Protesters chant anti-corruption slogans during a soccer match between Brazil and Mexico.

Brazil may see debt rise

S&P issues warning on public spending

BY **WALTER BRANDIMARTE**
Reuters

RIO DE JANEIRO – Nationwide protests could force Brazil to increase spending on public services at a time when its fiscal performance falters, Standard & Poor's warned on Wednesday, adding, however, that it is in no rush to decide whether to lower the country's debt ratings.

The ratings company, which last month said there was a one-in-three chance the country could lose its "BBB" rating over the next two years, said a decision on the matter will mostly hinge on Brazil's policy response to an adverse environment of low economic expansion and fragile investment growth.

A debt downgrade could come "if there is a greater sense of intervention in the public sector, which will increase debt levels," Sebastian Briozzo, S&P's lead analyst for Brazil, told investors and journalists in a web conference.

"There is very limited room to maneuver on the fiscal side," Briozzo said.

He added, however, that S&P "does not foresee any rapid change" in Brazil's ratings, but intends to make a decision in the next 12 to 24 months.

S&P was the first of the three major ratings agencies to lift Brazil to investment grade five years ago, when the country benefited from a commodities boom and was considered an emerging-market star.

The company's downgrade warning last month was seen as yet another sign of foreign investors' disappointment with Latin America's largest economy, which seems to be headed to a third straight year of subpar growth.

Briozzo said S&P revised Brazil's rating outlook to negative on June 6 because "we've seen some signs of potential use of fiscal policy in a way that is not consistent with the current rating."

In recent months Brazil has deployed a series of tax breaks and other fiscal stimulus, in a failed attempt to shore up the economy.

Those measures, along with weak economic growth, have lowered Brazil's primary surplus to 1.95 percent of its gross domestic product, less than the 2.3 percent the government has promised to deliver.

S&P would probably be comfortable with a primary surplus of about 2 percent of GDP, Briozzo said.

Since S&P revised Brazil's rating outlook to negative, Brazil's political and economic outlook was complicated by an unexpected wave of mass protests demanding better public transport, hospitals, and schools.

S&P does not see any governability issues arising from the protests. It believes the demonstrations may result in additional emphasis on structural reforms, but it also worries about the costs of meeting protesters' demands for better public services.

"Before these events happened, the strategy was that private investment had to take the lead, but there was no sense of urgency," said Briozzo.

"These demonstrations have shaken the status quo, and there could be a new sense of urgency (for reforms). How it translates into action, we'll have to see."