Alfredo Saad-Filho

New Dawn or False Start in Brazil? The Political Economy of Lula's Election[1]

This article offers a political-economy interpretation of the transformations in the Brazilian economy and society since 1980, concluding with the Presidential election of Luiz Inácio Lula da Silva in October 2002. Two main issues are considered. First, the transition from rapid growth under import-substituting industrialisation (ISI) to persistent economic stagnation under a new system of accumulation, defined as 'new liberalism'. Second, the article considers, in this context, the meaning and significance of Lula's election.

This article has four sections. The first reviews the weaknesses of ISI and the reasons for its collapse. The second explains the transition to new liberalism and the main features of this system of accumulation. The third analyses Lula's election in the light of Brazil's persistent economic problems, and considers

[1] I am grateful to Sebastian Budgen for the incentive to submit this paper for *Historical Materialism*, and to Sinesio Alves, Maria de Lourdes Mollo, Lecio Morais and Bruno Saraiva for their generous comments. The usual disclaimers apply.

Historical Materialism, volume 11:1 (3–21)

Also available online – www.brill.nl

the potential achievements and the limits of his administration. The fourth section summarises the article and draws the relevant conclusions. The most important conclusion is that the deteriorating performance of the Brazilian economy in the last two decades is the outcome of a range of complex political-economy constraints. They have not been addressed systematically in the transition to the new system of accumulation. In fact, this transition has aggravated some of the existing constraints, and added other important limitations to growth. Therefore, it is unlikely that the Brazilian economy will perform well in the near future. This limitation posits difficult dilemmas for the incoming administration, led by Lula's Workers' Party. In this context, three alternative scenarios for Lula's administration are briefly assessed.

The analysis developed below is limited in two important ways. First, it focuses primarily upon an innovative study of macroeconomic policies and constraints, rather than emphasising the shifting alliances and movements on the ground. This is because the limits and potential achievements of the new administration will be determined by macroeconomic constraints, more than by any other factor. Second, it largely omits the political conflicts within the PT, because they have been settled through the growing hegemony of the party's Centre-Right.[2]

1. From rapid growth to economic stagnation

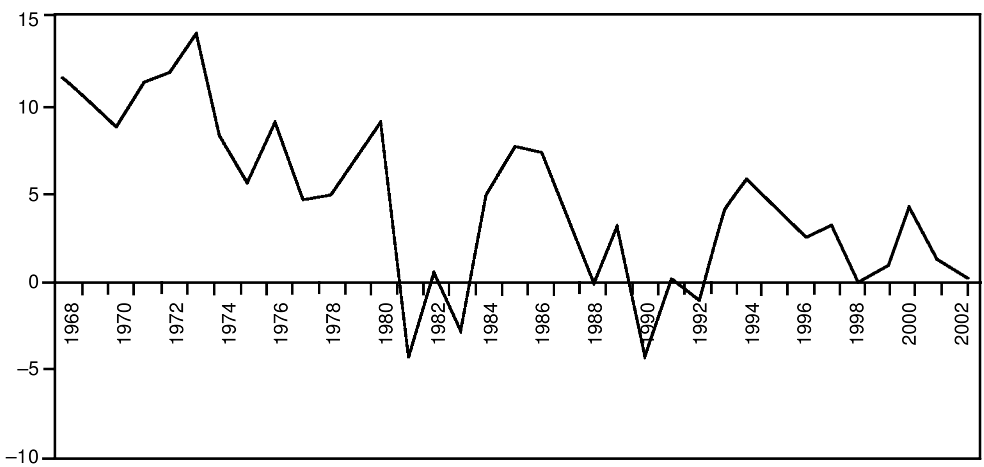
The Brazilian economy is the largest in Latin America, and one of the ten largest in the world. Between 1949 (when records began) and 1980, annual GDP growth rates averaged 7.3 per cent (3.8 per cent per capita), one of the best performances in the world. In the five decades following the Great Depression, the Brazilian economy and society were transformed profoundly and irreversibly. A poor agricultural country, specialised in coffee production and exports, became a large, diversified and relatively wealthy industrial power, capable of exporting aircraft to the United States, durable consumer goods to China, and construction technology to the Middle East.

However, these impressive achievements were not sustained. Growth faltered in the 1980s, and the economy was eventually overcome by prolonged stagnation. In the last two decades, growth rates declined to 1.8 per cent per

[2] The interested reader should consult Branford 2003 and Branford and Kucinski 1995, 2003.

annum (0.6 per cent per capita; see Figure 1 and Table 1), and the country's macroeconomic performance continues to deteriorate as we move into the new century. These worsening indicators are especially disturbing because the distribution of income and wealth in Brazil is one of the worst in the world. As a result, in spite of Brazil's considerable productive capacity, more than fifty million people currently live below the poverty line. Their prospects of material improvement in the short term are not good, at least in the absence of substantial political change (see Section 3).

Figure 1: Brazil: Rate of growth of GDP, 1968–2002 (%)



Source: Conjuntura Econômica.

Table 1: Brazil: Macroeconomic data (1980–2001)

	GDP Growth Rate (%)	Inflation Rate (%)	Current Account (US$mn)	Foreign Debt (US$mn)	Domestic Public Debt (DPD) (US$mn)	Primary Fiscal Deficit (%GDP)	Real Interest Payments on DPD (%GDP)
1980	9.2	90.3	–12 807.0				
1981	–4.3	109.9	–11 734.3	73 963.0			
1982	0.8	95.5	–16 310.5	85 304.0			
1983	–2.9	154.5	–6 837.4	93 556.0			
1984	5.4	220.7	44.8	102 040.0			
1985	7.8	225.5	–241.5	105 171.0			
1986	7.5	142.3	–5 304.1	111 203.0			
1987	3.5	224.8	–1 436.2	121 188.0			
1988	–0.1	684.8	4 174.8	113 511.0			
1989	3.2	1 319.9	2 134.8	115 506.0	48 769.7	1.0	5.9
1990	–4.3	2 740.2	–3 782.3	123 439.0	34 728.8	–4.6	1.5
1991	0.3	414.8	–1 406.8	123 910.0	16 368.2	–2.9	3.3
1992	–0.8	991.4	6 143.7	135 949.0	49 169.5	–2.3	4.4
1993	4.2	2 103.4	–591.7	145 726.0	63 160.5	–2.7	2.4
1994	5.8	2 406.9	–1 688.1	148 295.0	73 106.1	–5.1	3.9
1995	4.2	67.5	–17 971.7	159 256.0	112 536.9	–0.4	5.2
1996	2.7	11.1	–23 136.8	179 935.0	170 995.6	0.1	3.7
1997	3.3	7.9	–30 791.0	199 998.0	229 975.6	0.9	3.4
1998	0.1	3.9	–33 445.0	223 792.0	270 921.6	0.0	7.5
1999	0.8	11.3	–25 396.0	225 609.0	228 633.3	–3.1	7.2
2000	4.3	9.8	–24 669.0	216 921.0	260 122.2	–3.5	4.7
2001	1.5	10.4	–23 213.0	209 934.0	264 140.2	–3.7	5.2

Source: Conjuntura Econômica
* : Negative numbers = fiscal surplus.

Several explanations have been offered for the persistent weakness of the Brazilian economy. Briefly, mainstream economists generally blame the 'populist' economic policies of the developmental state. They highlight the resource misallocation and lack of competition under ISI, the large fiscal deficits and the expansion of state-owned enterprises under the military régime (1964–85), populist welfare expenditures and unrealistic wages in the public sector, and widespread corruption at different levels of government. In contrast, *dependentistas* and structuralist economists generally blame the stagnation upon underconsumption due to the concentration of income, and upon the distributive conflicts which inevitably plague a relatively rich but highly unequal society. They also criticise the external transfers due to the debt crisis and, more recently, trade and capital account liberalisation.

These insights are valuable, but also partial and insufficient. In my view, the recent difficulties in the Brazilian economy are due to structural weaknesses and limitations *both* in ISI *and* in the new system of accumulation imposed in the 1990s, which can be called 'new liberalism'.[3] In what follows, the weaknesses of ISI are explained briefly; the problems associated with new liberalism are reviewed in Section 2.[4]

It is widely known that Brazilian ISI was relatively successful, both in absolute terms and in comparison with similar experiences elsewhere. However, in spite of its remarkable achievements, ISI was severely limited, and the performance of the Brazilian economy was highly uneven between the early 1930s and the late 1970s. The best-known difficulty is the balance of payments constraint. During this period, Brazil was almost continually plagued by a severe scarcity of hard currency, and the lack of foreign savings, investment, technology and market access associated with it seriously impaired economic performance.[5]

This was not the only problem. Two other important difficulties contributed to short-term growth volatility, and to the on-going macroeconomic problems in Brazil. However, they have not been recognised clearly or addressed systematically, and they have persisted to this day.

The first problem is the inefficiency of the financial system. During ISI, the Brazilian financial system was (and it essentially remains) shallow, short-termist and heavily speculative, and it was generally unwilling or unable to fulfil the funding requirements of a rapidly expanding manufacturing sector. Consequently, long-term investment under ISI was funded primarily by foreign direct investment, foreign loans, state-owned banks, directed credit, own resources and inflation. This combination, always fragile, eventually became unsustainable.[6]

The second problem concerns the state. Under ISI, economic growth was based upon the systematic deepening and horizontal integration of manufacturing industry. The state played a key role in these processes. It

[3] The system of accumulation is determined by the economic structures and institutional arrangements that characterise the process of capital accumulation in a specific region, in a certain period of time. This concept is explained by Fine and Rustomjee 1996. The Brazilian case is discussed by Saad-Filho 1998, Saad-Filho, Coelho and Morais 1999, Saad-Filho and Mollo 2002 and Saad-Filho and Morais 2000, 2002.

[4] The term 'new liberalism' highlights the contrast between the new system of accumulation and the oligarchic 'old liberalism' of the early twentieth century, characterised by the hegemony of the coffee sector, foreign ownership of key industries, formal democracy, economic exclusion though oligarchic rule and state repression, and the lack of support for manufacturing industry.

[5] See, for example, Baer 1995, Furtado 1972, Hewitt 1992 and Tavares 1975.

[6] See Studart 1995.

influenced production and investment decisions through specialist agencies and institutions; mediated the relationship between domestic and foreign interests; played a key role in strategic technological development, for example, through the aerospace, defence, computer and nuclear programmes; and subsidised capital accumulation through the provision of cheap credit, infrastructure and inputs produced by state-owned enterprises (for example, steel, oil, gas, electricity, telecommunications, and air, road, rail and port links). In other words, activist industrial policies were an essential ingredient of Brazilian ISI. However, the tax system was never strong enough to support these policies. As a result, fiscal deficits and inflation became a persistent feature of the economic landscape, and the central and local governments accumulated substantial foreign and domestic liabilities.

In sum, the Brazilian state was never 'strong', although it certainly was interventionist. Careful historical analysis shows that the Brazilian state was weak, institutionally disarticulated, and unable to impose a consistent set of long-term policy priorities upon conflicting private interests. In other words, the state was generally unable to exercise the degree of co-ordination required for a successful and sustainable ISI (or, more generally, for *any* coherent and successful development strategy).

The weakness of the state is one of the main reasons why large sections of the Brazilian economy have remained uncompetitive and excessively fragmented. This helps to explain the feebleness of the national system of innovation, which never could upgrade productivity and competitivity across the manufacturing sector. The remarkable success stories in the steel, telecommunications, aircraft and defence industries show what the textile, plastics, toy, wood, beverages and food industries were missing.

For five decades, the economy managed to grow rapidly, if unevenly, in spite of these difficulties. However, in the early 1980s the accumulation of external and domestic difficulties made macroeconomic management extremely difficult. The oil shocks and the international debt crisis worsened the balance of payments constraint and contributed to the development of an acute fiscal crisis, culminating with the slide towards hyperinflation (see Table 1). At the same time, the social conflicts intensified, political instability became endemic, and the military government lost the capacity to select and implement *any* policy, whether economic or otherwise. Economic meltdown seemed imminent, and it was widely agreed that political changes were imperative.

2. The troubled rise of new liberalism

The economic tensions and displacements explained in the previous section, and the growing impetus of the mass mobilisations against the military régime, triggered a vast social and political realignment in Brazil between the mid-1980s and the early 1990s. This realignment, and the economic policy changes associated with it, was facilitated by two external developments. First, the contrast between Brazil's pitiful performance and the perceived success of such countries as Argentina, Mexico and South Korea convinced many Brazilian economists, and the country's economic and political élite,[7] that the so-called 'national project' centred on ISI was exhausted and could not be repaired. Second, the US and British governments, and the IMF and the World Bank, argued increasingly stridently that sustained growth was possible only under a neoliberal policy mix, including the retrenchment of the state, deregulation of product and factor markets, privatisation, fiscal balance, and trade and capital account liberalisation.

The combination of external and internal pressures gradually dissolved the resistance against the abandonment of ISI. During the 1980s and early 1990s, the élite gradually became convinced that the restoration of economic dynamism and the preservation of the existing patterns of social and economic exclusion demanded a *new* system of accumulation. This system, which I call 'new liberalism', includes four main features: neoliberal economic policies, the microeconomic integration of domestic capital into transnational circuits, a decisive role for finance in economic policy-making, and political democracy. This section argues that the prolonged stagnation of the Brazilian economy is due to the combination of the difficulties of ISI, identified in Section 1, with the shortcomings of new liberalism, explained below.

The shift towards new liberalism was validated indirectly by the closely fought presidential election of 1989, in which Fernando Collor de Mello narrowly defeated Lula's clearly left-wing platform (see Table 2). Collor would eventually be forced to resign because of his entanglement in an astonishing array of scandals involving drugs, sex and, especially public funds. The new liberal reforms sponsored by him proceeded slowly during the interim

---

[7] The élite includes the large and medium-sized capitalists, especially southeastern industrialists, exporters, large traders, financiers, media bosses, large landowners, local political chiefs, top civil servants, and their intellectual and political proxies. This concept transcends the (relatively less important) contrast between domestic and foreign capital, and between industrial and financial interests.

administration of his deputy, the erratic Itamar Franco. They would surge ahead only in 1994, after the presidential election of Fernando Henrique Cardoso. He originally was one of the gurus of the dependency school, and lately Franco's Minister of Finance.

Table 2: Brazilian presidential elections, number of votes and percentage of votes received, 1989–2002

Year	Winner (votes, %)	Runner-Up (votes, %)
1989 (1st round)	Fernando Collor (20.6m, 30.5%)	Lula (11.6m, 17.2%)
1989 (2nd round)	Fernando Collor (35.0m, 53.0%)	Lula (31.0m, 47.0%)
1994	Fernando Henrique Cardoso (34.4m, 54.3%)	Lula (17.1m, 27.0%)
1998	Fernando Henrique Cardoso (35.9m, 53.0%)	Lula (21.5m, 31.7%)
2002 (1st round)	Lula (39.4m, 46.4%)	José Serra (19.7m, 23.2%)
2002 (2nd round)	Lula (52.8m, 61.3%)	José Serra (33.4m, 38.7%)

The Brazilian experience shows that the new liberal reforms can be *sufficient* for short-term macroeconomic stability and growth, for two reasons. First, they are part of the conventional wisdom of our age, and are embedded in the belief systems of most institutions. Therefore, they are credible by definition. Second, if international liquidity is high and interest rates are low, as was the case in the early 1990s, trade and capital account liberalisation seem to abolish the balance of payments constraint. They can help to attract capital inflows sufficient to finance a large trade deficit, which allows consumption, investment and growth rates to increase rapidly, in a virtuous circle that may last several years.[8]

However, if the foreign capital flows decline substantially, as they did in the mid-1990s and, again, in mid-2000, less developed countries following neoliberal policies can find themselves in a highly vulnerable situation. The balance of payments constraint seems to reappear suddenly, either because of the scarcity of foreign exchange, or because higher international interest rates push up the domestic interest rates, squeezing the economy internally

[8] See Fine 2001, Fine and Stoneman 1996, Gore 2000 and Standing 2000.

and externally at the same time. Consequently, the domestic currency tends to behave erratically. This is an important part of the explanation of the currency crises in several middle-income countries during the 1990s, including Argentina, Mexico, Russia, South Korea, Turkey and, of course, Brazil.

The new liberal policy reforms were implemented gradually but increasingly systematically in Brazil since the late 1980s. The domestic financial system was reformed in 1988, international capital flows were liberalised between 1989 and 1992, and foreign trade was liberalised between 1990 and 1994. Finally, in 1994, Brazil concluded the renegotiation of its foreign debt along Brady lines, which would allow the Cardoso administration to unleash a fully neoliberal economic programme. This strategy was justified through the so-called 'imperatives of globalisation' and the urgent need to eliminate inflation, which had reached nearly 50 per cent per month. This was achieved in 1994. With the economy growing and inflation finally subdued, Lula's challenge against Fernando Henrique Cardoso was doomed. Lula pooled only 27.0 per cent of the vote in 1994, against Cardoso's 54.3 per cent.

The new liberal reforms helped to eliminate high inflation through the *real* stabilisation plan (named after the currency introduced in its wake), and they contributed to the growth spurt of 1993–5.[9] The *real* plan was not only a programme of disinflation and economic stabilisation. It also provided the perfect excuse for the systematic destruction of the remaining institutions of the previous system of accumulation. Trade, financial and capital account liberalisation, mass privatisations, state bank closures, changes in the labour laws, and dismantling the institutions that had provided industrial policy co-ordination in the previous decades, were invariably presented as being 'essential' for the struggle against inflation – while the opposition was absurdly accused of being 'for' hyperinflation.

In spite of these successes, the new liberal policy mix is severely limited. Six of its limitations, explained below, demonstrate that the transition to the new system of accumulation has not only failed to address the main short-comings of ISI but, also, that it has imposed new restrictions upon economic performance. This combination of problems has entrenched economic stagnation, and reduced the scope to accommodate social change without political upheaval. These restrictions will limit drastically Lula's ability to deliver growth with equity in the near future.

---

[9] For a detailed analysis, see Saad-Filho and Mollo 2002.

First, capital flows to developing countries are generally influenced more strongly by the circumstances in developed country financial markets than by recipient country policies.[10] Consequently, the liberalisation of the capital account of the balance of payments fails to eliminate the balance of payments constraint (in spite of the appearances, see above), and it tends to increase the economy's vulnerability to fluctuations in international liquidity and in the cost of finance. More precisely, under ISI, the balance of payments constraint appears through the absolute scarcity of foreign exchange, payment arrears and regular scrambles for last-minute loans. In contrast, under new liberalism, this constraint appears *either* through high domestic real interest rates (determined by the need to attract portfolio inflows sufficient to finance the balance of payments) *or* through exchange rate volatility (if the required inflows fail to materialise). Brazil has experienced both types of constraint. Real interest rates increased from 12 to 24 per cent per annum after the liberalisation of the capital account in 1992, and they remained at this level until the currency crisis of 1999. They subsequently declined to 7–10 per cent; however, exchange rate volatility has become a major source of disruption, showing that the balance of payments constraint continues to limit the performance of the Brazilian economy.

Second, financial and capital account liberalisation are destabilising because they necessarily raise the domestic interest rates and increase domestic financial fragility. For example, the accumulation of foreign and domestic liabilities, in the wake of the recession due to the Mexican collapse, led to a severe financial crisis in Brazil in 1995–7. This crisis was contained only through extensive central bank intervention, costing approximately US$25 billion, and it led to the further concentration and denationalisation of the financial system. However, these changes have not reduced the cost of loans or increased the availability of finance for domestic companies significantly – in other words, the policy reforms failed to resolve the financial constraints that crippled ISI.

Third, rapid foreign capital inflows tend to overvalue the exchange rate. The overvaluation increases the need for high domestic interest rates, partly in order to sterilise the capital inflows, and partly to finance the growing trade deficit. The Brazilian government condoned the sharp overvaluation of the *real* in 1994, and implemented policies that shifted the trade balance from

---

[10] See Calvo 1996 and Palma 1998.

a surplus of US$8 billion in the first three quarters of 1994, to a deficit of US$9 billion in the following three quarters. This was done deliberately, in order to stabilise the bulging international reserves without imposing restrictions on capital movements, and to keep inflation low through the pressure of foreign competition.

Fourth, high interest rates stimulated the accumulation of foreign debt and created scope for arbitrage through foreign borrowing for investment in government securities. In the second half of the 1990s, Brazil received foreign direct investment inflows of US$90 billion and portfolio inflows of US$60 billion, while the foreign debt doubled, to nearly US$250 billion.

Fifth, the *real* plan included a policy mix based on capital account liberalisation, sterilised intervention and exchange rate stability. However, these policies prevented the interest rate differential from narrowing, and stimulated short-term capital flows. Their impact upon the domestic public debt was explosive. In spite of substantial primary fiscal surpluses (see Table 1), and privatisations worth US$100 billion, the domestic public debt increased relentlessly, from less than 30 to nearly 60 per cent of GDP. In other words, the rapid growth of the domestic public debt (due to high domestic interest rates and the sterilisation of foreign capital inflows) has *caused* the fiscal crisis of the new liberal state. In the meantime, the tax system has become much stronger. However, tax evasion is still rampant among the 'entrepreneurial' classes, whose earnings are difficult to assess and easy to disguise. For these reasons, tax revenues remain insufficient to service the domestic debt and reverse the creeping process of social disintegration in the country.

Sixth, the introduction of a new mode of competition in the economy, based on the microeconomic integration of production and finance into transnational capital circuits, destroyed the institutions that delivered growth in the past, and that might have provided a platform for employment generation and the distribution of income and wealth in the future. It was expected, for example, that the integration between domestic and foreign firms would facilitate the transfer of savings and technology, increase competition and market access, assist macroeconomic stability, and lead to rapid productivity growth. This did happen, to a certain extent, but it was largely due to the introduction of new management and organisational techniques and specialisation in less complex products. They led to the hollowing out of important supply chains and the disarticulation of the industrial base, increased import dependence, and to a sharp reduction in the domestic content of the output. As a result, one million manufacturing jobs (one-third of the total) were lost, while output levels remained approximately constant.

The economic turbulence after the Mexican, Asian and Russian crises showed that the Brazilian economy was highly vulnerable to shifts in the provision of foreign finance. The sustained outflow of capital in the second half of 1998 was the immediate cause of the currency crisis of January 1999. This crisis devoured 40 per cent of the value of the *real* in seventeen days, and dashed the hopes of the recently re-elected President Cardoso.

The currency crisis showed the limits of new liberalism. In March, the government introduced a less dogmatic economic policy, based on lower interest rates, inflation targets, 'dirty' floating of the *real*, and fiscal surpluses. It was hoped that this would allow the restoration of the country's external competitiveness, inflation control, and limit the growth of the domestic public debt.

These policies were loudly praised by the Washington institutions and by most commentators until early 2002. However, their views were misguided.[11] The depressive impact of the currency crisis was relatively small in Brazil, when compared with other crisis-hit economies such as Mexico, South Korea and Russia for four reasons, none of which included policy choice or implementation.

First, the Brazilian economy is relatively large, and the influence of foreign trade, although increasingly important, remains limited. This reduces the contractionary impact of a given devaluation, in comparison with relatively smaller and more open economies. Second, the Brazilian economy remains relatively diversified and well integrated. This helps to preserve the level of activity, in spite of the depressive tendencies associated with new liberalism and the currency crisis. Third, although the crisis was highly costly to the government according to my estimations (its fiscal cost was 5.6 per cent of GDP), it brought substantial gains to the financial sector and, indirectly, to industrial capital involved in currency speculation. Fourth, in contrast with the debt crisis of 1982, the currency crisis did not reduce foreign capital flows to Brazil.

The interlude was brief. In the last two years, Brazil has been battered by the on-going global recession, and by the cumulative impact of its own internal and external vulnerabilities. Consequently, the *real* has been sliding downwards,

---

[11] See Saad-Filho and Morais 2002 – which was originally written in mid-2000.

losing nearly three-quarters of its value in four years (the *real* was close to parity with the US dollar in December 1998, stabilised around 1.4 after the crisis, declined to 1.8 during 2000, reached 2.5 in mid-2001, and accommodated around R$3.5 to the dollar one year later). In the meantime, inflation has raised its head again, creeping up from zero in 1998 to approximately ten per cent in late 2002.

The above two sections can be summarised briefly, as follows: the economic problems that Lula is going to face are very severe and, whatever he does, it is unlikely that the Brazilian economy can perform well in the near future.

3. The new administration

Lula's remarkable victory in both rounds of the Brazilian presidential elections of 2002 was the greatest political triumph of the Brazilian working class since the abolition of slavery, in 1888. This is also one of the most important achievements of the Left, anywhere in the world, in the last two decades, and it offers the most telling example of the bankruptcy of the 'Washington Consensus' and the shift of Latin American politics towards the Left.

This shift, and its timing, can be partly explained by the exhaustion of most neoliberal experiences undertaken in the last twenty-five years, and by the tensions created by the coexistence between political democracy and deep economic and social cleavages in the country. Left-wing views have an intuitive appeal in this context, especially in a relatively rich country such as Brazil, where the contrast between the existing wealth and productive potential and the misery of millions is both glaring and unjustifiable. Moreover, Latin America, and Brazil in particular, have been torn for decades between pro- and anti-US tendencies and, after the extremes of the 1990s, a more sceptical view of the US has emerged. Lula's victory is, therefore, part of the shift towards nationalism and the Left across the continent.

The Workers' Party (PT) is now the largest in Congress, even though it holds only twenty per cent of the seats. It will command a parliamentary majority, at least initially, through formal and informal alliances with smaller parties, groups and individual members of Congress. Unfortunately, these alliances will become increasingly expensive as the memory of Lula's triumph recedes, and horse-trading and pork-barrel politics return to the centre-stage, as they inevitably will, given the social divisions and the fragmentation of political representation in the country.

Obviously, Lula's victory is also the product of his personal history. For many years, Lula was despised and ridiculed by the middle classes (and even by many among the poor) because of his lack of formal education, ungrammatical Portuguese, rude manners and scraggly beard. Lula was born very poor in the Brazilian Northeast, from a large family that, later, migrated to prosperous São Paulo in search of work. He eventually became a lathe operator, and had a highly successful career as a trade-union leader. In the mid-1970s, Lula became the key figure in the left-wing 'new trade unionism' in Brazil. He achieved international prominence as the most important leader of the first large strikes held in Brazil since 1968. Although illegal, and the subject of heavy repression by the police and the army, the strikes of 1978–80 were overwhelmingly popular and largely successful.

For the first time in Brazil's history, a popular, incorruptible and seemingly uncompromising working-class leader had emerged, bypassing the established structures of power and patronage. Together with trade-union leaders, left intellectuals, political and community activists and Catholic organisations, Lula helped to launch a new political party, that challenged the established conventions. The Workers' Party and its leader were on the Left but were not the local representatives of a foreign Communist state. They confronted the state and its local minions more vigorously than other left organisations, but never considered the possibility of armed revolution. Finally, they distinguished themselves sharply from the liberal bourgeoisie, while the Communist parties dissolved themselves into united fronts with old-style populists, opportunists and thieves. The élite knew how to deal with the old Left, but it was unable to stem the growth of the Workers' Party.

The roots of the PT, and the memory of three failed bids to the presidency, played an important part in Lula's latest campaign. In 2002, Lula's campaign was planned in minute detail. His beard was impeccably trimmed, he wore the best Armani suits, he had far more cash than his opponents, and his TV advertisements were beautifully crafted. His discourse was studiously vague, and his programme was a collection of unobjectionable good intentions, not costed, and it included few tangible targets. Lula has offered the voters few unambiguous commitments or specific targets, and promised no significant social or welfare improvements. He gave his enemies no ammunition, and preserved the maximum freedom to do whatever he wishes after the election.

In his bid to clinch the election, Lula cajoled the PT into an alliance with several left-wing parties, as would be expected, but, surprisingly, also with the right-wing Liberal Party – to the disgust of the PT's Left. The PL has a colourful history. It has been, at various times, a stalwart of neoliberalism, the political arm of the evangelical church and, more recently, a reservoir for opportunist members of parliament who wish to be in government, but are unwilling or unable to join the PT. The PL is the home of José Alencar, a self-made man and leader of the nationalist wing of the manufacturing élite. Alencar was Lula's choice for the post of vice-president, and he helped to attract domestic productive capital (and large donors) to Lula's side. Lula's alliance with the Liberal Party also helped to neutralise the traditionally rabid opposition of the religious Right. The evangelical churches have been growing rapidly in Brazil, and their bishops never shy away from instructing the flock on how to vote. Their warm support in 2002 contrasts sharply with their previous description of Lula as the envoy of the devil – if not as Lucifer himself.

In order to disarm hard-core new liberals, Lula has promised to implement the recent Brazilian agreements with the IMF, including highly demanding fiscal targets, and to respect contracts and property rights. In other words, he will protect the interests of reactionary landowners, home-grown speculators and international financial institutions – precisely those who always hated and despised him, and did their best to destroy the Workers' Party in the past. Ominously, a string of infamous political leaders has rushed to Lula's support. Among them, former president (and currently Senator) José Sarney, disgraced by the nepotism and widespread corruption that infected his administration (1985–90), and the powerful *cacique* (traditional political leader) Antonio Carlos Magalhães, twice disgraced recently by fraud and corruption. Paradoxically, Brazilian new liberalism seems to be safer than ever in Lula's hands.

Is Lula the leader of the Brazilian working class, or a pawn of international capital? Can his administration deliver much-needed improvements in the distribution of income and wealth and social welfare, or will it strive to curb workers' demands in the name of stability, governance, globalisation and trickle-down? The answer depends on the political choices of Lula and the PT, and on objective constraints – especially the strength of the Brazilian economy and the correlation of forces underpinning the new administration (which is yet to be clearly determined).

Let us start from the economy. The balance of payments constraint and the fiscal crisis are the most urgent macroeconomic problems in Brazil. They cannot be addressed separately for two reasons. First, the openness of the capital account and the recent retraction of the international capital flows have made the interest rates required for balance of payments equilibrium much higher than those compatible with employment generation and servicing the domestic public debt. Second, the domestic financial system is, simultaneously, heavily indebted abroad and the main holder of the treasury bills. Stable and sustainable financial relations between the Brazilian state and the domestic financial system, and between the latter and the international financial system, are critical for growth.

Economic growth and political stability can be achieved in three different ways, and Lula and his party will be forced to choose one of the following strategies. First, they can emulate Tony Blair's New Labour, and stick to new liberalism while trying to manage the economy better than Cardoso's new liberals. Later, the efficiency gains can be used to improve the lot of the poor. However, this is problematic because the demands placed upon the Brazilian state are too great, the international environment is too hostile, and the resources available are too meagre to allow this strategy to succeed.

The second alternative is social democracy, in the post-war European sense. This would bring enormous gains to the Brazilian working class, and the Left should support it, while other options are explored. However, this government strategy is unlikely to succeed because financial, trade and capital account liberalisation and the fiscal crisis are incompatible with the Keynesian policies of employment generation and demand control at the core of traditional social democracy. Moreover, although the labour movement has been able to propel Lula from the shopfloor to the presidency, and achieve much in the other fronts of the class struggle, it is not (yet) strong, organised or unified enough to impose, through the state, a social-democratic pact including rising wages, income distribution, universal citizenship and state control of key economic sectors. In these circumstances, the first achievement of Brazilian social democracy would have to be the creation of its own preconditions. Although not impossible, this is certainly difficult in the current climate. Specifically, US political pressure and Brazilian economic vulnerability may not permit the development of a social-democratic alternative.

The third alternative is more radical. It would include an ambitious programme of financial and institutional reform in order to dismantle the new liberal consensus, expand economic democracy and restore economic dynamism *through* (and not merely 'with') redistribution. This programme would include targeted trade, capital and exchange rate controls, linked with aggressive import-substitution, export promotion and employment generation projects in key industrial areas. It would also include emergency initiatives to resolve urgent deficiencies in health, education, housing and energy provision, supplemented by large-scale land, urban and financial reforms. These policies would shift the economic incentives towards production rather than finance through a combination of rising wages and productivity, lower interest rates and cleverly designed tax policies, and they would generate foreign exchange through exports rather than fickle capital inflows.

However, this is very difficult to do, because it would require abandoning some of the key policy commitments of the current government, for example the fiscal surplus, the inflation targets and the liberalisation of trade and capital flows. This would raise objections from the IMF, the WTO and the US administration and, therefore, would generate severe balance of payments problems.

Moreover, Lula's political alliances do not permit an immediate attack on new liberalism, and there is no political will in the state apparatus to forge the coalitions required to support this policy shift. This is partly because this radical programme is hardly compatible with the *raison d'être* of the Brazilian state, and partly because of political inertia. Finally, although Lula was elected on a (largely implicit) platform of change, and his election brings the expectation of change, he has no *mandate* for radical change, and he is not committed to specific outcomes or even processes of change (as was shown above). In other words, although Lula has deplored some of the *consequences* of new liberalism, he has never identified this system of accumulation as a coherent obstacle to be confronted, and did not commit himself to rejecting any of its component parts.

Under these circumstances, it would be a terrible mistake for the Left to expect that the state will become the main vehicle of social change in Brazil, and its ally in the class struggle. Lula is not Allende, and Brazil 2002 is not Chile 1970. The Left must not either be co-opted or captured by the state, or become its hostage. Specifically, whereas support and participation are necessary, the key cadres and organisers of the social movements ought to remain outside of the government, and the left organisations must preserve their independence and negotiating capacity vis-à-vis the state. Radical political and economic changes, and the deconstruction of the power bloc that controls the Brazilian state, continue to depends primarily on the growth and strength of the Left, rather than the will of the President.

In spite of Lula's massive triumph, the historical importance of his election, and the unprecedented possibilities opened by it, the most important terrain of struggle for the Brazilian Left remains *outside* the state, or even *against* the state, as the case may be.

4. Conclusion

This article has shown that the Brazilian economy grew very little but changed substantially in the last two decades. The most important change, affecting both the economy and the society, was the shift from ISI to new liberalism. This shift was justified by the presumption that high interest rates and trade and capital account liberalisation would induce a substantial transfer of real and financial resources to Brazil, and guarantee high growth over long periods. However, new liberalism offers an inconsistent and socially undesirable development strategy. It has not addressed consistently the weaknesses of ISI; it relies on variables that Brazil influences only marginally, especially the volume and cost of the foreign capital flows; it has shifted the engine of growth towards an unreliable combination of externally financed consumption and investment in non-traded goods; it has deepened the country's external dependence, now at the microeconomic level, and it has destabilised the balance of payments and triggered fiscal, financial and currency crises. In sum, the poor performance of the Brazilian economy is due to internal and external causes but, increasingly, it is the outcome of the attempt to implement an accumulation strategy that can be stable only exceptionally.

Lula's electoral triumph is both the outcome of these developments, and a challenge to them. His victory could mean a lot for the internationalist Left: an inspiration, a viable example, and a strong base from which to build the movement against neoliberal globalism. However, in the domestic sphere Lula must tread carefully. The economic stagnation has become deeply entrenched, and there is little scope to accommodate social change without political upheaval. Difficult policy choices will have to be made, but none of them promises immediate relief, and there is little prospect of sustained economic growth or social change in the shortterm. Disappointment is likely, but important gains are possible. Whatever happens, Brazilian history has already been changed forever.

References

Baer, Werner 1995, *The Brazilian Economy: Growth and Development*, Fourth Edition, Westport: Lynne Rienner.

Branford, Sue and Bernardo Kucinski 2003, *Politics Transformed – Lula and the Workers' Party in Brazil*, London: Latin American Bureau.

Branford, Sue and Bernardo Kucinski 1995, *Brazil Carnival of the Oppressed – Lula and the Brazilian Workers' Party*, London: Latin America Bureau.

Calvo, Guillermo A. 1996, 'The Management of Capital Flows: Domestic Policy and International Cooperation', in *The International Monetary and Financial System*, edited by G.K. Helleiner, London: Macmillan.

Fine, Ben 2001, 'Neither the Washington nor the Post-Washington Consensus: An Introduction', in *Development Policy in the Twenty-First Century: Beyond the Post-Washington Consensus*, edited by B. Fine, C. Lapavitsas and J. Pincus, London: Routledge.

Fine, Ben and Colin Stoneman 1996, 'Introduction: State and Development', *Journal of Southern African Studies*, 22, 1: 5–26.

Furtado, Celso 1972, *Análise do 'Modelo' Brasileiro*, Rio de Janeiro: Civilização Brasileira.

Gore, Charles 2000, 'The Rise and Fall of the Washington Consensus as a Paradigm for Developing Countries', *World Development*, 28, 5: 789–804.

Hewitt, Tom 1992, 'Brazilian Industrialisation', in *Industrialisation and Development*, edited by T. Hewitt, H. Johnson and D. Wield, Oxford: Oxford University Press.

Palma, Gabriel 1998, 'Three and a Half Cycles of Mania, Panic and [Asymmetric] Crash: East Asia and Latin America Compared', *Cambridge Journal of Economics*, 22, 6: 789–808.

Saad-Filho, Alfredo 1998, 'Redefining the Role of the Bourgeoisie in Dependent Capitalist Development: Privatization and Liberalization in Brazil – A Critical Note', *Latin American Perspectives*, 98, 25, 1: 194–9.

Saad-Filho, Alfredo, Walter Coelho, and Lecio Morais 1999, 'Financial Liberalisation, Currency Instability and Crisis in Brazil: Another Plan Bites the Dust', *Capital & Class*, 68, Summer: 9–14.

Saad-Filho, Alfredo and Maria Mollo 2002, 'Inflation and Stabilization in Brazil: A Political Economy Analysis', *Review of Radical Political Economics*, 34, 2: 109–35.

Saad-Filho, Alfredo and Lecio Morais 2000, 'The Costs of Neomonetarism: The Brazilian Economy in the 1990s', *International Papers in Political Economy*, 7, 3: 1–39.

Saad-Filho, Alfredo and Lecio Morais 2002, 'Neomonetarist Dreams and Realities: A Review of the Brazilian Experience', in *A Post Keynesian Perspective on 21st Century Economic Problems*, edited by P. Davidson, Cheltenham: Edward Elgar.

Standing, Guy 2000, 'Brave New Words? A Critique of Stiglitz's World Bank Rethink', *Development and Change*, 31: 737–63.

Studart, Rogerio 1995, *Investment Finance in Economic Development*, London, Routledge.

Tavares, Maria da Conceicao 1975, *Da Substituição de Importações ao Capitalismo Financeiro*, Rio de Janeiro: Zahar.