At the intersection of law, economics, and the practices of states and development agencies, the field of law and development undergoes continuous realignment.\(^1\) As economic policies, legal theories, and institutional practices change, the salient issues in law and development change as well.\(^2\) The 21st century has ushered in a new era. Development theories are being challenged and new practices are emerging. Law and development scholars need to understand the new trends and explore their implications for legal studies and practice.

In the past couple of decades, development policy and practice have shifted in many regions, but nowhere more clearly than in Latin America. After a long period when neoliberal policies prevailed and the state’s role in the economy was curtailed, many countries in the region have begun to explore new forms of state activism. Brazil has been a leader in the formation of new development policies and in the creation of a new development discourse. Starting with the election of Lula da Silva in 2002 and gaining momentum during Lula’s second term in 2006, Brazil has instituted new forms of industrial and social policy, experienced a surge in growth, and seen a reduction in economic inequality.

This trend has led scholars to begin to talk about a “new developmentalism” and speculate about the emergence of a new kind of developmental state in which the government plays an active role in mobilizing resources, stimulating investment, and promoting innovation but does not command or

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1. This article draws on David M. Trubek, Diogo R. Coutinho, and Mario G. Schapiro, *New State Activism in Brazil and the Challenge for Law*, in *Law and the New Developmental State: The Brazilian Experience in Latin American Context* (David M. Trubek et al. ed., Cambridge U. Press, forthcoming) (hereinafter, Trubek et. al). An earlier version of the article was discussed at the 2012 IGLP Workshop at Harvard Law School and the Conference on Global Governance: Critical Legal Perspectives at the European University Institute (July, 2012). The authors are grateful to Peter Houtzager, Willy Forbath, Alvaro Santos, David Kennedy, Duncan Kennedy, Helena Alviar, Jeremy Perelman, Lucie White, Mushtaq Kahn, Shunko Rojas, and Yves Dezalay for comments and suggestions. The authors also received useful comments from Professor Wang Chenguang of the Tsinghua University School of Law.

control the economy. In this approach, the state employs an open-economy industrial policy to restructure production and increase international competitiveness while simultaneously using an active social policy to eliminate poverty, reduce inequality, and stimulate domestic demand. Unlike the old paradigm, in this new model, such a state seeks to benefit from participation in the global economy while avoiding the dangers of free trade fundamentalism, and it tries to stimulate, not replace, the private sector.³

This chapter explores shifts in government policy in Brazil since 2000, showing how these changes are influencing developments in the law. After a limited experience with neoliberalism, the country has embraced new forms of state engagement in the economy and social relations. Because these changes are recent and have not yet been fully consolidated, the resulting constellation can be viewed as new state activism (NSA),⁴ a term that suggests neither a return to the past nor a clearly consolidated alternative “model.” The chapter covers the emergence of NSA; identifies its salient features, noting how it differs from prior forms of state intervention; explores some of the forces that have shaped this new form of state action; and provides a preliminary assessment of the significance and challenge of these developments for the law.

Introduction: From the “Long 1990s” (1988-2004) to NSA

The evolution of NSA in Brazil was preceded by a series of policy changes that dismantled some of the institutions of the old developmental state and embraced some aspects of the Washington Consensus. Like several other developing Latin American countries, Brazil had a classic developmentalist phase in the twentieth century: from 1930 until the end of the 1980s, economic policies consisted of state-led initiatives to promote import substitution industrialization, and growth through state-owned enterprises, economic planning, price control, regulatory and administrative authorities in key sectors, and the use of tax and financial incentives.


Between 1988 and 2004, known as the “long 1990s,” Brazil partially dismantled these structures and policies and shifted to more market-oriented approaches. In 1988, after 24 years of military dictatorship and in a context of a threat of hyperinflation, Brazil passed a new constitution that has influenced and shaped policy ever since. The 1988 constitution is a social democratic document that created a vibrant democratic polity and includes civil, political, and social rights and a number of policy goals such as building a free, just, and socially integrated society; fostering national development; acquiring technological autonomy; eradicating poverty and marginalization; and reducing economic and social inequalities. Many of the constitution’s provisions have had a direct effect on government policy and budgetary allocations.

President Collor de Mello was elected in 1989, immediately after the new constitution came into force. Stressing the need for “modernization,” Collor de Mello rapidly liberalized the economy using drastic tariff reductions, privatization, and flawed attempts to control inflation. Under Itamar Franco, who replaced Collor de Mello after he was impeached, a stabilization plan (the Plano Real) was successfully adopted and inflation was controlled. New legislation on social assistance and welfare for the poor was also passed.

Franco’s minister of finance, Fernando Henrique Cardoso (known as FHC), became the next president in 1994. During Cardoso’s eight years in office, Brazil continued to move away from the dirigiste policies of the developmentalist period, embracing many of the neoliberal prescriptions favored by the Washington Consensus. In the Cardoso period, state owned-enterprises were privatized, direct subsidies for certain industries were scaled back, areas of the economy were deregulated, import barriers were reduced, competition was fostered and enforced, intellectual property rights were tightened, bilateral investment treaties protecting foreign investors were signed, and fiscal responsibility was enhanced. Also, the currency (the real) was constantly kept overvalued as monetary stability was pursued and attained.

Under Cardoso, the bureaucracy was partially modernized, regulatory agencies were created, public-private partnerships were designed, and new...

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5 In January 1990, inflation in Brazil reached 56 percent per month, raising to 73 percent in February and peaking at 84 percent in March; see Luiz Carlos Bresser-Pereira and Yoshiaki Nakano, *Hiperinflação e estabilização no Brasil: O Primeiro Plano Collor*, Revista de Economia Política 4 (1991). During the same period, economic inequality reached its worse level since it had been measured (the Gini coefficient peaked at 0.647, according to the Brazilian Office of Statistics).


7 Cardoso has always rejected the neoliberal label and claimed that his goal simply was to modernize the economy.

8 “[T]he goal of price stability has remained sacrosanct and the instruments for achieving this goal have been in line with the latest international fashions: central bank independence and inflation targeting.” Cornel Ban, *Brazil’s Liberal Neo-Developmentalism: New Paradigm or Edited Orthodoxy?* Rev. Intl. of Pol. Eco. (forthcoming).
social policies were adopted. To carry out privatization and encourage foreign investment, Congress made several changes in the constitution. But although the country adopted some ideas from the Washington Consensus, it did not wholeheartedly embrace neoliberalism. Privatizations were limited; Banco do Brasil, BNDES (the Brazilian Development Bank), and Petrobrás, three major state-owned enterprises, remained under government control. None of the bilateral investment treaties signed in the 1990s was ratified.

Institutional and Political Background: The New Democratic Constitution of 1988 and the Cardoso Administration

Political parties and social movements had been repressed during military rule (1964–85). When the constitution-making process started in the late 1980s, an eruption of social-political demands had to be accommodated. Not surprisingly, the resulting constitution was nicknamed “the citizen’s constitution.” Not only did it create democratic institutions, it also included an extensive charter of civil-political and social rights and reframed public-private relationships. The constitution incorporates provisions guaranteeing the rule of law, protecting individual rights, and guarding against arbitrary state action. It also created positive—and justiciable—rights that could impose policy obligations. The 1988 constitution includes rights to health, education, housing, social protection, and pensions. These guarantees have shaped a new and complex welfare system, including a massive universal public health system and a system of universal pensions. The new system in turn has had a major impact on the role of the state and on patterns of government spending.9 Instead of cutting back on social spending as many countries did during the 1990s, Brazil increased the percentage of GDP devoted to social protection during that period.10

Besides facilitating political mobilization and participation, instituting social rights and shaping social policies, the new constitution facilitated modernization of the state apparatus and reframed public-private relationships with consequences for the business environment. The 1988 constitution initiated a slow process of professionalizing state administration. Until the 1930s, public employees were hired through the “spoils system” of political appointments. A partial reform under Getulio Vargas had instituted meritocratic selection for some key agencies such as BNDES and the Foreign Ministry, but left most government jobs subject to political appointment.11 The 1988 constitution carried

11 The first initiative to reform the public sector to create a more professional public staff was undertaken by President Getulio Vargas (1930–45), whose government created the Department
the reform further, requiring that all public employees be selected through meritocratic processes and capping state salaries.

The constitution significantly affected relations between the state and business. It required competitive bidding for all state purchases and made the process more transparent. The special federal prosecutors (Ministério Público) were authorized to combat corruption and enforce laws protecting consumers and the environment. The constitution also protected individuals and businesses against regulatory takings and expropriation without compensation.

Although the new constitution embraced social-democratic values and norms and some developmentalist ideas, during the 1990s, Brazil flirted with neoliberal policies. In 1994, President Itamar Franco and Minister of Finance Fernando Henrique Cardoso launched the Plano Real, a macroeconomic stabilization effort that eventually managed to control inflation in Brazil. One of Cardoso’s first acts as president was to get Congress to remove some provisions in the 1988 constitution that enshrined “old developmentalist” policies such as state monopolies and restrictions on foreign investment.

Under Cardoso, Brazil experienced a strong devaluation of the real as a result of a harsh international crisis (particularly in Mexico, Russia, and Asia). The government raised the interest rate to a very high level, which severely hindered growth. At the same time, the Cardoso government managed to embed Brazil in the world economy through trade liberalization. In 2000, it ensured fiscal austerity by passing a fiscal responsibility act, and it sought to modernize public administration by adopting tenets of a “new public administration” that allowed outsourcing of certain functions to the private sector.

Under Cardoso, Brazil accelerated privatizations initiated by Collor and Itamar Franco: in 1997, Vale do Rio Doce, a major state-owned mining and steelmaking company, and Sistema Telebrás, the public-owned telecommunication conglomerate, were sold. In the same year, several electricity and gas distribution companies, as well as some state-level banks, were transferred to private owners. During his eight years as president, Cardoso raised

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12 In 1999, Brazil officially adopted an inflation target system (the target in 2012 is 4.5 percent per year).
14 The strategy segregated core activities that should be performed by politicians and senior officials, including conducting support activities that may be outsourced, separating policy formulation from policy execution, and granting more autonomy and accountability to services performed by the state, which would take the form of either “executive agencies” or of “social organizations” that are a special type of nonprofit. See Luiz Carlos Bresser-Pereira, The 1995 Public Management Reform in Brazil: Reflections of a Reformer, in Reinventing Leviathan: The Politics of Administrative Reform in Developing Countries (Ben Ross Schneider & Blanca Heredia, ed., North-South Center Press, 2003).
15 Franco privatized CNS, an important steel company, in 1995.
approximately US$79 billion through privatization. However, like Petrobrás, the Brazilian state oil and gas company, the three large federal banks—Banco do Brasil, Caixa Econômica Federal, and BNDES—were not privatized. Indeed, BNDES played an important role in facilitating privatization by offering credit to both domestic and international buyers. Table 1 lists the state-owned enterprises that were privatized in the 1990s.

Table 1. State-Owned Enterprises Privatized

<table>
<thead>
<tr>
<th>Enterprise</th>
<th>Date</th>
<th>Enterprise</th>
<th>Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>USIMINAS</td>
<td>24.10.1991</td>
<td>CSN</td>
<td>02.04.1993</td>
</tr>
<tr>
<td>USIMEC</td>
<td>24.10.1991</td>
<td>FEM</td>
<td>02.04.1993</td>
</tr>
<tr>
<td>CELMA</td>
<td>01.11.1991</td>
<td>ULTRAFÉRTIL</td>
<td>24.06.1993</td>
</tr>
<tr>
<td>MAFERSA</td>
<td>11.11.1991</td>
<td>COSIPA</td>
<td>20.08.1993</td>
</tr>
<tr>
<td>AFP</td>
<td>14.02.1992</td>
<td>PQU</td>
<td>25.01.1994</td>
</tr>
<tr>
<td>COPESUL</td>
<td>15.05.1992</td>
<td>EMBRAER</td>
<td>07.12.1994</td>
</tr>
<tr>
<td>CST</td>
<td>23.07.1992</td>
<td>LIGHT</td>
<td>21.05.1996</td>
</tr>
<tr>
<td>FOSFÉRTIL</td>
<td>12.08.1992</td>
<td>VALE</td>
<td>06.05.1997</td>
</tr>
<tr>
<td>ACESITA</td>
<td>23.10.1992</td>
<td>TELEBRÁS</td>
<td>29.07.1998</td>
</tr>
<tr>
<td>ENERGÉTICA</td>
<td>23.10.1992</td>
<td>GERASUL</td>
<td>15.09.1998</td>
</tr>
<tr>
<td>FASA</td>
<td>23.10.1992</td>
<td>DATAMEC</td>
<td>23.06.1999</td>
</tr>
</tbody>
</table>

Source: Ministério do Planejamento, Orçamento e Gestão (Brazil)

Brazil adapted the US model of regulatory agencies to supervise and enforce post-privatization rules and to introduce competition in natural monopolies. As a result, electrical distribution, fixed telecommunication networks, and transportation (railways, highways, waterways) were subject to a new legal and institutional framework that substantively changed the patterns of administrative law. New licensing and concession agreements were signed. For a list of areas subjected to regulation see table 2.
Table 2. Activity Regulated

<table>
<thead>
<tr>
<th>Activity Regulated</th>
<th>Commission</th>
<th>Foundation</th>
<th>Law</th>
</tr>
</thead>
<tbody>
<tr>
<td>Competition</td>
<td>CADE</td>
<td>1994</td>
<td>8.884/94</td>
</tr>
<tr>
<td>Electric power</td>
<td>ANEEL</td>
<td>1996</td>
<td>9.427/96</td>
</tr>
<tr>
<td>Oil &amp; Gas</td>
<td>ANP</td>
<td>1997</td>
<td>9.478/97</td>
</tr>
<tr>
<td>Telecommunication</td>
<td>ANATEL</td>
<td>1997</td>
<td>9.472/97</td>
</tr>
<tr>
<td>Health Surveillance</td>
<td>ANVISA</td>
<td>1999</td>
<td>9.782/99</td>
</tr>
<tr>
<td>Health Insurance</td>
<td>ANS</td>
<td>2000</td>
<td>9.961/00</td>
</tr>
<tr>
<td>Water</td>
<td>ANA</td>
<td>2000</td>
<td>9.984/00</td>
</tr>
<tr>
<td>Water Transport</td>
<td>ANTAQ</td>
<td>2001</td>
<td>10.233/01</td>
</tr>
<tr>
<td>Land Transport</td>
<td>ANTT</td>
<td>2001</td>
<td>10.233/01</td>
</tr>
<tr>
<td>Aviation</td>
<td>ANAC</td>
<td>2005</td>
<td>11.182/05</td>
</tr>
</tbody>
</table>

The Cardoso administration rejected the idea of industrial policy, long a mainstay of Brazil’s developmental state. Finance Minister Pedro Malan said that “the best industrial policy you can have is not to have one.” BNDES, which for decades had provided financing to targeted sectors and supported many state-owned enterprises, shifted to support of privatization. Rather than trying to support priority sectors, the government focused on increasing the efficiency of government services and reforming credit markets. For example, starting with Cardoso and continuing into Lula’s first term, the Central Bank sought to reduce the cost of credit. Among the microeconomic measures undertaken were improvements in bankruptcy procedures and debt collection.16

The Cardoso administration’s opposition to industrial policy did not deter it from stimulating selected sectors in order to promote competitiveness and innovation. Thus, in 1999, 16 new sectorial funds were charged with fostering innovation in strategic areas such as oil and gas, telecommunications, biotechnology, and agribusiness. The Cardoso period also saw important changes in social policy. Traditionally, the Brazilian welfare state has been regressive, clientelistic, and opaque. Between 1994 and 2002, the federal government took a number of measures aimed at transforming this system, including adding poverty-alleviation programs aimed at specific populations; introducing noncontributory social protection programs; decentralizing social policy implementation; and tackling some of the regressive features of the pension

16 According to Fabiani, during the 1999–2006 period, the law behind the government’s microeconomic agenda was seen as an instrument to protect creditors and ultimately to promote economic efficiency. See Emerson Ribeiro Fabiani, Direito e Crédito Bancário no Brasil (Saraiva, FGV, 2011).
scheme.\textsuperscript{17} The Cardoso government initiated the use of conditional cash transfers; for example, the Bolsa Escola program, implemented 2001, aimed to increase access to education, reduce poverty in the short term by transferring cash to impoverished households, reduce child labor, and serve as a social protection network.\textsuperscript{18}

Another important development in this period was LOAS (the Social Assistance Act). Enacted under Itamar Franco and implemented by Cardoso, LOAS seeks to guarantee “minimum social standards.” The noncontributory multilevel federal, state, and local program is designed to protect households, mothers, children, adolescents, and the elderly; to assist underprivileged children and adolescents; to promote labor market integration; and to train and rehabilitate persons with disabilities and promote their integration into community life.\textsuperscript{19}

\textbf{NSA Emerges}

Luiz Inácio Lula da Silva was elected president in 2002. For two four-year terms, his government preserved some Cardoso policies such as inflation control and openness to foreign investment while changing others by adopting state-activist initiatives, including an active industrial policy and a massive poverty-fighting program. Dilma Roussef, elected president in 2010, has maintained Lula’s priorities but expanded state activism in key areas.\textsuperscript{20}

Lula’s inauguration instigated a decade of experimentation. Developmentalist institutions have been reinvented, neoliberal policies were modified, new institutions were created, and a new form of state activism is emerging. Changes have occurred gradually.\textsuperscript{21} Some of Cardoso’s policies, such as

\begin{enumerate}
\item Almeida explains that during Cardoso’s first term, some changes in universal social polices confronted the regressive feature of the Brazilian pension system (a constitutional amendment changed the minimum age and the period of contribution for retirement), although the problematic topic of public servants’ pensions—a major source of inequality in the country—remained untouched. See Maria Hermínia Tavares de Almeida, \textit{A Política Social no Governo Lula}, 70 Novos Estudos - CEBRAP 70 7–17 (2004).
\item Inspired by successful experiences at the local level, the federal Bolsa Escola program reached more than 5 million families. Other conditional cash transfer programs widened the scope of protection and helped build a multilevel public-private network of providers.
\item The federal government is assigned the task of coordinating and promoting LOAS and providing technical advice and financial incentives to states, cities, and welfare entities and organizations. States must transfer certain funds to municipalities, provide them with technical support, and stimulate the collective rendering of social services. Municipalities must, among other things, execute social assistance and poverty-fighting policies, which includes the possibility of establishing partnerships with civil society organizations.
\item To win the election, Lula stated that debt agreements would be honored. Talking about the gradual manner through which changes would take place, Lula said in his “Letter to Brazilians” in 2002: “the premise of this transition will naturally be the respect to contracts
\end{enumerate}
macroeconomic stabilization, have been preserved, and some of his social policy innovations have been improved and substantially expanded. Institutions like BNDES that survived from the period of state developmentalism have been reinvigorated and redirected. Other developmentalist institutions, such as industrial policy, that were rejected during the neoliberal period have been revived, albeit in different form. Finally, new institutions have been added to increase coordination between the public and private sectors.22

**Macroeconomic Continuity**

Scarred by decades of high and damaging inflation, Brazil adopted policies in the 1990s to preserve monetary stability. The Plano Real used various measures to control public spending and regulate the money supply. This has kept the inflation rate low (by Brazilian standards) for more than 15 years and enshrined monetary stability as a cornerstone of economic policy. During the first Lula administration, emphasis was placed on instituting, developing, and strengthening political and economic credibility using fiscally responsible macroeconomic policy, a floating exchange rate, and inflation targeting. In general terms, the Dilma administration has continued these policies. However, this emphasis has come at a price: the main tools of macroeconomic policy are restrictions on government spending and a relatively high interest rate, putting a brake on public investment and increasing the cost of credit, thus possibly hampering growth. To offset these effects, Lula introduced several growth-inducing microeconomic policies, including a new form of industrial policy and social policies that helped spur domestic growth while relieving poverty and reducing economic inequality.

**Industrial Policy**

In 2004, after a decade in which Brazil had explicitly rejected industrial policy,23 the government introduced measures designed to foster selected industries. Lula’s first try at industrial policy was limited and focused primarily on innovation. At the time, there was strong opposition to industrial policy in policy making circles and academic opinion. It was thought that governments were not able to strategically identify targets and that trying to do so would divert resources from horizontal structural measures such as tax reform and infrastructure investment that would benefit the entire economy.

However, some people were prepared to accept a limited role for government in overcoming market failures and reducing the coordination and systemic problems that hampered innovation; the Cardoso administration had taken modest steps in this direction. Lula’s first foray into industrial policy

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22 A notable example is the Public-Private Partnership Federal Act of 2004.

—called PITCE—stressed a combination of general measures to improve the business environment and financial support in four sectors in which one could argue innovation was essential: semiconductors, software, capital goods, and medicines.

PITCE included substantial legislative activity, including the Innovation Law (designed to facilitate partnerships and synergy among universities, companies, and research institutes) and the Foundation Law (which facilitated government support for university research). At the same time, the government started building institutions designed to improve coordination within government and between government and the private sector. These included the Council of Economic and Social Development (CDES), designed to help foster inclusive growth; the National Council of Industrial Development (CNDI), a public-private body charged with defining directives for industrial development; and the Brazilian Agency for Industrial Development (ABDI), which coordinates implementation of industrial policy by bringing together government, industry, labor, and universities. Arbix and Martin describe ABDI as a “networked institution, formally under the Ministry of Development, Industry, and Trade. ABDI has played an important role in seeking to develop an industrial policy and helps identify and guides investment decisions in technological research, innovation and industrial development.”

In 2008, during Lula’s second term, the government launched the Program for Productive Development (PDP). PDP replaced PITCE and was much more ambitious and complex. It included both horizontal measures designed to increase the overall efficiency of the economy and vertical programs for targeted sectors. Reflecting the scope and complexity of the Brazilian economy, PDP covered a wide range of industries. The program set goals, established a complex governance regime, and placed special emphasis on collaboration between the public and the private sectors. It called for industry-specific competitiveness councils instituted by Cardoso and expanded under Lula. PDP relied on policy instruments such as financing, tax, public procurement, public-private alliances, coordination and consultation, and regulation.

Horizontal measures in PDP included improvements in infrastructure and education, increased investments in science, reductions in interest rates for investment, tax relief, and improvements in the legal environment, including

24 These include legal measures to improve incentives for innovation and to facilitate better relations between universities and business, as well as tax relief.

25 The Innovation Law allowed the government to invest directly in private companies as a minority shareholder in order to create new products and processes, and provides for sharing of any resulting intellectual property. The Foundation Law facilitated support from FINEP and the National Fund for Scientific and Technological Development for university-based research-support foundations.

26 Arbix & Martin, supra note 4.

modemizing the rules governing foreign trade. Vertical measures, which dealt with specific industries, were designed to meet three basic challenges. For each, there were different governance mechanisms and a different mix of policies and measures. Measures that might be employed included subsidized credit from BNDES and other public financial sources, tax incentives, technical assistance, advantages in public procurement rules, favorable trade policy, and supportive regulation.

The first challenge identified by PDP was to consolidate and expand leadership in sectors in which Brazil was deemed to have a competitive edge. The goal was to support Brazilian firms that could be world leaders or heavyweights in their industry. Sectors included aviation, mining, steel, cellulose, oil and gas/petrochemical, bioethanol, and meat. The second challenge was to foster and occasionally induce mergers and alliances (sometimes with BNDES holding a minority stake) to build up industries that had competitive potential but were not yet at the global frontier. These included capital goods, the automotive complex, wood and furniture, pharmaceutical, meatpacking, personal hygiene, perfumery and cosmetics, construction, various service industries, coastal and marine industry, leather, footwear and artifacts, the agro-industrial system, and plastics. The third challenge was to strengthen high-tech “vanguard” sectors that had both growth potential and whose growth could improve the technological capacity of the entire economy. These strategic areas included health, biotechnology, defense, nuclear energy, nanotechnology, and information and communication technology.

The governance of PDP was complex. A system of public management brings representatives of appropriate ministries and agencies together for each of the major tasks and links them to the private sector through a variety of coordination devices. Observers of PDP point to the importance of public-private coordination at every level, from setting overall priorities to working out packages of effective measures for each sector.

PDP was overtaken by the global financial crisis before it got off the ground. But even if there had been no recession, a program like this, which envisions major structural changes, must be considered in a long-term context. Although the government can point to some real achievements, critics have questioned whether the plan truly shifted resources from traditional sectors to high-tech industries or if did enough for small and medium industry, which often is a major source of innovation.28

In 2011, the new administration, led by Dilma Rousseff, introduced an updated version of PDP called Brasil Maior (Greater Brazil) with the motto

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28 According to information available from the BNDES, in 2008, out of the 179 beneficiary companies, 12 were listed in Bovespa (a Brazilian stock exchange). In 2009, out of the 156 beneficiary companies, 25 were listed in Bovespa. Available at http://www.bndes.gov.br/SiteBNDES/bndes/bndes_pt/Institucional/BNDES_Transparente/Consulta_as_operacoes_do_Bandes (accessed May 1, 2010).
“innovate to compete; compete to grow.” This plan continued many of the same objectives and policies of PDP. But reflecting rising concerns about “deindustrialization,” the plan emphasizes efforts to protect domestic industries hit hard by global competition, an overvalued currency, and low-cost imports. Taxes on manufacturing have been reduced, attention is paid to antidumping measures, and substantial preferences for local producers in government procurement have been introduced. At the same time, funding from BNDES and FINEP, the Financiadora de Estudos e Projetos, were increased and efforts were made to channel more funding to innovative firms and sectors.

ABDI identifies three major strategic areas for development and explains how Brasil Maior addresses each area. To increase investment and spur innovation, Brasil Maior offers tax relief, increased financing for investment and innovation, and further improvements in the legal framework. To promote exports and protect domestic industry from unfair trade, the plan offers tax relief, export financing and guarantees, trade promotion, and enhanced defense thorough antidumping and other trade remedies. To protect hard-hit domestic firms, the plan includes exemptions from payroll tax for selected industries and a 25 percent margin of preference for local firms in government procurement.

An important part of the Brasil Maior plan is the system of public-private coordination that builds on structures created for PDP: the National Industrial Development Council (CNDI), sectorial executive committees, and sectorial competitiveness councils. CNDI is a peak institution that includes ministers, the president of BNDES, and 18 representatives of industry, labor, and the public. Its role is to set strategic guidelines. The Brasil Maior plan identifies 20 priority sectors: petroleum, gas and marine construction, chemicals, health, renewable energy, furniture, automotive, mining, civil construction, defense, aviation and aerospace, agro-industry, capital goods, metallurgy, logistics services, electronics, personal hygiene, fragrances and cosmetics (HPPC), services, retail, shoes, textiles, candy and jewelry, cellulose and paper. There is an executive committee and a competitiveness council for each sector. The executive committee consists of government officials charged with developing an action plan for the sector. These representatives meet with the sectorial competitiveness councils to refine the action plans and explore implementation issues.

Social Policy

In addition to reviving industrial policy, the governments of Lula and Dilma have expanded Brazil’s social protection system and antipoverty programs. The result is a significant decline in the poverty rate, a reduction in inequality, substantial growth of the middle class, and stimulus for the domestic market. Between 2001 and 2008, incomes of the wealthy grew at a moderate pace, while the income of the poor increased substantively. Approximately 28 million people moved out of poverty and a “new” middle class has emerged—between 2003 and 2011 approximately 10.5 million Brazilians became part of

Available at http://www.brasilmaior.mdic.gov.br/.

29
the middle class, which now includes 55 percent of the population. The Brazilian social pyramid is now diamond shaped, with more citizens classified as middle class than as poor.

The distributive gains achieved in Brazil during the past decade are the result of a combination of economic and institutional reforms. These reforms include the reintroduction of previous efforts such as inflation control and changes in labor markets that include unemployment reduction and increases in the minimum wage, pensions, and social security improvements, as well as a new generation of social assistance policies, especially the Bolsa Família program (BFP), created in 2003 as a result of a consolidation of previously existing initiatives. Health and education spending as a share of GDP has grown considerably in recent years, magnifying the impacts of institutional reforms instituted in the late 1990s. In another recent development, in 2011, the Brazilian Unified Social Assistance System (SUAS) was institutionalized and formalized by a federal statute.

In June 2011, President Dilma Rousseff launched the Brasil Sem Miséria program, designed to rescue 16.2 million people from extreme poverty, 59 percent of whom live in the northeast region. Brasil Sem Miséria has been presented as a combination of complementary rural and urban sectorial actions—in the areas of income transfer, labor market integration, access to public services, education, health, social assistance, water, and sewage—and involves the creation of new initiatives and the reconceptualization of existing ones. This program aims to find and register extremely poor families and integrate them into different programs. Brasil Sem Miséria is also supposed to help those who graduate from BFP enter the labor market.

The changes in social policy seem to be working: poverty has been cut drastically and income inequality has been reduced. Although Brazil still is one of the most economically unequal countries in the world, the decline in poverty and the reduction of inequality in Brazil in recent years have been remarkable. Thanks to a wide range of policies—including universal, targeted, and decentralized programs—the Brazilian welfare state is becoming stronger.

31 Since its inception, BFP has reached more than 12 million families as beneficiaries. If one assumes that each family has four people on average, the total figure for individuals who have benefited from BFP reaches 48 million people, or approximately 25 percent of the Brazilian population. Half of its budget has been spent in the northeast part of Brazil, where millions of very poor families live. Considering its gigantic scale, the targeting of BFP (defined as the share of total benefits received by specific groups of the population) has been considered exemplary, outperforming other social assistance programs in both Brazil and internationally.
32 Translation: “Brazil without Indigence.”
33 Brasil Sem Miséria also changed the number of children and adolescents who can obtain the BFP benefit—as of 2012, up to five (it used to be three).
34 The Brazilian Gini coefficient in 1960 was 0.5367; it was 0.6091 in 1990; and in 2010, it was still very high (0.5304). See Nery, supra note 30 at 27.
35 As put by Arbix & Martin, supra note 4: “while Brazil’s ‘welfare state’ still has segmented
Brazil’s NSA: Something New under the Sun?

The emerging profile of state activism differs from state action in both the developmentalist period and the neoliberal phase of the 1990s. In the developmentalist period, from the 1930s to the 1980s, the Brazilian government not only set priorities for industrialization in a top-down fashion, it also was a primary actor in industry. The state bureaucracy set goals; state-owned enterprises played a central role in many sectors, including steel, mining, aircraft, automobiles, and banking; and the state development bank provided funding for areas deemed priority by government planners. Emphasis was on “catching up” by building domestic industries. The new industries used imported technology and paid little or no attention to innovation.\(^{36}\) The state created tariffs and multiple exchange rates to control imports. Social policy was not focused on redistribution or poverty reduction; social protection programs were elitist, designed to keep the industrial working class and the small middle class happy and managed in a clientelistic fashion.\(^{37}\)

The 1990s saw a partial reversal of the developmentalist model with privatization, liberalization, dismantling of the instruments of industrial policy, and tentative steps toward poverty alleviation. But when it took office, the Lula government decided the state needed to resume a more active role in industrial development and to take more aggressive steps to relieve poverty and reduce inequality.

The Lula administration recognized that markets were necessary but not sufficient for inclusive growth. The state could do more to promote growth with equity, and it started to act more selectively and aggressively in the economy. This shift away from neoliberalism was as notable for what it did not do as for what it did. When Brazil began to develop new forms of state activism, it did not renationalize former state-owned enterprises, impose price controls, create a top-down development plan, discourage foreign investment, default on international obligations, engage in deficit spending, or close its markets to foreign goods. Rather, it sought to maintain and benefit from openness by ensuring the competitiveness of the domestic industry. Efforts focused on qualities, benefiting the better organized and remunerated in the formal and public sectors disproportionately, this segmentation is now much less acute than it has been for decades, and perhaps since the creation of the country’s first social benefits many decades ago. In 2010 inequality in Brazil reached its lowest level since measurement started in 1960.”

During the import substitution period, Brazil copied technology from developed countries. This was often manifested in the form of factories owned by foreign companies that located R&D and innovation outside Brazil with no obligations to transfer technology. That meant that Brazilian industry had a very low level of capacity for innovation. See Ignácio José Godinho Delgado, “Desenvolvimento, empresariado e política industrial no Brasil,” in Estado, Empresariado e Desenvolvimento no Brasil: Novas Teorias, Novas Trajetórias, 115–141 (M. A. Leopoldi, W. P. Mancuso, & W. Iglesias ed., Editora de Cultura, 2010).

Arbix & Martin, supra note 4 observe that “over the course of several decades, the statist model shifted resources from consumption to investment, limiting real wages and social spending and directing social spending in clientelistic fashion toward more organized segments of society with an eye toward political stability and control.”
constructing new forms of industrial policy that emphasized innovation and partnership with industry. At the same time, an emphasis was placed on social policy and redistribution and the combination of social policy with industrial growth strategies.

**The Rise and Shape of NSA**

What explains NSA and why did it take the shape that it did in Brazil? What impelled the Lula government to reintroduce industrial policy? Why did it choose to emphasize innovation, engage with the private sector, and structure the program in a more bottom-up fashion? Why did NSA link industrial and social policy and refocus social policy toward poverty alleviation and reduction of inequality?

No one would claim that Brazil’s new form of state activism was planned from the start or that a clear or completely stable model has emerged. No master plan ever emanated from a government think tank or planning ministry. These policies evolved in a piecemeal fashion and are still changing. The Brazilian government has been feeling the stones as it crosses the river—recalling Deng Xiaoping’s phrase—not following an existing blueprint. However, looking back over a decade of experimentation and policy evolution, one can see several factors that explain the decision to resume an active role for the state as well as the forces that affected the form this role would take. This section considers three of these factors: political opportunity, structural impediments to growth, and international and domestic constraints. Taken together, they exemplify the profile of what Arbix and Martin call “new state activism without dominance.”

**A Political Moment**

When Lula was elected in 2002, growth had slowed and unemployment was very high. The effects of globalization and liberalization were being felt, and Brazilian companies were losing ground. It is not hard to understand why a government led by the Brazilian Workers Party (PT), predisposed to state activism, would want to increase the role of the state in the economy. But the PT was not alone—this view was shared by at least part of the wider business community. Business in general and many industrialists in particular wanted a more activist state and more voice in government policy.38

Although the PT was ideologically committed to state activism, the business community looked to the state as a force that could reignite growth. Dissatisfied by the effects of liberalization in the 1990s, powerful industrial groups (including the Federation of Industries of São Paulo, or FIESP) involved themselves in the electoral process in 2002 with the objective of “opening space for

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38 Shunko Rojas suggests that changes in the leadership of the Federation of Industries in São Paulo led to FIESP support for an expanded state role well before the 2002 election. Private communication with the authors, Aug., 2012.
developmentalist ideas.” Industry had played an important role in the old development state, so at least some industrialists were comfortable with an increased role for the state as long as they had a voice in state policy.

Although Lula’s first administration took cautious steps toward state activism, interest in a stronger role for the state grew during Lula’s second term (2006–10). In this period, NSA gained appeal, importance, and political support from industrialists, unions, intellectuals, and academics. Brazilian economist Antonio Barros de Castro suggests that the Brazilian elite realized that it needed to “deal with China.” He notes that trade liberalization and the rise of China led much of Latin America to abandon industry and refocus on natural resources. Due to the large size and central importance of its industrial sector, Brazil could not and did not want to take this route. Despite the modernization of Brazil’s industry that had made it globally competitive in some fields, once China came on the scene, Brazil was no longer as competitive. At the same time, Chinese demand for natural resources drove up the value of the real, thus further handicapping Brazilian industry by increasing the cost of exports and lowering the cost of imported manufactured goods. The situation worsened, leading to a slowdown in 2005 and a public outcry about the economic situation that generated calls for more action by the state.

The turning point came around 2006. As a result of a political scandal, Antonio Palocci, Lula’s finance minister, was replaced by Guido Mantega, a heterodox economist and academic closely linked to Lula. Palocci was also closely linked to the PT, had maintained an orthodox approach to economic policy, and was closer to the financial sector than to industry. His replacement opened a window of opportunity for the industrialists represented by institutions such as the National Industry Confederation (CNI), FIESP, and the Economic Institute for Industrial Development (IEDI), a business think thank, to push for policies that would allow them to recover and protect industrial chains dismantled during the 1990s, foster international competitiveness, and channel more state funds into infrastructure investments. Business support for neoliberalism, never so robust, declined, and its acceptance of state activism increased. Jackson De Toni suggests that “Brazilian industrialists partly conceded in their unconditional defense of a minimalist agenda for the state in exchange for a political economy that would maintain the inherited stability and defend them against external competition, but would also revive public investments in infrastructure.”


40 See de Castro, supra note 6.

In this context, continues De Toni, the Lula government created some new “arenas” for public-private coordination (including councils such as CDES, CNDI, and the so-called competitiveness fora) and new agencies (such as ABDI) in an attempt to ensure legitimacy while controlling the increasing demands of industrial entrepreneurs. At the same time it launched the Growth Acceleration Program (PAC) in 2007. PAC was designed to restart investment using the strength of public companies like Petrobrás to lead the process.

Another factor that helped cement political support for state activism was the global financial crisis. The pervasive and worldwide failure of markets, which were deeply affected by financial disorganization, epitomized the crisis of deregulated capitalism and legitimized the adoption of alternative policies. This gave more support for the expansion of industrial policy and the growing role of BNDES. The government adopted a rhetoric that stressed that the crisis was an opportunity for Brazil to gain comparative advantages, requiring proactive state action.

When the financial crisis broke out in 2008, the Brazilian economy was seriously challenged by the lack of credit. Like many institutions in the United States and Europe, Brazilian financial institutions halted the supply of credit. This led to more pressure by the industrial coalition for action by the Brazilian state. As a result, BNDES was heavily capitalized so that it could play a countercyclical role in the economy. BNDES sharply raised its disbursements, thus galvanizing a national industrial sector already suffering from reduced competitiveness and an unfavorable exchange rate and now also buffeted by credit stringency. In general, because of the worldwide crisis, the Brazilian government was able to become more active in shaping the trajectory of economic development.

**Structural Elements**

What problems did policymakers face and respond to as they shaped NSA? Three structural features were important:

- Major market failures that impeded economic activity, including a low level of investment in infrastructure and a lack of innovation
- Long-standing Brazilian social concerns
- The international embeddeddness of the Brazilian economy and its need to spur competitiveness

**Market Failures: Innovation, Infrastructure, Financial Sector, and Competitiveness**

Major domestic market failures forced policymakers to face the low level of innovation in Brazilian industry. By the early 2000s, they had recognized that Brazilian industry had slowed down and believed that markets alone could not restart the growth process and that state intervention was called for. The national economy had had its last impetus of vitality in the 1970s, during the
apogee of “old” development state policies. In that decade, Brazil underwent a second industrial revolution, acquiring a diversified industrial base. But the economy started to stagnate due to external and internal factors, and beginning in the early 1980s, the economy endured a long period of stagnation, in which growth slowed and Brazil fell behind the rapidly growing Asian tigers.

One external factor was changing global capitalist accumulation patterns and the consolidation of a knowledge-based economy, which made industrial innovation essential for economic competitiveness. The internal reasons included Brazil’s failure to reshape the political economy and the legal-institutional structure that underpinned the old developmentalism based on an alliance among the state, foreign capital, and national capital. The state provided infrastructure, organized key sectors of the economy through state-owned enterprises, generated savings that could be used for new investment, and created regulations and incentives to protect and promote the private sector. Foreign capital helped develop local industry using technology that had been created and perfected in advanced markets; sometimes this included bringing in equipment that had become obsolete at home. One effect of this arrangement was that the Brazilian economy was largely insulated from international competition. This, in turn, reduced the pressure for national innovation and the development of new technology: Brazil was limited to buying externally-generated technology. This helped slow the pace of development. Suzigan and Villela conclude:

> It was necessary to change not only to correct these problems, but also because there was [an awareness] that the country had reached the zenith of a historical development process (which many erroneously described simply as import substitution). Once an ample and diversified industrial basis [had been built], it was necessary to make it efficient and competitive. It was also necessary to incorporate sectors and industries representing new technologies, particularly informatics and telecommunications, and to develop innovation ability, a crucial element in competition.

During this time, Asian countries, noticeably South Korea and Taiwan, were on a brisk developmental pace, giving rise to a new round of growth based on knowledge, innovation, and reduction of poverty and inequality. Brazil and its Latin American counterparts lost vitality. One indicator is the

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relative success in patenting: Asians far surpassed Latin Americans in patents issued in the United States.

Brazilian policymakers took steps to increase the rate of innovation in industrial activity. Modest efforts to stimulate innovation began as early as 1999, but with the reintroduction of industrial policy in 2004, substantial resources were devoted to improving the overall climate for innovation; supporting restructuring in targeted industries; and fostering the development of new areas of specialization considered relevant and potentially able to consolidate key industrial chains.

Another structural barrier to growth was the low level of investment in infrastructure. The private sector was unwilling to invest in needed infrastructure expansion, and the state had not compensated for this deficiency. Although Brazil has one of the highest tax burdens in the world, public sector investment was relatively low, even by Latin American standards.  

The private financial sector played a large role in the structural economic failure in Brazil. Although it had grown in size and importance, the private sector still funded industrial expansion in only limited amounts. State banks, which date to the developmental period, filled the gap. When the Lula government decided to implement a broader industrial policy, it looked to the state banks, especially to BNDES, to prove the capital and expertise needed for growth, innovation, and competitiveness and to buffer the effects of the financial crises. Unlike other developing countries, Brazil did not dismantle its development bank in the 1990s, so that institution was available when the government decided to intervene more actively in the economy. Today, the state bank is the main source of long-term financing in Brazil and a key actor in the conception and implementation of industrial policy.

The fourth structural problem that affected the emergence of state activism is the side effect of the Plano Real. Undeniably, the Plano Real achieved its goal of ending runaway inflation. Since 1994, when the plan was implemented, inflation has been kept in check at around 5 percent per year. The problem, however, is that this plan is anchored in the interplay of two physical constraints are obvious and seriously threaten future development.”  

José Roberto Rodrigues Afonso, Erika Amorim Araújo, & Geraldo Biasoto Júnior, Fiscal Space and Public Sector Investments in Infrastructure: A Brazilian Case-Study, 1141 Textos Para Discussão IPEA (2005). Commenting on the infrastructure deficit in Brazil, Daniel Perrotti notes: “Although several factors were involved (such as high macroeconomic volatility, the lack of comprehensive policies and regulatory and financing issues), the effects of these physical constraints are obvious and seriously threaten future development.” See The Economic Infrastructure Gap in Latin America and the Caribbean, 293 FAL Bulletin (2011), available at http://www.cepal.org/usi/noticias/bolfall/6/42926/FAL-293-WEB-ENG-2.pdf (accessed Jul., 20, 2012).

BNDES and the other major state banks have access to public (pension and treasury) funds, so their cost of capital is well below that of the private sector. BNDES also makes profits and raises funds in the capital market, besides offering substantial expertise; the bank has been financing the Brazilian industrial sector for 50 years and has developed detailed knowledge of many important sectors and close ties to industry that add to its advantages over the private sector.
macroeconomic variables: interest rate and exchange rate. Whereas the interest rate is the main control against inflation, the exchange rate is directly influenced by the interest rate: if the interest rate is high, it attracts foreign investment, which results in an appreciation of the exchange rate. This has two direct consequences. First, the regulation of inflation by management of the interest rate creates side effects in the financial markets, inasmuch as appreciation of the value of the currency encourages investors—including foreign investors—to buy government bonds. This means that less money is available for the private sector. Second, the resulting appreciation of the exchange rate affects domestic industry because it makes imports cheaper and exports less competitive. This situation put pressure on policymakers: industry pressed for solutions that would lower the cost of finance and guard against deindustrialization. Industrial policy seemed like a way to handle both concerns.

**Social Concerns**

Social concerns shaped the development of NSA in Brazil, in particular four issues: poverty, social inequality, unemployment; and the tendency of wages to lag behind productivity.

In 1981, 31 percent of the Brazilian population was living on less than US$2 per day. Other social indicators were negative: child mortality was high, life expectancy at birth was only 63 years, illiteracy was widespread, and many people had no regular access to sanitation and potable water.\(^48\) Economic inequality was extreme. Brazil has been profoundly unequal and unjust for a long time: in 1990, the Gini coefficient was 0.6091. The degree of inequality is further aggravated when considering race and gender. Unemployment was also high: the rate of unemployment reached 10 percent in the early 1990s, and from the 1980s to 2000, unemployment was a crucial political issue.\(^49\) Education was also a problem: the education system did not produce the number of skilled people needed by a growing and competitive economy. Industrial policies designed to spur technological upgrading were hampered by the lack of adequate human resources; people did not have the skills needed in a changing labor market. The government recognized the need for job creation and skills upgrading in connection with social and welfare initiatives.

Wage lag is another social issue in Brazil. Because of the large rural population in most Latin American countries including Brazil, a huge pool of underemployed workers depresses wage levels.\(^50\) As a result, domestic demand does not grow as fast as domestic production, thus hindering growth of the

\(^{48}\) Data in this section is taken from Mauricio Font & Laura Randall, *The Brazilian State: Debate and Agenda* (Lexington Books, 2011).

\(^{49}\) Id. Some observers put the effective rate as high as 20 percent.

\(^{50}\) This is what W. Arthur Lewis called development with “unlimited supplies of labor.”
domestic market. Economists stress the need for government action to offset this with an income policy that will bring wages up to optimal levels.51

**International Embeddedness and the Need to Spur Competitiveness**

A third structural feature affecting the emergence of NSA was Lula’s decision to liberalize the economy and maintain openness. Although export promotion had been a development target since the 1960s, domestic industrialization dominated the governmental agenda until the 1990s. This situation changed with globalization and liberalization. In the 1990s, Brazil opened itself to international competition and began to actively pursue export markets, forcing the state to pay more attention to competitiveness.

When Lula’s government took office, one of its first moves was to emphasize the need for state action to encourage the solutions needed to maintain competitiveness. This decision, brought about by the commitment to open economy policies, explains both the revival of industrial policy and the government emphasis on innovation. From PITCE through Brasil Maior, policies have focused on boosting the international competitiveness of Brazilian companies, including BNDES’s support for the internationalization of Brazil’s most competitive industries and various mechanisms to subsidize exports. Although the government has recognized the importance of competitiveness and that maintaining openness to foreign goods is necessary to preserve competitiveness, it has also taken measures to provide protection for domestic industries.

**Structural Elements: Conditioning Factors**

The stage was set for the government, led by the Brazilian Workers Party, to increase the role of the state in the economy. But why did Brazil’s role as a development state take the shape that it did? Why did Brazil opt for an innovation-focused and collaborative public-private form of industrial policy rather than, say, renationalization as did Venezuela, Argentina, Ecuador, and Bolivia? Why was Brazil supportive of foreign investment in most sectors? This section discusses factors that influenced the choices Brazil has made in its search to help the economy regain dynamism and promote inclusive growth. Among these factors, four are especially important:

- Constitutional considerations
- The strength and scope of the private sector
- International economic law and policy
- Global financial markets

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51 Bresser-Pereira, *supra* note 4 at 193.
Constitutional Considerations

The 1988 constitution influenced the choice of strategies and measures by making direct state control of industry both more expensive and less important than in the past. The new constitution protected property rights and regulatory commitments, thus making renationalization of privatized industries an expensive proposition. It reduced the possibilities for corruption and for private capture of state power, thus increasing the government’s capacity to steer the private sector and provide control and accountability mechanisms for the public sector. This made state ownership seem less necessary. Finally, by creating an open and democratic political structure, the constitution enhanced the power and participation of civil society, including industry, vis-à-vis the state.

The Private Sector

The size, complexity, and sophistication of the private sector in Brazil influenced the path of collaborative innovation-oriented industrial policy. The Brazilian economy includes many well-developed sectors and a growing capital market. Many firms are either at the global competitive frontier or close to it. Others have incipient capabilities. Many sectors accept the need for restructuring and continuous improvement. Many firms have the kind of deep knowledge essential for effective innovation even though they may not be able fully to utilize this knowledge without public incentives and support.

It must have seemed much easier to create incentives for these firms to innovate and provide support for new private start-ups than to try to replace them with state-owned enterprises. At the same time, the size and scope of the private sector meant that once democracy was restored, the private sector gained an important voice in public affairs. The private sector was eager to support an expanded role for the state as long as this support was offered in collaboration with industry and was appropriate to resume growth. Thus, Cypher notes:

given the many endemic macroeconomic problems that had made the 1990s a period of slow growth in spite of the restructuring of industry, powerful industrial groups (including the Federation of Industries of São Paulo) involved themselves in the electoral process in 2002 with the objective of “opening space for developmentalist ideas” (Delgado 2010: 125) . . . the business federations—the organizations representing the interests of Brazil’s vast and diversified industrial base—correctly understood Lula’s election as a mandate for a pro-growth strategy and as an indication that a structural change would occur opening-up channels of direct intermediation between the industrial sector and the new administration. . . . In short, there was a consensus between the PT and important fractions of industrial capital to reverse “the loss of the centrality of the State as an agent of accumulation.”

See supra note 39.
International Economic Law and Policy

World Trade Organization (WTO) law places restrictions on policies like export subsidies and weak enforcement of intellectual property that had been used by the East Asian states, so Brazil had to work around these restraints or find ways to defend them. The Lula administration did a little of both by defending some heterodox policies and modifying others. Because it never ratified the Bilateral Investment Treaties (BITs) signed in the 1990s, Brazil did not encounter similar restrictions in international investment law. Nonetheless, because the government recognized that foreign investment was important for its innovation strategy and sought to encourage its own firms to invest in foreign markets, it followed many of the principles of the investment regime. Similarly, while Brazil’s export surpluses and growing reserves have made it less dependent on international financial institutions, Brazil has been influenced by the World Bank and other international financial institutions that promote market solutions but accept industrial policy as long as it respects comparative advantage and focuses on innovation.

Global Financial Markets

The Lula government decided to rely on foreign investment to help it reach and maintain international competitiveness. It realized that classic protectionism would threaten the availability of such investment, while an innovation-oriented and collaborative industrial policy offering selected benefits and incentives to both foreign and domestic firms would be acceptable to investors.

Other Influences on the Emergence of NSA

Several other factors help explain the profile of Brazil’s NSA, including the increased professionalism of the state apparatus and bureaucracy, which made it possible to carry out industrial policy, and the rise of alternative economic theories that legitimized state activism. The macroinstitutional arrangement provided by the 1988 constitution contributed to upgrading state capacity and played an important role in NSA. In the past few decades, the Brazilian state has enhanced internal coordination, increased public-private collaboration, and learned how to better define policy mandates. Thus, NSA is partly the result of institutional learning, through which the Brazilian state progressively acquired greater administrative capacity and the expertise needed to implement complex and ambitious development policies.

Until recently, the vast majority of public employees was appointed politically, weakening the public service ethos necessary to build a professional bureaucracy staffed by people with technical expertise who can administer

53 See Alvaro Santos, Carving out Policy Autonomy for Developing Countries in the World Trade Organization: The Experience of Brazil and Mexico; and Michelle Ratton Sanchez Badin, Developmental Responses to the International Trade Legal Game: Cases of Intellectual Property and Export Credit Law Reforms in Brazil, in Trubek et al., supra note 1.
policies rationally and efficiently. There were some islands of excellence in public administration: some key institutions of developmental coordination, such as BNDES, Petrobrás, Embraer, Embrapa, IPEA, and the Central Bank, were professionalized. But these cases were in stark contrast to the rest of public administration, which compromised state capability. This lack of professionalism changed with the 1988 constitution, which mandated the recruitment of public employees through public and official exams (concursos públicos). As a result, there has been a substantial increase in the percentage of public employees selected meritocratically.

The constitution also regulates the ceiling of earnings, determining that the maximum wage should be no higher than that one received by members of the Supreme Court (Supremo Tribunal Federal). This rule was designed to limit public expense and curb discretionary distortions in the level of salaries. Although both meritocratic recruitment and wage policy face problems of enforcement, they represent an improvement in terms of governmental quality. When the Lula administration began to expand the state’s role, it could count on a more professional workforce in government.

Other measures helped enhance state capacity, making it easier to carry out the direction called for by NSA. The constitutional framework established in 1988 gave rise to policy initiatives designed to “implement rights” and “modernize” the state. New ministries were created, several others were reorganized, subministerial entities were added, and councils and committees were formed to increase participation by business and labor. In addition, BNDES has played an increasingly important role in industrial policy.

Changes in the world of ideas also facilitated NSA. With the turn to a more robust role for the state in the economy, and its particular profile in Brazil, there have been corresponding changes on the intellectual scene. Internationally, more attention is paid to the positive role industrial policy might play, and the World Bank has endorsed certain types of industrial policy.54 Similar developments are occurring within Brazil as Brazilian economists seek to explain and guide the evolving new configuration. Brazil has also attracted the attention of theorists around the world who hope to create a new political economy of development.55

The academic focus has resulted in analytical tools and offers intellectual justifications that can help sustain policy experimentation. Some observers have labeled the emerging set of ideas “new developmentalism.” James Cypher describes this approach:

On the one hand, New Developmentalism [rejects] prevailing ideas of neoclassical economics regarding a passive reliance on an export-


55 For a detailed discussion of Brazil and new developmentalism, see David M. Trubek, Law, State, and the New Developmentalism: An Introduction, in Trubek et al., supra note 1.
led, resource-based economy [and agrees with]. . . the original developmentalist economists such as Rosenstein-Rodan, Hirschman, and Nurkse, and their emphasis on the centrality of a developmentalist state. . . . On the other hand, New Developmentalism stresses a “growth with equity” approach along with an emphasis on industrial policy, highlighting public, growth-supporting, infrastructure spending, and a “neoschumpeterian” emphasis on building a national innovation system through deep public-private cooperative programs that will drive investment expenditures toward productivity-enhancing science and technology applications throughout the national industrial base of the economy.56

In Brazil, after the relative theoretical hegemony of liberal ideas associated with the Washington Consensus in the 1990s, a burgeoning literature has lent support for NSA. This can be seen in two different fields: economics (both macroeconomics and microeconomics) and political science. In economics, an important contribution has been research on the exchange rate and its effect on industrialization. According to the argument developed by Bresser-Pereira, there has been appreciation of the value of the real, leading to a “Dutch disease” effect that promotes deindustrialization.57 Due to the floods of dollars that have been reaching the Brazilian economy, the currency has become overvalued, with a negative effect on national industry. By showing that free market policies can lead to these negative effects, Bresser-Pereira and his colleagues created a rationale for an aggressive industrial policy. This criticism was accompanied by microeconomic studies that challenge the market-oriented model. These studies include sectorial and market analyses and document specific and pervasive market failures that require active industrial policies.58

In addition, microeconomists and political scientists have been providing inputs to social policy. Studies have demonstrated how economic inequality itself is a problem, detaching this problem from poverty. This sort of consideration has given impulse to the formulation of two different sets of social measures: poverty alleviation measures and instruments intended to reduce economic inequality more generally.

56 Cypher, supra note 39, comments that “As yet, New Developmentalism has not been rigorously defined. Some find that trial and error rather than the adoption of a coherent ‘model’ such as ‘new-developmentalistism’ better describes the current conjuncture,” citing Arbix & Martin, supra note 4.

57 The “Dutch disease” refers to the effect of a commodities boom on industry. Increased demand for commodities leads to appreciation of the currency, which makes industrial exports less competitive. This occurred in the Netherlands with the discovery of natural gas. See Luiz Carlos Bresser-Pereira, The Dutch Disease and Its Neutralization: A Ricardian Approach, 28 Brazilian J. of Pol. Eco. 47–71 (2008).

58 Two issues have been highlighted: failures in the market for innovation and gaps in the industrial chain. Studies conducted by Arbix & Pacheco and the Institute for Economic Applied Research show the need for innovation policies, while Erber, Cassiolato, & Kupfer highlight gaps in supply chains that require government action.
Challenge for Law

What does the emergence of NSA mean for law, and vice versa? As the role of the state in the economy and social protection changes, there will be corresponding changes in law. And it seems possible that law will shape and channel the path for policy innovation, as well as providing room for adaptation. This section outlines some general considerations about NSA’s challenges for law.

Although it is easy to say that law and NSA must in some way be mutually constitutive, it is another matter to say how NSA affects law and vice versa. Part of the problem derives from the complexity of the situation, and part from the paucity of empirical studies. Although abstract models of political economy such as neoliberalism and new developmentalism suggest clear delineations, in the real world, policies are a mix of the old and the new, layered on top of one another, and sometimes contradictory. This complexity and contradiction at the policy level carries over into the legal domain: key legal variables are difficult to define and causalities involving changes in the law and in policy outcomes are blurred. As a result, studies on relationships between the law and development policy present methodological challenges.

This section focuses on methods for understanding these relationships, outlines some functionalities that NSA seems to demand, and provides a few examples of how law has responded to these functional needs.

New Roles, New Frameworks of Analysis, New Functionalities

NSA will generate pressures for new laws and new roles for law. Much will be straightforward: statutes will change, procedures will be altered. This has been occurring in Brazil for years. Laws created ABDI, MDS, Cadastro Unico, and other institutions that are central to Brazil’s NSA. Laws aiming at specific goals such as innovation and competiveness are also important. Although recognizing the importance of these legal changes, this section focuses on “new functionalities”—roles for law that have not been as important (or did not exist in Brazil) in the past and take on new importance with the emergence of NSA.

Three sources were used to identify new functionalities and legal responses: research done by the project on Law and the New Developmental State (LANDS), of which this study is a part, other research on law and develop-

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59 LANDS, the Project on Law and the New Developmental State, is coordinated by the Global Legal Studies Center at the University of Wisconsin, Madison with assistance from CEBRAP (the Brazilian Center for Analysis and Planning), and Los Andes University. Funding for LANDS was provided by the University of Wisconsin School of Law, the University of Wisconsin’s Center for World Affairs and the Global Economy (WAGE), and the Ford Foundation.
ment policies conducted in Brazil; and “reverse engineering.” Reverse engineering means starting with policies and programs, describing the functions associated with them, and seeing if law has contributed, or could contribute, to those functions.

For NSA to be successful and new development policies to work, the government must maintain flexibility, orchestrate the relations among public actors and between them and the private sector, create conditions that will maximize synergy between actors, and preserve legitimacy. These functional needs point to new roles for law: if one isolates the role law can play in these new functionalities, one can identify four roles the legal system could play in NSA in Brazil: safeguard flexibility, stimulate orchestration, frame synergy, and ensure legitimacy.

Safeguard flexibility means to use legal norms to allow room for experimentation, to promote innovation, and to facilitate feedback from experiments to policy. NSA demands legal regimes that permit learning by doing and that encourage path correction. Different from import substitution and neoliberalism, NSA requires the assurance of some degree of flexibility and learning to implement initiatives that in most cases do not resemble preexisting recipes or strategies; this is one reason why NSA employs “new governance” tools.

Stimulate orchestration means to use law to structure state activities for effective industrial and social policy. This means facilitating coordination and articulation within the state—both horizontally (that is, between entities that belong to the same bureaucratic state level) and vertically (that is, between entities that are subject to hierarchies or belong to different state levels).


61 The idea of reverse engineering appears in David Kennedy, The Rule of Law, Political Choices, and Development Common Sense, in The New Law and Development — A Critical Appraisal (David Trubek & Alvaro Santos ed., Cambridge U. Press 2006), in the context of a discussion of the postwar consensus (1945–70). Kennedy reckons that although there was a clear demand for instrumental law during this period, the legal theory was implicit. In order to reveal it, he proposes, “We need to reverse engineer the legal theory of mainstream development professionals from their economic and political projects, and from the attitudes toward law they manifested in managing developing policies within national administration. A great deal of law was required to translate the leading economic theories of development economic policy.”

Orchestration can consist of norms and procedures that assign institutional tasks and foster cooperative (rather than competitive) governance regimes, including rules that encourage government to work with the private sector. Also, it can mean supporting policy networks that share tasks and interact in a complementary way to implement policies; this can include defining policy hubs. Finally, orchestration can mean using norms that harmonize new policies with preexisting ones to ensure coherence. Norms and processes playing these roles are crucial in NSA because it relies on the integration of different fields.

*Frame synergy* involves using the law to frame public-private partnerships and ensure that they are more effective than purely public or private solutions. Such modalities include collaborative governance regimes that create incentives for public-private cooperation (through incentive alignment and/or the use of private contracts by public entities), risk sharing, and hybrid instances in which public and private players regularly meet to interact and exchange opinions on regulatory and contractual instruments that bring private expertise and public financial capacity together.

*Ensure legitimacy* means to keep government transparent and ensure adequate participation. NSA requires a regime in which it is easy for new ideas to percolate upward and be widely shared. This makes older authoritarian models obsolete and increases the importance of democracy. Legal regimes must ensure accountability, transparency, and participation in development policies, which requires norms for disclosure, frameworks for participation, methods to hold policymakers accountable for results, and ways to avoid industry capture of government at the same time public-private dialogue is fostered.

Developments in industrial and social policy illustrate how Brazil is dealing with these new needs and functionalities.

**Flexibility and Synergy in Industrial Policy**

The industrial policy promoted by NSA in Brazil is as much process as policy. It is part of a joint public-private discovery process, a collaboration through which partners experiment with different trajectories to identify products and processes that are optimal for individual firms and sectors as a whole. Efforts to encourage innovation through a full-scale partnership with the private sector move the state into new territory. For example, instead of traditional arms-length lending with well-defined goals set in advance, internationalization strategies for Brazilian companies and innovation financing call for substantial flexibility, risk sharing, and alliances—this requires legal innovation.

One area in which this is occurring is BNDES’s program to foster innovation that replaced its traditional form of fixed obligation loan agreements with a variety of flexible devices that support collaboration and experimentation. The tools developed for this purpose represent a break in BNDES’s

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63 Coutinho & Mattos, *supra* note 60.
legal pattern: the bank relies on flexible legal structures that, formally or informally, support a financial relationship that permits changes of trajectory and adaptation of plans. These legal tools include partnerships with technological institutes and grants to promote the development of new products; relational loan contracts that include nonbinding performance criteria, staged disbursements, and constant BNDES monitoring through shared governance mechanisms; equity investments coupled with shared governance established through shareholder agreements that give BNDES a seat on the board and that subject certain corporate decisions to its approval; and arrangements by which BNDES participates on the investment committee of venture capital funds that it assists.64

Other new legal mechanisms connected with industrial policy include risk sharing with the private sector, soft law, and special public-private partnerships. Risk-sharing agreements are designed to encourage private investors to increase investments in technological research and innovation, expand industry capacity and exports, and acquire assets abroad in order to exploit comparative advantage in sectors where Brazil is a global leader. Soft law has also been used to induce investment. For example, governmental letters of intent communicate public investment strategies and serve as signals for the private sector, inducing private investment decisions. Other tools that create incentives for private companies to innovate include public-private partnership contracts, cooperation agreements between government and research centers, and flexible private law contracts (credit contracts, shareholder and investors agreements) between government and corporations.

**Orchestration and Decentralization in Social Policy**

Brazil has sought to strengthen its welfare state through cooperation among the several levels of government in the federation. It also brings together different types of social policies to deal with major problems. This requires a continuous orchestration of different levels and types of policies (universal and targeted, federal and local, contributive and noncontributive). Thus, the government has found new uses for old administrative law tools and created new instruments. This strategy can be seen in BFP, which uses a registry for all social programs (Cadastro Único) and a decentralized management index (IGD) to coordinate the work of several ministries, local administrators, and other public actors and to encourage policy innovation. BFP uses conditionalities—obligations of recipients for child education and health—that it enforces through revisable regulatory rules such as ordinances. It employs the Cadastro Único to gather data and reduce asymmetric information with the purpose of expanding education and health coverage. It also adopted a carrot-based

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64 Mario Schapiro, *Rediscovering the Developmental Path? Development Bank, Law and Innovation Financing in the Brazilian Economy*, in Trubek et al., *supra* note 1. Although the bank’s innovation funding clearly represents a new form of state activism and new approaches to law, Schapiro emphasizes that the program represents a tiny portion of the bank’s total portfolio, and it is unclear whether this segment of the program will expand in the future.
federal arrangement through the use of financial incentives such as IGD to get municipalities to gather data on very poor families.

In addition, IGD aims to encourage Brazilian cities to deliver effective performance, employing funds to reward those who provide dependable and quality information, maintaining updated data in the Cadastro Único, and providing information on the effect of the health and education conditionalities. BFP uses contractual arrangements with cities to ensure that they set up local agencies of social control and participation. These agencies receive IGD funding to support the BFP management and develop activities with recipient households, including managing conditionalities and benefits, monitoring recipient households, registering new households, updating and reviewing data, implementing complementary programs for basic adult literacy, providing occupational training, creating jobs and income, stimulating regional development, and strengthening BFP’s social control.

This system has led to a more collaborative (rather than imposed) and flexible (rather than based on rigid rules and sanctions) relationship between the federal and local levels. Such an articulation fosters decentralization (with federal guidance, steering, and expertise) and is the result of a broader picture in which, although universal programs remain central, “targeting within universalism” has been fostering development outcomes.

**Experimentation and Synergy in Labor Law**

In a study of new approaches to the enforcement of labor laws in Brazil, Roberto Pires shows that labor inspectors using flexible and reflexive experimentalist governance approaches had more success than their peers who employed more traditional management tools. The study compares two different styles of enforcement: one, drawn from the theories of the new public management stresses, specific targets and quotas; the other, which draws more on the experimentalist governance literature, stresses public-private cooperation, dialogue, exploration of options for compliance, careful analysis of the causes of violations, and revision of goals and standards as mutual learning progresses. Pires shows that through a system of hybrid governance that employs experimentalist methods while keeping sanctions in the background, health and safety inspectors in Pernambuco are able to significantly reduce the incidence of industrial accidents.

The key to this success, Pires suggests, is creating institutions that allow interaction among government, business, and labor; encourage the search for

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67 New public management refers to the idea, and consequent policy prescriptions, that market-oriented management of the public sector will lead to greater cost efficiency for governments. It gained its momentum during the 1990s.
ways companies could revise their business plans to comply with the law and still prosper; and facilitate experimentation with new technologies that might reduce risks of accidents at low cost. He notes that because of the success of these methods, the experimentalist model has been scaled up to the federal level. Although Pires does not relate his study and the growth of experimentalism in governance directly to the new political economy of development or how the Brazilian government is redefining its role in that development, the affinity between the development literature and changes in public administration seems clear.

Building Legal Capacity for Development: Trade Law

In addition to adapting law to deal with functionalities demanded by NSA, Brazil has built the legal capacity needed to shield the new industrial and social policies from restrictions that might be imposed by international law and policy. Built into NSA are policies that challenge some orthodox prescriptions backed by international economic law, including restraints on export subsidies and stricter protection of intellectual property. The clearest example of this kind of legal response is in the field of trade law.68

When it initially joined the WTO in 1995, Brazil accepted the full package of WTO agreements without first determining to what extent they might clash with domestic policies and priorities. But as neoliberal enthusiasm waned, successive administrations protected domestic policy space by challenging restrictive interpretations of global trade rules. This growing willingness to challenge WTO-based restrictions is a result of changes in development policy and in the way trade policy is formulated in Brazil. As the state began to play a more robust role in the promotion of economic growth and social protection, trade policymaking became more closely integrated with overall development policy, and Brazil invested in the legal and related skills needed for success in trade disputes. At the same time, the arena for discussion of trade policy expanded as more government agencies began to participate and the private sector and a flourishing civil society movement entered the debate. As a result, Brazil has been able to use trade law as a shield for policy innovation.

In the case of intellectual property, Brazil was able to carve out space within the regime for the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) that allowed it to negotiate better prices for antiviral drugs. Although initially it seemed that TRIPS would preclude this kind of action, a number of changes in law, politics, and government organization at the domestic level, as well as action in the international arena, strengthened the Brazilian government’s capacity to shape domestic health policy in the face of international constraints. The judiciary entered the arena to enforce a

68 See Alvaro Santos, Carving out Policy Autonomy for Developing Countries in the World Trade Organization: The Experience of Brazil and Mexico; and Michelle Ratton Sanchez Badin, Developmental Responses to the International Trade Legal Game: Cases of Intellectual Property and Export Credit Law Reforms in Brazil, in Trubek et al., supra note 1.
constitutional right to health, administrative changes were made that opened trade policy discussions to a range of interests, and the legislature was mobilized.

Specific legal changes at the domestic level included reforms of the legal system in order to eliminate TRIPS-plus provisions; authorization for use of flexibilities such as compulsory licenses; the approval of new mechanisms implicitly authorized by the international system that favor access to technology; and the creation of new government institutions that could serve as countervailing powers to industry interests in the patent approval process. Brazil and other developing countries carried on a campaign at the international level that led the WTO and the World Intellectual Property Organization (WIPO) to take a more supportive stance toward the use of policy in this field.

Brazil has been able to legally protect domestic trade policy from WTO restrictions. As part of its new industrial policy, Brazil sought to build Embraer into a national champion and facilitate efforts to develop market share in the global regional jet market. Government financing is an essential part of any deal for aircraft manufacturers, and Embraer had been hampered by the high cost of finance available to Brazilian companies. The government decided to provide a subsidy to the institutions that provided finance for Embraer sales. Canada’s Bombardier challenged this practice as a violation of the WTO subsidies code. After a long and drawn out litigation, Brazil was forced to make changes in its subsidies. But through a partially successful campaign that drew on the growing capacity of government and industry working together in the trade law field, Brazil was able to preserve part of the subsidy program and shift the issue of aircraft financing terms into the Organization for Economic Cooperation and Development (OECD). By moving the issue to the OECD, Brazil gained a voice in the main forum affecting global rules for aircraft finance. This meant it has a say in the terms affecting its competitors and thus more bargaining leverage in the continuing dispute with Bombardier.

Conclusion: Assessing the Brazilian Experience in Development Policy and Law

The Brazilian foray into NSA is a work in progress. Policies are altered as domestic and international conditions change. Industrial policy seems to be working and is helping the country both weather the storms from the global financial crisis and resume economic dynamism. World markets have accepted this trend, and foreign investment has soared. Significant gains have been made in poverty alleviation and the reduction of economic inequality.

Yet questions remain. Is a coherent model of a new development state emerging, and is Brazil’s new state activism likely to become consolidated? Does the government have the capacity to manage and implement the ambitious set of processes and policies that have been put in place? Can Brazilian institutions develop and sustain the new roles demanded by NSA? Finally, is the Brazilian experience unique to that country, or can it be replicated?
A New Development State?

Although the current situation in Brazil is described here as NSA, a discussion of a “new Brazil model” in the sense of a coherent and stable configuration of state, law, and political economy would be premature. Brazil is experimenting with a variety of new policies and procedures. Many of them have yet to stand the test of time. But the trends show continuous movement toward a set of policies that could cohere into a sustainable model. A new form of industrial policy stressing state assistance for innovation and competitiveness in the private and public sectors is in place and has been combined with a robust social policy. The commitment to NSA has lasted for more than a decade, through two presidential elections. President Dilma Rousseff has deepened the government’s commitment to the new industrial and social policies.

Does Brazil Have the Capacity to Manage and Implement the New Policies?

NSA places great demands on the state, which must be able to assist the private sector without stifling it. It must make choices among sectors, industries, and firms in the public interest. Complicated decisions involving massive sums of money require both technical expertise and distance from special interests. Through a series of reforms, the Brazilian state bureaucracy is more professional today than it was in the past. But this is not true everywhere, and in many areas inefficiency, bureaucratic rigidity, or both, persist. Finally, the risk of corruption and capture is always present. Some measures have been taken to limit corruption; although new anticorruption laws and agencies have been created, corruption remains a problem in Brazil as elsewhere.

Can the Brazilian Legal System Meet the Needs of NSA?

Brazilian law can contribute to the operation of the new policies and procedures under NSA. In at least a few cases and a few areas, new legal tools are being created and old ones are being put to new use. The legal system has the capacity for innovation that new developmentalism demands. But it is not clear that this is happening—or will happen—in all the areas where change is needed. The cases that have been studied suggest it is possible, but they are too limited to warrant a conclusion. For that to happen, many rigidities and obstacles in the Brazil legal system must be overcome.

Is the Brazilian Experience Unique, or Can It Be Replicated?

There is no question that other nations can learn from the Brazilian experience in development policy. The approach to industrial policy that assists the private sector and fosters structural changes needed for competitiveness can be followed in other countries. The potential for using a state development bank as an engine of innovation and growth also provides lessons that can be replicated. Brazil’s successful merger of industrial policy and social policy is worth further study. The same can be said for the Brazilian experience in law and development. To the extent that countries adopt aspects of NSA, they will
need to adapt their legal system to new functionalities and can learn from the way Brazil has developed legal institutions that address these needs.

That does not mean, however, that the Brazilian experience has resulted in a template that can be followed by everyone, everywhere. The account presented in this chapter has stressed the contextual features that explain Brazil’s turn to NSA, such as a large, well-developed industrial sector, advanced research centers, a huge domestic market, a democratic constitution, a professionalized bureaucracy in key agencies, a long history of state involvement in the economy, and some transformative capacity in legal institutions. Because the development of NSA in Brazil is based on these contextual features, NSA in the Brazilian form will not be easily replicated in countries that lack any or all of these features.