

## Economics Group

### Special Commentary

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# Brazilian Pension Reform in Queue

## Executive Summary

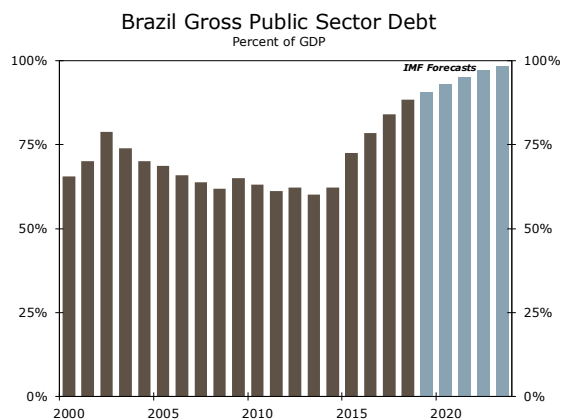
Brazil’s President, Jair Bolsonaro, submitted his much anticipated pension reform proposal to congress last week. While the proposal should keep markets optimistic in the short term, a fractured congress and a lengthy constitutional amendment process are likely to make an approval challenging. As developments unfold and the administration’s reform proposal gets challenged in congress, we believe the Brazilian real will begin to gradually weaken over time.

## Outlook for Pension Reform in Brazil

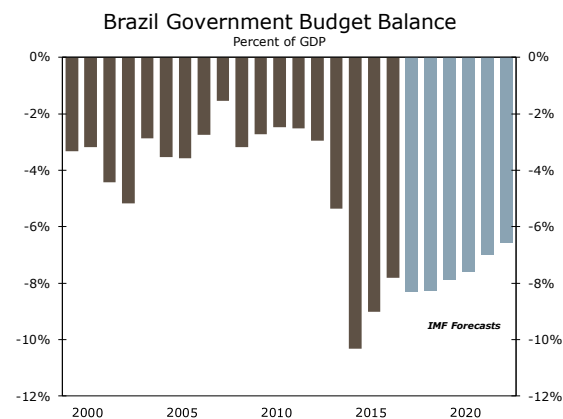
Bolsonaro’s pension reform plan should keep markets optimistic on the Brazilian real in the short term, as many of the key points he needed to address were included in the proposal. One of the highlights is a required minimum retirement age for both men, proposed to be age 65, and women, age 62. Bolsonaro’s proposal also includes a plan to make pension contribution amounts more progressive, raising the contribution rates for households with higher incomes, while lowering rates for workers with lower incomes. The current version of the bill also seeks to adjust special pension regimes, particularly for teachers, military and police officers, a provision prior proposals did not have. In aggregate, the plan is estimated to save the government about 1.16 trillion reais over the next 10 years, approximately 9% of nominal GDP, a much more aggressive plan than what ex-President Michael Temer brought to congress. This may be significant enough to support government finances and put Brazil’s debt ratios on a more stable trajectory.

***Bolsonaro’s pension reform plan should keep markets optimistic on the real in the short term.***

**Figure 1**



**Figure 2**



Source: International Monetary Fund and Wells Fargo Securities



***We remain cautious over the medium to long term as the process for implementing pension reform is likely to be challenging.***

However, the process of congress approving Bolsonaro's reform bill is likely to be quite challenging, with the bill headed to the lower house of congress (Chamber of Deputies) first. In order for the bill to pass through the lower house, a three-fifth's majority vote must be achieved (308 votes). As of now, estimates suggest the bill is about 60-70 votes short of being passed, meaning additional support will eventually be needed, something which will likely not be achieved swiftly. Aside from being divided, the lower house can also make amendments to Bolsonaro's original proposal, which we expect to occur given congress' history of diluting prior pension reform proposals, as pension reform is broadly unpopular in Brazil. This will likely slow the approval process and has the ability to reduce the bill's potential impact on government savings. Assuming the plan can pass the lower house, which is not assured, the bill can still face potential amendments in the senate, and will then still require a three-fifth's majority for the bill to be officially passed and for pension reform to be legally implemented.

While we share short-term optimism for the real based on the bill's intentions, we remain cautious over the medium to long term as the process for implementing pension reform is likely to be more challenging than markets currently expect. A fractured congress will likely make the approval process difficult, while congressional amendments to the bill will likely contribute to a delay in the approval until mid-2019 or later. As a result, we maintain our forecast for a gradual weakening of the real over a medium to long-term horizon and place a 60% probability that any version of a pension reform gets passed.

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