC notes that the legacy of trade protectionism in the country held back its global competitiveness and productivity gains.[91] Despite some opening up in the 1990s, the economy continues to be relatively closed. Brazil is one of the few countries that has not significantly lowered its tariffs on trade in the last 20 years, a period that was marked by intensive liberalization of global trade and the signature of trade agreements around the world. Brazil's tariffs on capital goods are punitive, with a negative impact on the country's supply potential.[92] In addition to being high, tariffs are widely dispersed which makes access to good-quality production inputs costly and distorted.

3.19 **Nontariff barriers and bureaucratic red tape also limit Brazil's international integration.** Compared to international standards, Brazil imposes a large number of nontariff barriers such as sanitary rules, technical regulations, and national content policies.[93] The country's manufacturing sector is protected by nontariff barriers that are higher than the global average,[94] and the country ranks 106th out of 190 economies in terms of international trade facilitation, according to the World Bank's 2019 Doing Business Report. In a 2014 survey conducted by the CNI,[95] 44% of companies identified red tape at customs as one of their main problems, citing excessive demands for documents, lack of communication between the different agencies involved, generally slow and unpredictable processes, and delays in customs inspections.

3.20 **Brazil is not just poorly integrated with the rest of the world, but also internally, promoting internal disparities in its economic and social development.** States in the country's North and Northeast do not have strong physical or economic ties with the main centers in the Southeast and South, and their competitiveness levels are among the country's lowest (CDC 2018). The

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91 There is ample literature linking Brazil's productivity to trade liberalization. Studies based on company data indicate that growth in TFP in the country's manufacturing sector in the second half of the 1990s can be attributed to trade liberalization at the start of that decade. Broadly speaking, the results suggest that the more exposed companies are to foreign competition and the greater their access to foreign inputs, the more their productivity increases. See Rossi and Ferreira (2003) and Muendler (2004).

92 A recent analysis by the SAE (2018) shows that a reduction in tariffs would increase trade volume and economic efficiency.

93 United Nations Conference on Trade and Development (UNCTAD), 2013. In a world of dense value chains and just-in-time management, it is difficult to overestimate the importance of reducing border crossing times. Optimization of trade regulations and a guarantee they will be effectively applied by customs and other border agencies are fundamental for trade facilitation. Risk-management systems, authorized economic operators, simplified postal export regimes, electronic one-stop windows, simplified transit schemes, and cooperation among border agencies can facilitate trade and reduce import and export times.

94 SAE, 2018.

95 CNI, 2014.

Southeastern and Southern states are among the most competitive and have higher per-capita income levels. Ninety-nine percent of the 500 cities with the best development indicators are located in the Southeast, South, and Center-West regions, while more than 97% of the 500 least-developed municípios are concentrated in the North and Northeast. These regions must, out of necessity, integrate with the more productive sectors of the national economy to tap their competitive advantages and lay the groundwork for increasing their income levels and reducing inequality. Brazil's natural capital can be a factor in low-carbon-emission economic diversification and dynamism if used appropriately. Furthermore, ecosystems like the Amazon which straddle borders provide a platform for regional integration and continental unification.

3.21 **Insufficient infrastructure, scant institutional capacity, and limited access to financing are the main challenges to building a sustainable economy for the less-developed regions.** Deficient transportation and connectivity infrastructure hamper the sustainable development of those regions. Limited access to low-cost financing and long-term capital form a barrier to the promotion of sustainable financing in depressed regions. Local financial institutions are conservative in their lending and have little appetite for risk. This is compounded by institutional and managerial weaknesses in regions that are trailing economically.

3.22 **According to the 2018 national economic and social development strategy,**[96] **the North and the Northeast are less competitive and diversified.** Nonetheless, these regions have the potential for building a low-carbon, climate-resilient economy, based on the sustainable use of biodiversity and natural resources.[97] Brazil's biodiversity offers a comparative advantage in the development of biotechnology and the bioeconomy in general. Natural capital is the region's most valuable production factor. If global demand continues to favor ecologically-sustainable production methods, a new environmentally responsible model that guarantees sustainability and traceability standards could leverage the comparative advantages of those regions and boost their competitiveness. Sectors such as tourism could also be a significant source of revenues and inclusive development, with a focus on vulnerable populations.[98]

3.23 **Although agriculture is a central sector in the North and Northeast, it poses significant productivity, competitiveness, and sustainability challenges.** The CDC notes that sustainable agriculture could be a path to increasing the competitiveness of less developed regions by creating jobs and income. However, the sector presents different challenges. In the last 10 years, substantial

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96 Ministry of Planning, public consultation (2018).

97 For example, with close to 55,000 different species, Brazil's flora represents one fourth of global diversity and is the most varied in the world (Lopes, 2012).

98 "In contrast with other service-exporting activities, in the case of tourism consumption, visitors are the ones that travel to the location of production/service delivery (the destination), coming into direct contact not only with tourism enterprises, but also the local population. In addition, tourism is a labor-intensive sector. These characteristics mean that (i) a high percentage of value added needs to be produced in the destination itself; (ii) the local population (including the most disadvantaged groups) can have direct access to foreign exchange and tourism expenditure as providers of tourism services; (iii) tourism services help to create local employment; and (iv) some of the supplies for the sector can be sourced locally." IDB, Tourism Sector Framework Document, Washington, D.C., July 2017.

agricultural losses have been incurred as a result of the introduction of at least 35 new pests. Furthermore, the expansion of farming has been the main driver of land-use change (deforestation), greenhouse gas emissions, and water pollution. In the depressed states and in the North and Northeast regions in particular, much remains to be done in the areas of agricultural research, technical assistance, rural extension, credit programs, irrigation infrastructure, road connectivity and logistics. Institutional and organizational restrictions have reduced the impact of some agricultural and rural programs. Finally, climate change represents one of the greatest risks for the future of agricultural productivity.[99]

3.24 **Strategic objectives and action areas.** To promote international and national integration that will in turn boost the country's productive capacity, the following are proposed: (i) promote trade liberalization; and (ii) integrate the country's less developed regions. To move ahead with the first strategic objective, the IDB Group will promote: the adoption of a multidimensional approach to reducing trade barriers; implementation of a regional trade agenda; access to the largest global markets; reduction of bureaucratic obstacles to international trade; and attraction of foreign investment. As for the objective of integrating less developed regions, the IDB Group will support comprehensive territorial proposals that include innovative forms of financing and the adoption of comprehensive sustainable development plans in states and metropolitan areas, with public and private participation, and the use of public policies to spur sustainable production methods. Special attention will be paid to comprehensive development plans for regions such as the Amazon, considering the need for conservation and use of their environmental goods and services. In rural and agricultural development, the focus will be on institution building, development of technical assistance programs, private-sector development, the supply of credit, and the development of financing instruments and markets, including the consolidation and growth of the market for climate bonds.[100]

3. Build a more effective public sector that promotes fiscal sustainability

3.25 **The country presents structural challenges for fiscal sustainability.** Brazil faces serious fiscal sustainability challenges and to solve them it needs to reduce expenditures, improve public sector investment management, and address the challenges of the subnational governments, particularly on the fiscal front, which are urgent and critical tasks. Lastly, transparency in the use of public resources should be stepped up as a tool for social accountability, combating corruption and supporting the necessary fiscal reforms.

3.26 **Public sector expenditure is higher than the international standard.** Spending on benefits for private sector employees covered by the General Social Security

[99] Recent projections of the impact of climate change on Brazilian agriculture by 2050 suggest that the sector will face acute losses. A temperature increase of 3°C or more would be enough to make large areas of land currently under cultivation unproductive (Assad et al., 2017). A study by Margulis and Dubeux (2010) shows that a majority of crops (cotton, rice, coffee, beans, and corn) would be negatively impacted by global warming. Sugarcane is the exception.

[100] These instruments have significant growth potential in the agribusiness, forestry, and energy sectors, considering the country's abundant natural resources, and in the transportation, construction, and sanitation sectors, given Brazil's need for sustainable and resilient infrastructure.

System (RGPS) amounts to nearly 8% of GDP, while spending on public sector employees covered by Special Social Security Regimes (RPPS) is over 4% of GDP, which exceeds the level of every OECD country.[101] As well, substantial tax expenditures total 4.1% of GDP and 19.9% of revenues.[102] Spending on public sector personnel is also high compared to international standards. The federal government's wage bill amounts to 13% of GDP, which is higher than in many comparable countries.[103] The CDC 2018 notes that since 1986, the increase in spending on social security and personnel as a percentage of total public sector expenditure contributed to the reduction in public investment in the country, which is essential to increase its competitiveness.

3.27 **Brazil's public investment management systems are not up to the task of ensuring efficiency.**[104] According to the IMF's Public Investment Efficiency Indicator (PIE-X),[105] Brazil's public investment efficiency indicator (0.61) is below the average for Latin America (0.71) and the emerging markets (0.73). Brazil's efficiency gap is estimated to be 39%, which is much higher than the average for the emerging markets (27%) and Latin America and the Caribbean (29%).[106] Different studies suggest that improvements in the quality of public infrastructure in the G-20 countries can be attributed to solid institutions and the application of effective public management processes,[107] which also heightens the impact of public investment on economic growth.[108] In the Latin American context, actions to improve project selection, optimize infrastructure portfolios, reduce excess costs and delays, and ensure adequate maintenance would generate substantial efficiency gains of more than 1% of potential GDP.[109]

3.28 **Brazil needs to revisit the structure of its fiscal federalism.** Disorderly decentralization of administrative functions and financial flows has distorted the allocation of resources between the different levels of government. The subnational governments do not receive enough money to deliver the public services that are their responsibility (CDC 2018). Collectively, the subnational governments account for 44.1% of total public spending, equivalent to about 24% of GDP. However, the revenues they collect only represent 11% of GDP, which creates large imbalances and makes them highly dependent on intergovernmental transfers. The overlapping of responsibilities between the federal, state, and

[101] Despite the relatively high contribution rates, the combined deficit in the various social security regimes is nearing 4.5% of GDP. This is particularly worrisome in light of Brazil's demographic trends. Although the percentage of the population currently over the age of 65 is relatively low, at about 12%, it is expected to grow rapidly to close to 45% by 2060.

[102] Federal Income Department (2018).

[103] Ter-Minassian (2018).

[104] IDB, 2018.

[105] IMF, June 2015.

[106] IMF, 2015 and 2017. The efficiency gap is the difference between a country's production (a combination of physical indicators and based on surveys of access to and quality of infrastructure) and the production of the most efficient country with the same capital stock.

[107] IMF, 2015.

[108] Furceri and Grace (2017) conclude that higher public investment increases production in the short and medium terms and that the impacts are greater in countries with more efficient management processes.

[109] Serebrisky et al., 2018; IDB, 2018.

municipal governments in key areas such as education, health, and social welfare further complicates fiscal federalism's structure. As a result, subnational governments face serious financial problems and structural challenges related, in particular, to social security and spending on personnel. The financial limitations reduce public investments, with negative social and economic consequences. Although the subnational governments can borrow under a fiscal responsibility framework, the limitations on capacity and fragile institutional mechanisms reduce their effectiveness.[110]

3.29 **Brazil has been slow to adopt innovative e-government technologies to promote transparency and fiscal sustainability, particularly at the subnational levels**. According to the OECD (2014), e-government technologies can promote more open and inclusive processes, spurring more effective participation by the public and private sectors and civil society in policy formation, in the design and implementation of public services, and in the creation of a culture guided by data use and transparency. The CDC 2018 points out that the country needs to use new technologies to improve the supply of public services. In the 2018 United Nations e-Government Development Index, Brazil ranks 44th out of 193 countries, behind Uruguay, Chile, and Argentina in the region. That index measures the motivation and capacity of national governments to use information and communication technologies in the delivery of public services.

3.30 **Strategic objectives and action areas**. To build a more effective public sector that promotes fiscal sustainability, the country strategy proposes the following objectives: (i) reform the structure of public expenditure; (ii) improve the public investment system; and (iii) promote e-government and digital solutions to foster transparency, accountability, and efficiency in delivering public services to citizens and enterprises. Specifically, the IDB Group will seek to help build a more effective public sector that promotes fiscal sustainability. The IDB Group's programs will support lower growth in different types of expenditure, for example in the context of pension system reform and other actions that help boost public investment efficiency, supporting the adoption of medium-term budget frameworks.[111]

4. Reduce social inequality and inequality of opportunity by enhancing public policy efficiency

3.31 **Brazil's results in reducing social inequality and inequality of opportunity are unsatisfactory.** In the 2015 Programme for International Student Assessment (PISA), 70% of Brazilian students did not meet the minimum proficiency level in mathematics. This percentage is significantly higher than in Chile (50%) and Peru (66%). In the health sector, life expectancy at birth in Brazil (75 years) is lower than in Chile (79 years), Uruguay (77 years), and Mexico (77 years).[112] Insecurity has reached crisis levels and affects the most vulnerable classes in particular, as indicated by the figure of 60,000 homicides a year, with 71% of the victims being

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110 Manoel and Garson, 2016.

111 See CDC 2018 for a breakdown of implementation.

112 IDB, 2018. Recent studies show that Brazil's health system leaves ample room to improve efficiency on the basis of international comparisons and the relative performance of different states and municípios.

Afro-Brazilians. Access to housing is a growing problem. Brazil still has a shortage of more than 6.5 million housing units. Broadly speaking, the digital technology gap holds back vulnerable groups and sharpens inequality.[113]

3.32 **The challenge of reducing social inequality and generating opportunities is affected by the weak performance of government and low levels of social spending effectiveness and efficiency.** Brazil spends more on health and education than other Latin American countries. Its budget for education accounts for 5.6% of GDP, which is much higher than the regional average of 4.6%, and its public spending on health is 5.1% of GDP, while other countries in the region spend 3.4% of GDP. These public spending levels do not translate into good performance indicators. Brazil ranks 99th out of 193 countries in terms of government efficiency. By this indicator, Brazil has not improved at all since 1996 and has deteriorated since 2013. Public policy formulation faces structural problems that contribute to low growth and high social inequality. Spending on health and education, for example, account for 28% of the central government primary expenditure. These costs have grown quickly in recent decades, driven in part by the minimum spending levels constitutionally imposed on the two sectors. International comparisons based on a data envelopment analysis indicate that Brazil could gain more than five years of healthy life expectancy (a commonly used health indicator), simply by improving efficiency while maintaining current per capita spending levels.[114]

3.33 **The poor quality of spending on education creates social inequality.** Education in the country suffers from weak intergovernmental coordination (CDC 2018). The overlapping of services spurs state and municipal schools to compete for student enrollment, to the detriment of the efficiency of spending on public education. Resources are not distributed with an eye to results and to benefiting students. Curricula are not exhaustive or consistent and the skills taught by the education system do not reflect labor market demand. The technical and vocation education systems are deficient and do not prepare students to compete in a dynamic job market. In a recent study, 67% of the companies surveyed mentioned inadequate workforce skills as a major drawback for productivity. A recent evaluation[115] showed that the technical skills programs offered by the Ministry of Labor did not achieve the expected results and only a limited number of courses offered by the Programa Nacional de Acesso ao Ensino Técnico e Emprego (PRONATEC) [national access to technical education and employment program] reflect private sector demand for job skills.[116]

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113 The public job placement system also exhibits significant disparities around the country in terms of efficiency, and the technical and vocational education systems are generally deficient and do not prepare students to compete in a dynamic labor market.

114 OECD, 2018. Economic Reports-Brazil, September 2018.

115 The projects evaluated were: Plano Nacional de Qualificação do Trabalhador (PLANFOR) [national worker qualification plan], Programa Nacional de Estímulo ao Primeiro Emprego (PNPE) [national first job incentive program], Plano Nacional de Qualificação (PNQ) [national vocational qualification program], and Programa Nacional de Inclusão de Jovens -ProJovem) [national youth inclusion program].

116 O'Connell, 2017.

3.34 **In the area of public health, Brazil has one of the region's most complex service delivery models (CDC 2018).** Despite the growth in primary care under the family health strategy (ESF), the system does not effectively cover demand for primary services.[117] Assuring access to quality services requires the coordination of responsibilities at the municipal, state, and federal levels, which is poor at present. The recent progress in medical technology and the incorporation of information and communication technologies in the health sector could boost efficiency, facilitating remote monitoring of convalescents and treatment in the home.

3.35 **Citizen security and combatting violence are Brazil's most serious public policy challenges (CDC 2018).**[118] With over 60,000 homicides a year, Brazil has 42% of all homicides in Latin America and the Caribbean. Just 123 municípios account for 50% of the county's homicides. Seventy-five percent of victims are young people between the ages of 15 and 24, mainly male Afro-Brazilians living in urban fringes. Out of 81 countries, Brazil presents the fifth-highest rate of femicide.[119] Over the last decade, robbery rates increased from 15.5% to 23.9%, while the perception of neighborhood insecurity jumped from 33% to 51%. Shortcomings in public security policies heighten the challenges in addressing crime and violence. The huge volume of court cases, coupled with the low level of digitization and automation in proceedings that can take years to complete add to public expenditure, deepen legal insecurity and economic inefficiency, and contribute to prison overcrowding. The incarceration rate has nearly tripled over the last 15 years and Brazil's penitentiary system is extremely congested, with more than double the number of prisoners it can accommodate and high criminal recidivism rates.[120]

3.36 **The public job placement system (SPE) is highly disparate in its efficiency, with an impact on inequality and access to opportunities.** The private sector has difficulty in contracting workers. In Brazil, it takes nearly twice as long (nine weeks) to fill a vacancy with a qualified worker than the average in the Latin America and Caribbean countries (five weeks).[121] This challenge can partly be explained by the poor efficiency of the public job placement system. A recent study using an efficiency index for the efficiency of matching skills to jobs in the SPE identified significant differences, and therefore room for improvement, among the different SPE offices.[122] The recent Law 13,667/18 creates results-based financing mechanisms for more than 2,000 SPE offices at the state and municipal levels. It

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[117] The ESF has national coverage but reaches just 62.5% of the population, with significant gaps in the major cities that were late to join, where coverage is between 35% and 55%. In many of these cities, the public tends to seek emergency services in hospitals, which is a costly, resource-intensive environment.

[118] The homicide rate, which was 11.7 per 100,000 population in 1980, rose to 26.6 in 2007, and to 30.5 in 2016.

[119] World Health Organization (2017).

[120] Institute for Criminal Policy Research (ICPR) (2018) http://www.prisonstudies.org/country/brazil.

[121] Aedo and Walker, 2012.

[122] Albuquerque et al., (2018). Data envelopment analysis has been traditionally used to estimate the efficiency frontier of SPE offices and distinguish the more efficient units from the less efficient.

also requires the standardization of job referral services and better integration with unemployment insurance and vocational training.

3.37 **The country's main housing policies face the challenge of reducing the shortage of low-income housing (CDC 2018)**. The 2010 national census points to a housing shortage of 6.5 million units, affecting close to 12.1% of Brazilian families. Evaluations of the Minha Casa Minha Vida (PMCMV) [my house my life] program, which requires 40% of new units to be reserved for families earning less than two minimum wages, indicate that in most cities just 5% of projects were set aside for families at this income level.[123] Furthermore, the PMCMV units located in fringe areas can end up costing more than expected.[124]

3.38 **Strategic objectives and action areas.** To reduce social inequality and inequality of opportunity by enhancing public spending efficiency, the country strategy establishes the following strategic objectives: (i) build a more effective government; (ii) improve management and the quality of spending and infrastructure in the health and education sectors; (iii) enhance the effectiveness of citizen security services; (iv) raise the efficiency of the public job placement system; and (v) implement efficient policies to increase access to housing. In this context, the IDB Group will support the creation of more efficient financing mechanisms under better institutional coordination on all levels of government. The IDB Group will seek to help boost the efficiency of education through policy reforms and the development of institutions and tools to improve efficiency and equity of access, attention to market demand for vocational and technical skills, and access to innovative private-sector technologies that provide novel educational solutions. In health, it will help to reorganize the service delivery model to strengthen primary care,[125] with an approach that prioritizes health promotion and disease prevention for proactive management of chronic conditions. In citizen security, the development of comprehensive public security policies will be prioritized, with a focus on areas, individuals, and behaviors that pose high criminal risk. To improve employment conditions, the IDB Group will help to promote training and learning models that increase the supply of skilled labor and facilitate entry into the workforce. Lastly, actions to reduce the housing shortage will be promoted, centering on implementing housing projects based on metropolitan mobility, access to the workplace, environmental sustainability, and quality of life.

Crosscutting themes

3.39 **The country presents significant inequalities in terms of gender and race.** Women make up half of the population and 54% of Brazilians self-declare as Afro-

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[123] Cardoso, 2013.

[124] Cepesp-FG, 2018. The Getúlio Vargas Foundation (2018) compared two housing complexes in the metropolitan region of São Paulo, the first 16 kilometers and the second 79 kilometers from the city center. The authors calculated the total costs, including the direct and indirect costs of the program (government subsidies, tax exemptions, environmental offsets, cash contributions, land, and other public contributions) necessary for the financial close of the project. The study found that the complex furthest away from the city center entailed a maximum price difference per square meter of 27%, even though construction costs were the same.

[125] Different studies show a link between the family health strategy and a reduction in hospitalizations for ambulatory care sensitive conditions (ACSC), including chronic conditions.

descendants (black or brown), but gender and race inequality persist in the areas of income, education, and access to the job market (CDC 2018). In recent years, the government adopted different measures and plans to reduce these inequalities but evidence suggests that their effectiveness has been limited.[126] The IDB Group will continue to support initiatives targeted to vulnerable groups. Gender and racial equality will be promoted in access to financing and in entrepreneurial activities led by women and Afro-Brazilians.[127] To reduce social inequality and inequality of opportunity, the gender and diversity perspective will be incorporated into the effort to boost public policy effectiveness.

3.40 **Environmental considerations should figure prominently on the sustainable development agenda.** Like the rest of the region, Brazil is vulnerable to climate events and their negative impact on economic and social development.[128] The country is the region's main greenhouse gas emitter owing to changes in land use and has established the target of reducing emissions by 37% by 2025 compared to their 2005 level, as part of the commitment established in its NDC. Therefore, folding environmental considerations into the development agenda and broadening environmental policy beyond conservation to include productivity gains associated with responsible use of the country's natural capital are essential for constructing a sustainable development model.[129]

3.41 **National environmental and social systems.** Brazil has an advanced legal framework in environmental and social affairs. However, the country's decentralized federal nature and the complexity of its institutional structure pose challenges for implementing systems at the federal, state, and municipal levels. Therefore, the IDB Group will help to strengthen the country's environmental and social systems to improve their consistency and effectiveness.

3.42 **Competitiveness is linked to the country's capacity to generate and adapt to new technologies.** An emerging digital economy is bringing about deep changes in production models, the labor market, and living standards. Leveraging the potential of the new economy as a driver of economic development demands a forward-looking effort that seeks to transform the country into a producer (and not just a user) of technological solutions. The CDC 2018 stresses that most Brazilian workers are not ready to benefit from or contribute to the emerging digital economy and that the adoption of technology will depend on efforts to prepare the workforce and improve education. The technologies of the fourth industrial revolution (such as advanced digital production and the new knowledge in life sciences) offer an opportunity to raise productivity in some of the most relevant sectors from the

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[126] These policies include efforts to ensure the basic rights of Afro-Brazilians, incorporating their racial perspectives into sector policies, for example the establishment of quotas for access to public universities. The country recently completed its first national women's plan (2012-2015) as part of its efforts to correct gender inequality. However significant differences persist and social policies should focus on equal access to opportunities.

[127] Heath and Jayachandran (2016) show the positive impact of support for women.

[128] Climate Future Initiative (CFI), 2016.

[129] Climate change has aggravated the country's social challenges. The World Bank estimates that it could force 400,000 Brazilians into poverty (living on less than US$2 per day) by 2030. (Hallegatte et al., 2015).

standpoints of economic growth, public services, and private sector participation, including financial services, manufacturing, health, education, and agriculture.

IV. ESTIMATED LENDING FRAMEWORK

4.1 During the 2019-2022 country strategy period, the IDB estimates approvals averaging US$1.8 billion a year and annual disbursements of close to US$1.75 billion. Support will also take the form of national and regional technical-cooperation projects and remunerated advisory services. The new flow of loans will be about US$515 million annually. As a result, the country's debt with the IDB will be US$17.2 billion or 1.22% of its total public debt and 26% of its external public debt. Moreover, IDB Invest loans and technical assistance are expected to play an increasingly prominent role in the IDB Group's exposure to Brazil and facilitate resource leveraging to speed up economic growth and investment. IDB Lab will also facilitate synergies between the public and private sectors, spurring the development of innovative, high-impact operations.

V. STRATEGY IMPLEMENTATION

5.1 **IDB Group coordination.** Coordination between the IDB, IDB Invest, and IDB Lab will be based on the following parameters: (i) joint implementation of this country strategy; (ii) planning of joint missions for relations with the authorities and public and private clients, particularly in areas requiring policy reforms and/or identification of synergies for complementary work, especially in implementation of PPPs and concessions; (iii) promotion of crosscutting innovations and adoption of technological solutions; (iv) design of comprehensive sustainable development plans; (v) organization of joint dialogues; and (vi) maximization of operational synergies.

5.2 **Strategy implementation.** In accordance with the recommendations set out in OVE's evaluation, the IDB Group will implement the country strategy developing individual business models for each type of borrower (federal government, states, municípios, private sector, and public financial institutions). Specifically, the Bank will facilitate operations that make it possible to: (a) participate in and contribute to the discussion and formulation of federal public policy, increasing its participation through lending (policy-based loans and/or results-based loans) and technical assistance for federal ministries in charge of the areas prioritized by the country strategy and in their relations with the subnational entities; (b) continue to support subnational governments through lines of financing to help implement federal strategies, including direct investment operations for states and municípios or through federal and regional public banks; and (c) support the states in generating a larger aggregate impact through the participative formulation and implementation of comprehensive sustainable development strategies. In addition, IDB Invest's role as a catalyst for financing will be consolidated.

5.3 **Coordination with other donors**. Efforts to coordinate with the federal government will be monitored to facilitate participation in cofinancing by different multilateral and bilateral agencies, considering client demand for promoting the use of the procurement, financing, and socioenvironmental safeguards of one of the cofinancing institutions. Moreover, all cofinancing participants should have a standard loan contract agreed upon with the federal government. In a new scenario of greater openness to technical assistance by the federal and state governments, the IDB Group will promote the coordination of efforts to generate dialogues and policy proposals based on technical synergies among multilateral and bilateral agencies, seeking to add new sources of financing and technical expertise for our clients. Another good opportunity for coordination lies in the production of comprehensive sustainable development plans for the states that will foster participation by those agencies in the project development and cofinancing stages. The IDB Group will monitor dialogue and operational coordination in areas such as: (i) water and sanitation with the Japan International Cooperation Agency (JICA) and the Kreditanstalt für Wiederaufbau (KfW); and (ii) urban development with Agence Française de Développement (AFD).

5.4 **Project implementation.** To obtain an improvement in the quality of its portfolio of operations, the IDB will continue to implement specific strategies to use loan proceeds effectively, in cooperation with the Ministry of Economic Affairs. The actions include: (i) increasing the original timeline for the last disbursement by a maximum of 50%; (ii) only projects classified as "satisfactory" will be eligible for that increase; and (iii) for projects on "alert" status, time extensions will be conditional. As well, the use of project managers will be rationalized when warranted and duly justified and not contrary to the objective of strengthening borrowers' project executing units. As for operating costs, efforts to reduce them will be monitored by automating processes and focusing Bank supervision on activities and processes posing the greatest risk.

5.5 **Strategic use of technical cooperation.** Country strategy implementation will also be supported by the strategic use of technical cooperation both to support the country's new demands for knowledge and to facilitate project design and execution. A strategic programming framework will be established for that purpose in coordination with the country that promotes a knowledge agenda, lessons learned, and good practices, with a focus on complex and cutting-edge operations and subject areas.

5.6 **Fiduciary systems**. The most recent assessments of fiduciary systems in Brazil indicate that they are satisfactory for the fiduciary management of Bank-financed projects, in compliance with the principles of transparency, economy, and efficiency. As Table 1 shows, the budget and treasury systems have been used in 100% of Bank projects and the external control system in 54%, which indicates that the greatest challenges continue to be the accounting system, since it does not generate financial reports in foreign currency, and internal audits. The information system is used for all government procurement and up to 80% for shopping. Substantial progress will be proposed in the use of national competitive bidding (NCB).

5.7 The Bank will continue to promote the use of country fiduciary systems at the federal, state, and municipal levels. During the strategy period, support will continue for the audit offices in the process of implementing International Auditing Standards and increasing the use of this external control system in Bank projects from 54% at present to 65%. The Bank will also continue its support for aligning national accounting with the International Public Sector Accounting Standards (IPSAS) and for improving state and municipal integrated financial management systems. As for government procurement, the Bank will support discussions on the rules and implementation of the new legal framework for procurement that includes updating the law and regulations governing e-reverse auctions which are widely used in Brazil and in Bank-financed projects. This will enable the Bank to identify opportunities to strengthen capacity for government procurement of innovative solutions and to develop a specific strategy to involve the respective control agencies.

Table 1. Country fiduciary systems

Use of fiduciary systems	Baseline 2018	Estimated use by the end of the strategy (2022)	Planned actions
Budget	100%	100%	None anticipated
Treasury	100%	100%	None anticipated
Accounting and financial reports	34%	40%	Support for implementation of IPSAS on the federal, state, and municipal levels. Support for organizing the FOCAL 2019 event and follow-up on the agreed actions
Internal audit	13%	15%	Joint actions with the CGU to disseminate and strengthen internal audits
External audit	54%	65%	Validation of the external control systems and certification of new state audit offices
Information system	100%	100%	None anticipated
Shopping	80%	90%	Dialogue with the government to incorporate modern practices into draft legislation
Individual consulting services	0%	0%	Dialogue with the government to incorporate modern practices into draft legislation
Partial NCB[130]	0%	20%	Dialogue with the government to incorporate modern practices into draft legislation
Advanced NCB	0%	0%	None anticipated

VI. RISKS

6.1 **Macroeconomic risk.** The country's fiscal imbalance is a threat to its macroeconomic stability. Brazil is implementing a program of gradual adjustments to improve the fiscal results, stabilize the debt, and strengthen its economic policy framework and market credibility. In this context, the country passed a constitutional amendment limiting growth in expenditure. The measure is insufficient to solve the fiscal problem and fiscal reforms are needed to ensure that the public debt will be sustainable. Reform of the pension system is the key item on the agenda, but there are other issues such as a reduction in budget rigidity and measures to make the public sector more efficient. The fiscal difficulties are not restricted to the federal government. Subnational finances are also in a delicate situation, with some states declaring bankruptcy or accessing financial recovery programs organized by the federal government. Beyond the government's agenda, implementation of the reforms is complex and will demand political capacity to

[130] Despite reporting use of 58%, it was found that that the reporting was of e-reverse auctions for contracts within the shopping threshold of up to US$5 million. It did not correspond to Concorrência Pública Nacional (local equivalent of national competitive bidding). Considering that e-reverse auctions are shopping, the index has been corrected to refer only to national competitive bidding in this measurement.

move ahead. Accordingly, the years covered by the strategy will be filled with challenges. In the current circumstances, the main risks for the Brazilian economy lie on the external front: (i) trade and geopolitical tensions that cause world growth to stagnate; (ii) a faster-than-expected increase in global interest rates that reduces risk appetite for emerging markets, thereby affecting capital flows; and (iii) a sharp slowdown in the Chinese economy that has a significant impact on commodities prices. Internally, a deterioration in expectations of reforms could have a negative impact on market sensitivity which would give rise to further doubts about public debt sustainability, undermining confidence in the country and possibly impeding the economic recovery process. Thus, the external and domestic risks could pose significant challenges for policy formulation and macroeconomic stability. The choice of the strategy's priorities is closely linked to mitigation of the fiscal deficit through strengthening public finances, a larger role for the private sector in the country's growth, and mitigation of socioeconomic impacts through more efficient public policies. The country's economic situation will be monitored periodically through the Bank's economic reports such as the Independent Assessment of Macroeconomic Conditions and macroeconomic reports by the Department of Research and Chief Economist.

6.2 **Execution risk.** The main execution risks faced by the IDB in Brazil include: (i) the low technical and organizational capacity of some executing agencies, particularly at the subnational level; and (ii) changes in the price of the U.S. dollar. The first could have an impact on the physical development and disbursement of operations and, consequently, on the expected results. To mitigate this risk, as part of the project preparation stage, the Bank will conduct an institutional capacity assessment of the executing agency to identify weaknesses that can be addressed from the outset. The IDB holds also periodic meetings in Brazil to review the portfolio which include participants from the federal government, to monitor the execution of operations and reach agreements to guarantee satisfactory performance. It also offers training opportunities for executing agencies.

RESULTS MATRIX

Priority area	Strategic objective	Expected results	Indicator	Baseline, source, and year
Improve the business climate and narrow gaps in sustainable infrastructure for enhanced competitiveness	Promote greater economic competitiveness	Enhanced competitiveness	Global Competitiveness Index score	59.5 (72th out of 140 countries), World Economic Forum (WEF), 2018
	Increase the role of the private sector by improving the quality of the business environment	Improved business climate	Ease of Doing Business Index score	60.01 (109th out of 190 countries), Doing Business, World Bank, 2019
		Simplified processes for opening and closing businesses	Average time to open a business	20.5 days, Doing Business, World Bank, 2019
		Simplified tax payments	Average time used by companies to pay taxes (hours per year)	1,959 hours, Doing Business, World Bank, 2019
		More private sector investment in R&D	Private sector share of R&D investment	45%, UNESCO, 2016
		Increased private sector access to credit	Total credit to the private sector (% of GDP)	43.7%, Central Bank, 2019
		Stronger framework for PPPs	Infrascope Index	70/100, Economist Intelligence Unit, 2018
	Narrow infrastructure gaps	Better quality infrastructure	Global Competitiveness Index 2018 - Infrastructure	64.3 (81th out of 140 countries), WEF, 2018
		Better quality logistics	Logistic Performance Index	2.99 (56th out of 160 countries), World Bank, 2016
		Increased share of renewables (e.g. wind and solar) in the energy matrix	Share of renewable energy (e.g. wind and solar) in the energy matrix	8.8%, National Electric Energy Agency (ANEEL), 2018
		Enhanced energy efficiency	Energy intensiveness of the economy (tons of oil equivalent/10^3R$)	0.040, Energy Research Office (EPE), 2017

Priority area	Strategic objective	Expected results	Indicator	Baseline, source, and year
			Energy distribution and transmission losses[131]	19.2%, EPE, 2017
		Better access to improved water, solid waste, and sanitation services	Percentage of households connected to a piped water system	83.5%, National Sanitation Information System (SNIS), 2017
			Percentage of households connected to a sewer system	64%, SNIS, 2017
			Percentage of households whose sewage is treated	46.0%, SNIS, 2017
			Percentage of households receiving adequate service for the final disposal of urban solid waste	58.4%, Brazilian Association of Public Sanitation and Special Waste Removal Companies (ABRELPE), 2017
			Distribution loss index (volume of unbilled water caused by leakage, breaks, or illegal connections divided by total volume)	38.3%; SNIS, 2017
		Better planning of sustainable urban mobility	Number of cities with sustainable urban mobility plans	193, Ministry for Cities, 2018
Promote national and international integration to boost productive capacity	Promote trade liberalization	Increased trade flow	Exports plus imports divided by GDP	22.4%, Central Bank, 2018
		Lower tariff barriers	Import tariffs (average)	13.6%, Foreign Trade Department (SECEX), 2018
		Less red tape in international trade	International trading across borders index score	69.85 (106th out of 190 countries); Doing Business, World Bank, 2019

[131] Ratio between losses and total supply.

Priority area	Strategic objective	Expected results	Indicator	Baseline, source, and year
	Integrate the less developed regions	Reduction in income disparities between regions	Region's share of GDP	Northeast, 14.3%; North, 5.4%,IBGE, 2016
		Increased competitiveness of the less developed regions based on a sustainable development model	Competitiveness ranking of Brazilian states	North: 38.8; Northeast:40.9; CLP, 2017
Build a more effective public sector that promotes fiscal sustainability	Reform the structure of public expenditure	Reduction in the pension system deficit	Pension system fiscal deficit, General Social Security Regime (% of GDP)	2.84% of GDP, Central Bank, 2018
		Reduction in tax expenditure	Total value of tax expenditure (% of GDP)	4.12% of GDP, Ministry of Finance, 2018
		Control over the increase in the consolidated public sector wage bill	Total expenditure on personnel (% of GDP)[132]	4.1% of GDP, National Treasury, 2018.
	Perfect the public investment system	Greater public investment efficiency	Public Investment Efficiency (PIE-X)	0.61; IMF, 2015
	Promote e-government and digital solutions to foster transparency, accountability, and efficiency in delivering public services to citizens and enterprises	Increased adoption of electronic solutions for public service delivery	e-Government Development Index	0.7327 (44th out of 193 countries), United Nations, 2018
Reduce social inequality and inequality of opportunity by enhancing public policy efficiency	Build a more effective government	More effective public policies	Government Effectiveness Index score	-0.29 (-2.5<Index<+2.5); World Bank, 2017
	Improve management and the quality of spending and infrastructure in the health and education sectors	Better student learning levels	Average PISA score	Science (401); reading (407); mathematics (377), OECD, 2015
			National Human Development Index (HDI) average in the final year of primary school	4.7, National Educational Studies and Research Bureau (NEP), 2017

[132] For the federal government.

Priority area	Strategic objective	Expected results	Indicator	Baseline, source, and year
			National HDI average in the final year of secondary school	3.8, INEP, 2017
		Workers able to compete in a dynamic labor market	Ease of finding skilled workers	38.6 (127th out of 140 countries), WEF Global Competitiveness Report 2018-2019
		Increased life expectancy	Life expectancy from birth	75.5 years, IBGE, 2017
		Improved access to and quality of primary care services	Primary health service coverage (% population)	74.12%, DATASUS, 2018
	Enhance the effectiveness of citizen security services in the control and prevention of violent crimes	Reduction in the number of homicides	Number of homicides per 100,000 pop.	30.33, Violence Atlas, 2016
		Reduction in the number of violent crimes against property	Violent crimes against property per 100,000 population (robbery, vehicle theft, robbery of financial institutions, and theft of freight)	280.1, Violence Atlas, 2016
	Raise the efficiency of the public job placement system	More effective job referrals at public job placement system offices	Effectiveness of referrals using the Web. Ratio between contracted/referred	3%, SINE, 2017
	Implement efficient policies to increase access to housing	Reduction in the housing shortage	Housing shortage	6.355 billion units, Fundação João Pinheiro–PNAD/IBGE, 2018

FIDUCIARY SYSTEMS MATRIX

Strategic objective	Expected outcome	Indicator	Unit of measure	Baseline	Base year	Target	Timeline	Alignment with CRF
Increase the use of country fiduciary systems	Increased use of the external control subsystem	Active portfolio that uses the external control subsystem	Percentage of the active portfolio	54%	2018	65%	End of the country strategy	• Institutional capacity and rule of law • Productivity and innovation
	Increased use of the shopping subsystem	Active portfolio that uses the reverse auction subsystem	Percentage of the active portfolio	80%	2018	90%	End of the country strategy	• Institutional capacity and rule of law • Productivity and innovation
	Increased use of the partial national competitive bidding subsystem	Active portfolio that uses the national competitive bidding system	Percentage of the active portfolio	0%	2018	20%	End of the country strategy	• Institutional capacity and rule of law • Productivity and innovation
Strengthen country fiduciary systems	Strengthened accounting subsystem	Progress in the plan to implement International Public Sector Accounting Standards (IPSAS) in the federal government	Percent progress made on the plan to implement IPSAS within the federal government	59%	2016	100%	End of the country strategy	• Institutional capacity and rule of law • Productivity and innovation
	Regulations approved that are compatible with international practices	Dialogue promoted by the Bank	Number of events	0	2018	3	End of the country strategy	• Institutional capacity and rule of law • Productivity and innovation
	Roundtables with the audit offices to discuss	Action plans generated at the roundtables	Percent progress made on the action plan	0	2018	50%	End of the country strategy	• Institutional capacity and rule of law

Strategic objective	Expected outcome	Indicator	Unit of measure	Baseline	Base year	Target	Timeline	Alignment with CRF
	contracting innovative solutions							• Productivity and innovation
	Public sector manuals for contracting innovation	Manuals in use	Number of institutions using manuals	0	2018	3	End of the country strategy	• Institutional capacity and rule of law • Productivity and innovation
Improve the operating efficiency of the IDB portfolio	Fiduciary network with control bodies implemented	Criteria agreed on with audit offices (e.g. confidentiality, challenges, modifications, price schedule, and arbitration)	Agreements, resolutions, or roundtables	0	2018	3	End of the country strategy	• Institutional capacity and rule of law • Productivity and innovation

MAIN ECONOMIC AND SOCIAL INDICATORS

ECONOMIC AND SOCIAL INDICATORS	2014	2015	2016	2017	2018
Real GDP growth (%) (1)	0.50	-3.50	-3.30	1.10	1.10
GDP at current prices (US$ billions) (2)	2,454.84	1,796.16	1,799.53	2,053.27	1867.91
GDP per capita (US$) (3)	12,026.62	8,750.22	8,639.37	9,821.41	-
GDP per capita (PPP) (3)	16,195.87	15,656.27	15,181.47	15,483.54	-
Gross fixed-capital formation (% of GDP) (1)	19.70	18.00	15.53	14.98	15.83
Gross domestic savings (% of GDP) (1)	16.00	14.24	13.44	14.30	14.55
Unemployment rate (economically active pop. %) (1)	4.30	8.70	11.50	12.70	11.70
Inflation (%) (1)	6.41	10.67	6.29	2.95	3.75
Exchange rate (R$/US$ - end of period) (4)	2.70	4.00	3.25	3.31	3.87
Real exchange rate (end of period – June 1994 = 100) (2)	96.70	122.10	97.55	100.99	109.46
Current account balance (% of GDP) (2)	-4.13	-3.03	-1.33	-0.35	-0.77
Capital and financial account balance (% of GDP) (2)	-4.09	-3.04	-0.90	-0.28	-0.47
Foreign direct investment (% of GDP) (2)	3.70	3.90	4.30	3.70	3.26
Portfolio investment (% of GDP) (2)	-1.69	-1.24	1.06	0.68	0.63
International reserves (US$ billions, end of period) (2)	374.10	367.00	365.02	373.97	374.71
Nominal public sector balance (% of GDP) (2)	-5.95	-10.22	-8.98	-7.8	-7.09
Primary public sector balance (% of GDP) (2)	-0.56	-1.86	-2.49	-1.69	-1.57
Net general government debt (% of GDP) (2)	33.15	37.9	47.79	53.49	55.76
Gross general government debt (% of GDP) (2)	56.28	65.5	69.86	74.07	76.69
SOCIAL INDICATORS					
Population (millions) (1)	202.80	204.50	208.80	210.70	212.60
Income inequity (Gini coefficient) (3)	0.52	0.51	0.53	0.54	-
Poverty (% of total population) (1)	20.00	21.60	23.70	24.50	-
Internet users (% of total population) (1)	54.40	57.50	64.69	69.75	-
Mobile telephony subscribers (% of total pop.) (1)	77.90	78.30	77.09	78.22	-

Sources:
(1) IBGE
(2) Central Bank of Brazil
(3) World Bank
(4) Bloomberg

INDICATIVE LENDING FRAMEWORK

	2014	2015	2016	2017	2018	2019	2020	2021	2022	Average 2019-2022
Approvals	1,741.9	56.0	1,196.8	1,495.4	2,391.2	1,450.0	1,700.0	2,000.0	2,200.0	1,837.5
a. Disbursements	1,772.8	1.110.0	1,080.2	1,766.7	2,025.0	1,600.0	1,600.0	1,800.0	2,000.0	1,750.0
b. Repayments	889.8	999.3	1,017.4	1,079.5	1,368.0	1,268.9	1,242.7	1,227.4	1,198.1	1,234.3
c. Net loan flows	883.0	110.7	62.8	687.2	657.0	331.1	357.3	572.6	801.9	515.7
d. Subscriptions and contributions	3.6	51.8	83.1	3.4	-	-	-	-	-	-
e. Interest and fees	254.8	255.2	349.4	358.5	467.0	547.2	538.1	509.1	478.5	518.2
f. Net cash flow	624.6	-196.3	-369.7	325.3	190.0	-216.1	-180.8	63.5	323.4	-2.5
IDB debt	13,572.1	13,697.5	13,776.3	14,485.2	15,139.2	15,470.3	15,827.6	16,400.2	17,202,1	
IDB debt/multilaterals (%)*	33.9%	33.8%	34.2%	35.1%	37.0%	37.8%	38.6%	40.0%	42.0%	
IDB debt/external public debt (%)	18.0%	21.4%	19.6%	20.2%	22.0%	22.1%	22.6%	23.4%	24.6%	
IDB debt/gross central government debt (%)	1.11%	1.36%	1.03%	0.99%	1.11%	1.13%	1.12%	1.16%	1.22%	

Source: FINSOL.
*Authors' estimates for 2019 and after.
Note: Amounts subject to Bank Ordinary Capital availability. Scenario based on projections as of 31 December 2018.

DEVELOPMENT EFFECTIVENESS MATRIX

COUNTRY STRATEGY DEVELOPMENT EFFECTIVENESS MATRIX	
In August 2008, the Board of Executive Directors approved the Development Effectiveness Framework (document GN-2489) to enhance the evaluability of all Bank development products. The country strategy development effectiveness matrix is a checklist of the elements necessary to evaluate a country strategy. It is based on the evaluation criteria developed by the Evaluation Cooperation Group of the Multilateral Development Banks in the "Good Practice Standards for Country Strategy and Program Evaluation."	
COUNTRY STRATEGY	
STRATEGIC ALIGNMENT This refers to the degree to which the design and objectives of a country strategy are consistent with the country development challenges and with the government's development plans and priorities. EFFECTIVENESS This measures whether the country strategy is likely to achieve its intended objectives, through an examination of three dimensions: (i) the quality of the diagnostic assessment on which Bank action is based in each area of work; (ii) the quality of the results matrix for the strategy; (iii) the use and development of country systems.	
Effectiveness dimensions	
I. Country diagnostic assessment – Country Development Challenges (CDC)	Yes/No
- The CDC clearly identifies the main development challenges prioritized in the country strategy	Yes
- The main development challenges included in the country diagnostic assessment are based on empirical data	Yes
II. Diagnostic assessment of priority areas**	%
- Identifies the main limitations and difficulties involved in the **priority areas**	100%
- Identifies the **main factors/causes** that contribute to the specific obstacles and challenges	100%
III. Results matrix*	%
- The strategic objectives are clearly defined	100%
- The expected outcomes are clearly defined	100%
- The strategic objectives and expected outcomes are directly related to the main constraints identified in the diagnostic assessment	100%
- The indicators are outcome indicators and are specific, measureable, achievable, realistic, and timely (SMART)	100%
- The indicators have baselines	100%
IV. Vertical logic	
- The country strategy has vertical logic	Yes

* The results matrix is comprised of indicators that are meaningful to, and capture progress towards, the expected outcomes. The expected outcomes stem from the strategic objectives.

** The country strategy includes the Country Development Challenges document.

Country strategy diagnostic assessment

As part of the country strategy, a country development challenges diagnostic assessment was presented (see the link containing the Country Development Challenges). This diagnostic assessment of development challenges is comprehensive and based on empirical evidence. It identifies four priority areas for the Bank's intervention: (i) improve the business climate and narrow gaps in infrastructure for enhanced competitiveness; (ii) promote national and international integration to boost productive capacity; (iii) build a more effective public sector that promotes fiscal sustainability; and (iv) reduce social inequality and inequality of opportunity by enhancing public policy efficiency.

- The diagnostic assessment clearly identifies and dimensions, based on empirical evidence, the specific constraints and challenges for the priority areas.
- It clearly identifies and measures, based on empirical evidence, the main factors or causes contributing to the specific constraints and challenges for the priority areas.
- It offers policy recommendations for Bank action, based on empirical evidence.

Results matrix. The results matrix corresponding to the new priority environment includes 13 strategic objectives for Bank action, 32 expected outcomes, and 39 indicators for measuring progress.

100% of the strategic objectives are clearly defined.

100% of the expected outcomes are clearly defined.

100% of the country strategy objectives are related to the main constraints identified in the diagnostic assessment.

100% of the indicators used are SMART.

100% of the indicators have baselines

Fiduciary systems. Diagnostic assessments are available for all fiduciary subsystems. The Bank will continue using 100% of the country budgeting and treasury subsystems and partial use will be made of the accounting and information subsystem. For procurement, a diagnostic assessment is available for the information system. The Bank will work to strengthen procurement subsystems.

Vertical logic. The country strategy has vertical logic.

Risks. The main risks for implementing the country strategy are: (i) macroeconomic, linked to fiscal sustainability and external shocks; and (ii) execution, linked to low capacity of executing agencies and the exchange risk.

MANAGEMENT'S RESPONSE ON THE COUNTRY PROGRAM EVALUATION OF BRAZIL 2016-2018

OVE recommendation	Management's response
<u>Recommendation 1:</u> **Develop individual business models for working with each type of borrower (federal government, states, municípios, private sector, or public financial institutions), establishing key considerations in each case, such as:** (i) objectives that the IDB Group intends to achieve; (ii) engagement conditions; (iii) potential use of instruments; (iv) areas requiring particular attention or support; (v) replicable factors of success in working with each borrower; and (vi) the way in which activities requiring other borrowers to participate will be coordinated. By way of example, the objectives at the federal level could include: (i) positioning the Bank as a strategic partner on emerging key issues with long-term implications for the country and on which the Bank has experience and knowledge. To this end, the Bank should use instruments such as technical cooperation operations, fee for services, and even loans to the extent that they are able to leverage resources, knowledge, or good practices; and (ii) delineating policy guidelines to orient interventions at the subnational level and enable greater coordination between the federal and subnational levels.	**Agree.** *The IDB Group will continue implementing individual business models, in accordance with the dialogue under way with the government in the framework of the new country strategy with Brazil.* **Actions proposed by Management:** • *Participate in and contribute to the discussion and formulation of federal government policy, enhancing the IDB Group's participation through loans and technical assistance to federal government ministries with responsibility for the issues being prioritized in the dialogue on the new country strategy;* • *Continue the IDB Group's support for the states and municípios, through lines of financing to federal and regional public banks;* • *Create a model to formulate integral sustainable development plans for the states, based on the promotion of production value chains;* • *Continue coordination efforts with the federal government to facilitate cofinancing by different multilateral and bilateral organizations to generate additional value added for clients. The IDB Group will continue to pursue dialogue and operational coordination in the priority areas of the new country strategy: (i) water and sanitation with the Japan International Cooperation Agency (JICA) and Kreditanstalt für Wiederaufbau (KFW); and (ii) urban development with Agence Française de Développement (AFD).* • *Continue implementing the IDB Group's private-sector business model developed in the Renewed Vision by (a) approving the IDB Invest Business Plan 2020-2022; and (b) identifying priority sectors for intervention and support in the country strategy with Brazil 2019-2022.*
<u>Recommendation 2:</u> **Consolidate the efforts to manage the size of the portfolio and explore new mechanisms for assisting executing agencies,**	**Agree.** *We will address this recommendation by continuing the activities implemented over the last three years, which have resulted in a portfolio with 88% of projects rated "satisfactory," in accordance with the project monitoring report dated 31 December 2018.*

considering their institutional capacity, with a view to improving the execution of projects.	**Actions proposed by Management:** • *Continuing the practice of conducting two comprehensive portfolio reviews per year, with the participation of the federal government guarantor (STN and SAIN);* • *Retaining the criteria agreed upon with the federal government to grant extensions of the last disbursement of operations;*[133] • *Improving the quality and capacity of executing agencies to manage projects, providing them with training and good practices in planning and monitoring, fiduciary (i.e. procurement and financial) management, and risk management;* • *Limiting the use of management firms to cases that really generate value added for the executing agency; and* • *Continuing to strengthen management capacities of our operational team.*
<u>**Recommendation 3:**</u> **In the context of new approvals, promote a greater use of available loan instruments, considering the type of project and the executing agencies' experience and capacity.**	**Agree.** *The implementation of this recommendation will be governed by the guidelines being prepared for the new country strategy and those the federal government decides to use for financial and nonfinancial instruments, particularly with subnational entities.*
	Actions proposed by Management: • *Present in programming meetings with STN and SAIN proposals for instruments based on type of project and executing agency capacity; and conduct an exhaustive analysis of the proposed instrument during the eligibility review meetings;* • *Continue promoting the use of policy support instruments for federal sector policies; based on good practices implemented in the use of the CCLIP line, e.g. on fiscal issues, in the use of results-based loans in the agriculture sector; and* • *Promote the use of guarantees and local-currency loans.*

[133] Without exception, the basic criteria agreed upon for authorizing an extension of the last disbursement are: (a) "satisfactory" rating; (b) maximum extension equivalent to 150% of the original period; (c) for operations classified as "alert" or "problem" status, extensions are conditioned on cutting the resources needed to guarantee the execution of the remaining funds in the additional period granted.

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<td rowspan="2"><u>Recommendation 4:</u>

Strengthen coordination between the Bank and IDB Invest and identify cases in which the use of sovereign-guaranteed and NSG financing for the same purposes is justified.</td>
<td>Agree. We will continue strengthening coordination between the IDB, IDB Invest, and IDB Lab.</td>
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<td>Actions proposed by Management:
Coordinate interventions to identify synergies in complementary work, especially with regard to the implementation of private-public partnerships and concessions; in the implementation of sustainable state development plans, and in identifying the type of financing on a case-by-case basis;
Continue promoting crosscutting initiatives in innovation and the adoption of technology solutions, such as developing innovation ecosystems and startups that have received IDB Lab support in different sectors; and
Organize joint dialogue activities, especially in areas requiring policy reforms.</td>
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<td rowspan="2"><u>Recommendation 5:</u>

Emphasize expenditure control and quality considerations in the Bank’s sector work at the subnational level in view of the fiscally restrictive context that will frame the next country strategy.</td>
<td>Agree. The IDB Group will continue working in this areas as will be proposed in the new country strategy currently in preparation.</td>
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<td>Actions proposed by Management:
Promote programs aimed at improving quality, efficiency, and expenditure control in social, fiscal, and digital transformation issues;
Develop a dialogue and coordination agenda on expenditure control and quality with the subnational entities through structures/ agencies such as CONFAZ.</td>
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