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Fool's Gold

Comparing Two Political and Economic Crises in Brazilian History

By Carrie Katan

This paper's goal is to compare and contrast the political and economic crisis that affected the Brazilian military dictatorship from the late 1970's to mid 1980's to the political and economic crisis currently affecting Brazil in order to get a better idea of what may be the political effects of the current crisis. This paper argues that both the current crisis and the one under the dictatorship stem from similar causes. It also argues that Brazilian democracy, much like the military dictatorship before it, risks being fatally undermined politically by an economic crisis it is responsible for.

Whether a member of a poor nation's elite desires economic growth for the sake of the poor or the good of the nation, or, far more likely, to stay in power, the elite want economic growth as soon as possible. But this headlong rush into a prosperous future is not easy to carry out and cannot be sustained for long unbroken stretches of time. Often instead of dealing with major issues in the economy, elites will continue down an unsustainable path only worsening the inevitable economic, and often associated political, crisis. Brazil has been down this route multiple times in recent history, the two most recent times under a decade's long military dictatorship stretching from 1964 to 1985 and under a string of Workers Party lead government from 2003 to 2016. Both the Workers Party and the military dictatorship embraced similar economic programs, a rapid buildup in debt, unwillingness (or inability) to change in the face of a changing economic situations, and ineffectual state involvement in the economy particularly relating to State Owned Enterprises, in hopes to protect their hold on power only to cause a major economic and political crisis in Brazil.

Both the military and the Workers Party governments ran Brazil for well over a decade while never seriously deviating from the economic strategies they began with, regardless of whether they still made economic sense or not. In 1964 the Brazilian Military toppled democratically elected President João Goulart largely to stop the President from enacting left-wing economic reforms. After the military took power it spent a few years employing an economic strategy called "shock therapy" restricting the money supply causing a recession but bringing inflation down.¹ After 1969 the military government began an economic policy it's predecessors would continue until the 1980s encouraging the creation and growth of State Owned Enterprises or S.O.E.s, funding aggressive industrialization programs through debt, keeping economic growth high, and focusing on increasing exports. These policies worked rather well in the early years, producing 11.5% average yearly growth between 1968 and 1973 without triggering high levels of inflation leading some observers to call this "The Brazilian Miracle". However, the oil crisis of 1973 and 1979 each made this economic strategy less and less practical by depressing the economies of export markets, stoking inflation, and increasing the cost of borrowing. Instead of changing course and reverting to the deeply unpopular "shock therapy" strategy they had successfully used to control inflation in the late 1960s the Brazilian government borrowed more money to try to industrialize even faster. Continuing this push until it was left with the highest debt of any developing economy, high inflation, and an inability to borrow more money putting them at the mercy of the demands of the International Monetary Fund.² Decades later the Workers Party would make the same mistake of keeping an economic model for longer than it was useful. After President Lula was elected into office in 2003 as a candidate of the Workers Party, his government slowly and tentatively moved away from the fiscally tight policies of the preceding government. Instituting a variety of programs to develop the country and deal with poverty. This caused government expenditures to steadily rise from 29 billion U.S. dollars in the 4th Quarter of 2003 to 52 billion dollars into the 4th quarter of 2008. At the same time the level of debt relative to GDP did not change significantly because the Brazilian economy was expanding from under one trillion U.S. dollars in 2003 to over two and a half trillion

1 Joel Wolfe, "Military Dictatorship and The Economic Miracle" Lecture for History of Modern Brazil 359 Umass Amherst, Amherst, Massachusetts, November 13th, 2017, Accessed November 13, 2017.

2 Antonio de Souza Aguiar Marco, et al. "Economic Dictatorship versus Democracy in Brazil." *Latin American Research Review*, vol. 11, no. 1 (1982), pp. 13–25. www.jstor.org/stable/2633263.
 DOI: <https://doi.org/10.7275/gp8m-n406>

in 2011.³ The high cost of commodities on the international market including many Brazilian exports, notably soybeans, petroleum, and iron ore, played a large part in this economic growth. This model of high government spending propped up by a growing economy and high commodity prices managed to make Brazil “one of the last to go into recession in 2008 and one of the first out in 2009” according to *The Economist*.⁴ However the period of high commodity prices and a rapidly growing Brazilian economy disappeared in the early 2010’s with oil, soybean, coffee, and iron ore prices all falling. Instead of cutting back, government spending continued to increase at a similar rate as it had when there were more favorable economic conditions. This caused the federal debt to increase by 16% of GDP between 2014 and 2016. At the same time state debt climbed as the federal government under President Rousseff, a member of the Workers Party and Lula’s chosen successor, failed to enforce rules on fiscal spending for states. Not only did Rousseff continue her predecessor’s policies, but she also pushed for populist measures like price controls and low interest rates that reduced business confidence and hurt consumers with inflation. President Rousseff, much like the leadership in the later years of the military dictatorship, not only stayed with an economic system designed for a different world economy, but pushed it further making the following economic contraction worse.⁵ Once again the leaders of Brazil had found an economic policy that worked well at first but stuck to it far too long, causing both governments to fall in tandem with the economic policies they were unwilling to deviate from.

Another issue both governments shared is that connections between business and government caused major issues, this is and was especially true for State Owned Enterprises. The State Owned Enterprises, S.O.E.s, the military government created either failed or delivered a return on invested government funds after the dictatorship had fallen. The military government did not introduce S.O.E.s to Brazil, what it did do was drastically increase their number, adding 231 S.O.E.’s from 1966 to 1973 compared with the 40 that had existed around the time the military took power.⁶ Between the late 1960’s and early 1980’s the percent of revenue generated by manufacturing S.O.E.’s as a total of the revenue of the biggest 500 companies in Brazil grew from 15% to around half. Their increased size and number however did not mean S.O.E. were economically successful. Some of these S.E.O.s were out right failures, Nuclebrás, in charge of developing nuclear power in Brazil poured billions of dollars into constructing two nuclear reactors that produce a small amount of intermittent power. As a whole Brazilian S.O.E.’s also did not escape the common international tendency of S.O.E.’s to be less willing to lay off workers in bad economic conditions compared to private companies leading to inefficient overstaffing. Some Brazilian S.O.E.s were referred to as “pockets of competence” or “pockets of efficiency” but that saying by itself implies that effective S.O.E.s were not the norm. The companies that the dictatorship bankrupted itself funding that did pay off in the long run only did so too late to save the dictatorship’s finances. Embraer made aircraft and was protected by the Air Force but the business would only become successful in the 1990s. Petrobras increased Brazil’s oil output starting in the 1980’s by expanding deep sea oil drilling, a

3 “Brazil Economic Indicators.” *TheGlobalEconomy.com*, accessed November 5, 2017, www.theglobaleconomy.com/Brazil.

4 “Lula’s Legacy.” *The Economist*, September 30, 2010, <https://www.economist.com/node/17147828>.

5 Kimberly Amadeo, “How to Ruin an Emerging Market Success Story.” *The Balance*, October 25, 2016, <https://www.thebalance.com/brazil-s-economy-3306343>.

6 Luciana De Souza Leão, “Bringing Historical Sociology and Path-Dependence Together: A Case Study of the Brazilian Political Economy (1930-2000).” *Historical Social Research/Historische Sozialforschung*, vol. 38, no. 2 (2013):172–196, www.jstor.org/stable/24145481.

technically challenging objective, but again the benefits from large amounts of investment needed to tap that oil would only come later.⁷ Either the time delay or the entire lack of an adequate return on capital invested in State Owned Enterprises would help lurch the military dictatorship into its fatal economic situation.

The Workers Party government, instead of causing issues by incurring too much debt pushing S.O.E.s experienced difficulties because it was caught using Petrobras, the national oil company and by far the most important S.O.E. in Brazilian history, as a source of illegal funds. The Workers Party, and later on with its ally the PMDB, initiated a major political and economic crisis by doing two things. The first was to appoint directors of the state oil company Petrobras who would buy overpriced goods and services from contractors in return for bribes which were then sent to the governing coalition. The second action was largely taken under the Rouseff administration which was to hand far more power to prosecutors allowing them to more aggressively go after corruption. These two actions resulted in what amounted to massive purge of the highest ranks of the Brazilian political and business elites taking out C.E.O.'s, politicians, and indirectly leading to the impeachment of Rouseff. The purge was powerful enough to eliminate entire companies, including Odebrecht a construction company involved with bribing Petrobras costing 100,000 jobs at a time of rising unemployment. Another effect of the anti-corruption campaign is that it became harder to pass laws since Brazilian system of government is dependent upon coalitions which are historically kept together by bribery. By taking away the capacity for governments to give coalition partners massive bribes it hurt any government's ability to pass legislation hampering any attempt to reform the economy to avoid or escape a crisis.⁸ The government's effectiveness at dealing with the economic crisis was also hampered by the distraction caused by the power struggle between the Rouseff administration and members of Congress, many of them angered by the threat to their power the anti-corruption campaign signified, ending with the protracted impeachment of Rouseff. In the long term, assuming the current system of government survives and Rouseff's successors don't hamper the law enforcement agencies involved in anti-corruption, the anti-corruption drive triggered by Rouseff should have positive economic consequences since eliminating corruption could open up markets to newcomers and remove a drain on business and government money.⁹ However much like the successes of S.O.E.s after the military dictatorship, the long term benefits will come too late to save the Workers Party's control over the government. At the moment the Workers Party needed to be most effective to deal with the problems of debt and low commodity prices it was fatally weakened by a massive corruption scandal of its own making; made possible because of the interconnectedness of the State Owned Enterprises and the government.

Outside of State Owned Enterprises the military government had other organizations and programs to sink borrowed money into in the name of building up the nation, with questionable results. One of these, Proalcool, a program that spent 30 billion dollars over two decades to support ethanol powered cars, despite ethanol only being competitive during periods of unusually high gas prices. Much like some S.O.E.s, the Proalcool

7 Ben Ross Schneider, "The developmental state in Brazil: comparative and historical perspectives." *Revista de Economia Política*, vol. 35, no. 1, (2015): 114–132, doi:10.1590/0101-31572015v35n01a07.

8 Vanessa Barbara, "Opinion | In Brazil, a New Nostalgia for Military Dictatorship." *The New York Times*, May 3, 2016, www.nytimes.com/2016/05/03/opinion/in-brazil-a-new-nostalgia-for-military-dictatorship.html.

9 Marina Lopes and Nick Miroff, "A Corruption Scandal Wrecked Brazil's Economy. Now, Workers Face the Consequences." *The Washington Post*, June 19, 2017, https://www.washingtonpost.com/world/the_americas/a-corruption-scandal-wrecked-brazils-economy-now-workers-face-the-consequences/2017/06/16/a2be0faa-505b-11e7-b74e-0d2785d3083d_story.

program is paying off economically now due to the high gas prices of the 21st Century but the benefits are coming in decades after the fall of the dictatorship.¹⁰ The government also sank massive amounts of money into producing durable consumer goods, resulting in new problems due to poor planning. For example the government encouraged the production of cars without upgrading the transportation network to function with a higher number of vehicles on the road.¹¹ Brazilian economic policies also turned Brazil into an oil importer in the 1970's causing the oil shocks of that decade to hit the Brazilian economy harder than they would have otherwise. Other major misallocation of resources included building a new railroad when repairing an old one would have been cheaper and building more power generating capacity than the country was projected to need till the year 2000. One of the Ministers of Social Welfare late in the military dictatorship Mr. Beltrao said of the technocratic central planners they were "dominated by the fascinating exercise of abstract planning, by the optical illusion of centralized decisions and macroeconomic theories, by the rapture of important and sophisticated decisions, incompatible with our reality and the reality of our modest standards and the incomes of our people."¹² What central planners thought in Brazil was a common for many in their positions, they believed they could industrialize their nation under their wise leadership at breakneck speed and in their arrogance they made expensive miscalculations which in this case would help bring down the dictatorship.

Compared to the Generals the leadership of the Workers Party spent government funds more efficiently with the exception of money lost to corruption (see above), the large amount of money wasted on hosting international sporting events, and under Lula's successor Dilma Rousseff. Hosting the Olympics is almost always a money sink costing far more revenue than it generates, the only recent exception to this rule being Barcelona in 1992.¹³ While the full economic cost of the Olympics is still not clear what is clear is Brazil spent far more to prepare the games than and it can hope to get back. Hopes that the games would raise Brazil's standing in the world were dashed since the the games instead highlighted it's descent into crisis. The World Cup is often also an economic mistake and looks to be in Brazil's case but to a lesser degree than the Olympics.¹⁴ Like the Generals, President Lula did use the government to invest in projects saying at the end of his term "Wherever you go in Brazil you will see work financed by the federal government," including schools, power stations, rail lines, and sanitation systems. But evidence suggests a far more sound development policy than the military's technocrats pushed. Poverty fell from 26.7 percent in 2002 to 15.3 in 2009, average schooling become two years longer, and the country saw a reduction income inequality all without increasing the debt relative to G.D.P..¹⁵ This defensible economic management ended during Demila Rousseff's presidency as she pushed more populist measures like price controls, cutting taxes while raising spending, and encouraging more lending. While these measures could win short term popular support, they lowered government's revenues while increasing expenses and fueling inflation. Rousseff also lost by these and other actions the business confidence

10 Schneider, "The developmental state in Brazil:," 123.

11 Marco, "Economic Dictatorship versus Democracy in Brazil.," 15-15.

12 Peter T. Kilborn, "BRAZIL'S ECONOMIC 'MIRACLE' AND ITS COLLAPSE." *The New York Times*, November 25, 1983, www.nytimes.com/1983/11/26/business/brazil-s-economic-miracle-and-its-collapse.html?pagewanted=all&mcubz=1.

13 Andrew Zimbalist, "3 Reasons Why Hosting the Olympics Is a Loser's Game." *The Atlantic*, July 23, 2012, <https://www.theatlantic.com/business/archive/2012/07/3-reasons-why-hosting-the-olympics-is-a-losers-game/260111/>.

14 Tim Vickery, "Football World Cup: Is It Worth the Expense of Hosting? - BBC Sport." *BBC News*, December 31, 2014, accessed December 4, 2017, <https://www.bbc.com/sport/football/30642071>.

15 "Lula's Legacy."

that Lula had worked hard to build between the Workers Party and business leaders leading rating agencies to lower the value of Brazilian debt making it harder to borrow.¹⁶ What multiple administrations had worked since the 1980's to build up, a sound fiscal and monetary policy that would inspire internal and external business confidence about Brazil Rousseff undid in a little over one term in office.

The answer the question of why both the Workers Party and the military behaved so irresponsibly and why that behavior got worse and not better with time is that political weakness caused them to adopt and stay with their economic model. The military did not switch to debt fueled industrialization of Brazil from its shock therapy approach in the late 1960's because the economic situation had changed rapidly, instead it came from the fact the political situation in Brazil was unfavorable to the military. While shock therapy brought down inflation it also resulted in the closing thousands of business and dissent from student, workers, and businessmen which posed a serious threat to the survival of the regime.¹⁷ That is why when a decade later when shock therapy could have reduced inflation and put the economy on a more sustainable path the military instead doubled down on debt fueled industrialization.¹⁸ The Brazilian military also was in the unusual position of knowing that they would not be in power forever since through the policy of decompression they planned to slowly hand power back to civilian control, this meant that the Brazilian military did not have to keep the economy going forever just until it became the problem of their civilian successors. Like the military, Dilma Rousseff would end up making bad long term economic decisions because she was too weak to make better ones and survive politically. This stems from the fact the Rousseff did not rise to power as Lula did through charisma and being well known, instead she became president because the Workers Party was popular and she was the only high level member to not be tainted by a Lula era corruption scandal.¹⁹ Neither as inspiring nor as good at deal-making as Lula it is doubtful she could have become President on her own, a fact that would hamper her ability to govern and win reelection. Her popularity was further hampered by the slow leak of information about the extent of corruption in the government that emerged during her time in office, which tainted Rousseff by association. If Rousseff had not pumped debt fueled growth into the economy, and she did increasing the debt by 10% of GDP in 2014 the year of the election more than the increase in the year before and after combined, it is likely she would have lost her bid at re-election rather than getting by with 52% of the vote in the second round.²⁰ Both governments drove the long and medium term growth prospects of Brazil into the ground and by doing so bought a temporary reprieve from their fall from power. This kind of short term thinking and unwillingness to change course would cause economic problems in any economy, however this problem is compounded in Brazil's case because its role in the world economy as a commodity exporter puts it at the mercy of changing conditions in the global economy beyond its control. The slowing of China's economic growth in recent years causing a fall in commodity prices, and the oil crisis of the 1970's, all hit Brazil hard because it was integrated into the world economy. Worse for Brazil the extreme nature of this boom and bust cycle along with the inefficient use of state spending meant that attempts to use Keynesian economic strategies to get over the busts required more money than anyone was willingly to cheaply lend Brazil. Neither the military administrations

16 Amadeo, "How to Ruin an Emerging Market Success Story."

17 Wolfe, "Military Dictatorship and The Economic Miracle"

18 De Souza Leão, "Bringing Historical Sociology and Path-Dependence Together:."

19 "Lula's Legacy."

20 "Brazil Economic Indicators."

nor the Rouseff administration could conceivably turn around and tell the Brazilian people that forces outside their control were going to increase economic hardship for the foreseeable future and there is nothing they can do about it. In a democratic system citizens will vote leaders out of office if they do not seem to be doing everything in their power to help the economy and in a dictatorship to admit the economy is beyond the leadership's control is to look ineffectual and to embolden the opposition. Both governments fell amid an economic crisis largely of their own making, but if they had not tried to avoid the inevitable downturn forced upon them by the wider world economy it is possible both governments could have been pushed out of office sooner.

Both the Workers Party and the military dictatorship were in the end pushed out of office ostensibly over falsifying records and being a dictatorship respectively, but it is doubtful if those reasons would have caused a regime change if an economic crisis was not affecting the population. As the Brazilian "Miracle" of the early 1970's receded into the past strikes began to take place in 1978 starting with a major auto workers strike in Sao Paulo demanding higher wages followed by a strike of three million workers the following year. The 1982 elections took place with an economic backdrop of inflation at 100 percent, and a debt crisis caused by a problem with serving the massive load of debt and a severe recession, helping opposition politicians sweep elections in the national, state, and local levels.²¹ The situation was further worsened for many Brazilians as the I.M.F. stepped in to keep Brazil from defaulting on its massive debt by imposing austerity, including wage controls on workers to control inflation. The government's attempts to tamp down on government spending lead some universities, doctors, and police officers either to go on strike or threatening to. Unemployment entered double digits with crime and malnutrition growing more prevalent as a consequence.²² As the economic situation further deteriorated The Direct Elections Now or "diretas já" movement, which demanded direct elections for President rather than through an electoral college as the military wanted, pulled hundreds of thousands of people onto the streets and had the backing of 90% of the population, showing what base of support the military had maintained through the 1970's had effectively evaporated.²³ Even though the "diretas já" movement failed, in that the 1984 Presidential "election" despite being controlled by a military friendly electoral college, the military candidate still lost to an alliance between the opposition and breakaway pro-military politicians.²⁴ While there had always been dissent against the military regime in the end the failure of its own economic model energized the opposition and weakened the military to such an extent it could not win even an indirect and rigged election. During Rouseff's administration decades later it would be largely the same story, the government's borrowing large amounts of money to keep the economy afloat, debts rise and borrowing becomes harder, the economy enters recession anyway, popular anger rises, and politicians go against the wishes of the executive branch and install new leadership. While the motive for many in Congress to remove her had more to do with the fear her anti-corruption campaigns would force them out of power, impeachment was only possible because rising inflation and unemployment caused Rouseff's approval rates to fall into the single digits. In both cases

21 Dr Joseph Smith, *History of Brazil*. (Routledge, 2016), 201-205

22 Alan Riding, "Brazil's Hard Life with Austerity." *The New York Times*, August 11, 1984, www.nytimes.com/1984/08/12/business/brazil-s-hard-life-with-austerity.html?pagewanted=all.

23 Alan Riding, "Direct Vote Demanded For Brazil." *The New York Times*, Feb. 18, 1984, www.nytimes.com/1984/02/19/world/direct-vote-demanded-for-brazil.html.

24 Joel Wolfe, "Challenge to Dictatorship and the Rise of New Democratic Actors" Lecture for History of Modern Brazil 359, Amherst, Massachusetts, November 15, 2017.

it was not the economy itself that brought down the government but the economy did weaken both regimes to such an extent that they fell. However while both the military and the Workers Party entered an economic crisis for similar reasons and lost power in comparable ways the current crisis is not playing out in the same way as the one at the end of the dictatorship did; meaning that it may not only be the Workers Party that falls but Brazilian democracy as an institution.

The economic and connected political crisis now occurring inside Brazil has not ended with the fall of the Workers Party and the new political landscape is far less stable and favorable to democracy than it was after the military pulled out of the government in the 1980's. Part of the reason for this is simple, with democracy in crisis it's only realistic alternative in Brazil dictatorship looks better, a process further helped by nostalgia distorting memories of the past. In the 1980's Communism was a spent political force in Brazil and around the world, and both hard and moderately authoritarian military rule had failed so democracy was the only realistic option.²⁵ Another problem in Brazil's current crisis that is different from the 1980's is that Rousseff's government did not institute the years of austerity necessary to start the recovery from the crisis fiscally before leaving office, leaving the deeply unpopular task to her former Vice President and successor Temer. Another problem with any belief that the Temer government can help push the recovery from the crisis is that all evidence points to him being highly corrupt which hurts his legitimacy.²⁶ As the Brazilian people deal with the economic crisis, political crisis, corruption, and rising crime many are turning to authoritarian solutions to the country's problems. In a 2014 Poll 51% of all Brazilians thought the streets were safer under the generals, and there is a widespread belief there was less corruption. During anti-government protests during Rousseff's impeachment, signs could be seen that read "Why didn't they kill them all in 1964?" and "Dilma it's a pity they [the military dictatorship] didn't hang you".²⁷ Another symptom of this authoritarian shift is the rise of the far-right Presidential candidate Jair Bolsonaro currently polling in second place behind former President Lula. Jair Bolsonaro served in the army during the dictatorship and in his time in Congress has punched a Senator, praised the dictatorship, mocked a rape victim and fellow member of Congress on air on purpose, and announced he would rather have a dead son than a gay son. This behavior has made him the favored candidate of Brazil's upper class because they believe he can keep the poor and minorities in their place.²⁸ Even if Bolsonaro is defeated in the election his rise shows that not only the Rousseff administration and the Workers Party has lost legitimacy in the eyes of many Brazilians but democracy and the norms that support it has too much like authoritarianism lost what legitimacy it had after the "Brazilian Miracle" fell apart. Whether the entire institutional setup of the Brazilian government will collapse due to an economic crisis is not now known; but it has happened before.

The quest to make a nation rich in a short period of time is always tempting for a nation's elite but these can lead to poor decision making especially a nation like Brazil where people have history of falling for a belief in quick fixes. State Owned Enterprises look tempting because the national leadership can summon massive

25 Barbara, "Opinion | In Brazil, a New Nostalgia for Military Dictatorship."

26 Jonathan Watts, "Operation Car Wash: The Biggest Corruption Scandal Ever?" *The Guardian*, June 1, 2017, <https://www.theguardian.com/world/2017/jun/01/brazil-operation-car-wash-is-this-the-biggest-corruption-scandal-in-history>.

27 Barbara, "Opinion | In Brazil, a New Nostalgia for Military Dictatorship."

28 Glenn Greenwald "The Most Misogynistic, Hateful Elected Official in the Democratic World: Brazil's Jair Bolsonaro."

The Intercept, December 11, 2014, <https://theintercept.com/2014/12/11/misogynistic-hateful-elected-official-democratic-world->

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corporations and industries out of the ground, but they can be inefficient, expensive, fail, or become a source of corruption. Deficit spending can also be a tempting way to pump the economy quickly and win support, but if, like in Brazil, the money is not spent in a way that pays back reliably and relatively quickly governments can fall when the sources of credit loses faith in the regimes ability to repay. For any government a loss in revenue is problematic but as these two cases from Brazil show the bigger problem is not economics it is political. People lose faith in not only leaders who cause an economic crisis but often the ideology those leaders believe whether that is authoritarian dictatorship or democracy. Brazil's democracy may survive this crisis, but it may not.

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Drucker, Jeffrey. Winter Carnival: Stephanie Bourbonnais is crowned Carnival Queen outside Student Union Building, UMass Amherst, ca. February 21, 1968. Jeffrey Drucker Photograph Collection (RG 50/6 D78). Special Collections and University Archives, University of Massachusetts Amherst Libraries