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## FIRJAN's IFGF: Brazilian Municipalities Weathering Crisis with Good Fiscal Management

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Most Brazilian municipalities have been severely hit by the economic crisis and went into the red, with no money for basic investment areas including education, health, and sanitation. But some other cities are responding to the crisis by keeping high standards of public account management with low reliance on federal support.

The **Fiscal Management Index (IFGF)**, a metric created by the Federation of Rio de Janeiro Industries (FIRJAN) that looks into the finances of Brazilian municipalities based on data the local governments send to the National Treasury.

Released in 2012, the IFGF illustrates how taxes paid by society are managed by city halls administrations. The IFGF provides greater transparency to municipal accounts through a simple and available tool for public inquiry, in which every Brazilian citizen can participate in the discussion regarding the fiscal situation of his/her city. In addition, indicators are used as a management tool for thousands of municipal managers in the country, either to build scenarios or to improve decisions regarding the correct allocation of public resources. IFGF is based on five aspects: the ability to earn revenue without relying on state and federal transfers, the ratio of the budget that goes into payroll, cash sufficiency, investment capacity, and indebtedness. The indicator ranges from 0 to 1.

There are three outstanding points in the budget of the cities. On the revenue side, the problem is the reliance on intergovernmental transfers, which leaves the vast majority of municipalities with little control over their revenues. On the spending side, the challenge is the management of current expenditures (mainly staff costs), since a rigorous budget due to its exaggerated expansion may jeopardize resources destined for other purposes, especially investments. In addition, it has been identified that, depending on the total financial assets available, postponing expenses by registering them in accounts payable may jeopardize the execution of public policies. In fact, the lack of budget planning has generated liquidity problems for many Brazilian municipalities, considering the recurrent and widespread practice of using accounts payable as an alternative to indebtedness.

Based on this analysis, the five indicators that make up the IFGF were built: Own Revenue, Staff Costs, Investments, Liquidity and Cost of Debt. The first four have a 22.5 % share of the aggregated result. The Cost of Debt, in turn, has a 10 % share, considering the low level of Brazilian municipality indebtedness. This fact is reflected in the inability of most municipalities to contract debt, either due to the numerous restrictions they are subjected to, or to the lack of guarantees faced in the credit market. Finally, it is noteworthy that all indicators are in accordance with the parameters set by the Fiscal Responsibility Law - FRL (LRF). Below there is a description of each indicator:

**IFGF Own Revenue:** measures the total revenue generated by the municipality in relation to the total current net revenue - CNR (RCL). The index facilitates assessing the degree of a municipality's dependence with regard to states and Union transfers.

**IFGF Staff Costs:** represents how much municipalities spend on staff salaries, relative to the total current net revenue - CNR (RCL). Considering that this is the cost with the biggest share in the total municipality expenditure, this indicator measures the degree of budget rigidity, i.e. the municipality's room to maneuver in implementing public policies, particularly in investments.

**IFGF Liquidity:** verifies if municipalities are leaving sufficient resources to honor the accounts payable in the year, measuring the municipality's liquidity as a proportion of current net revenues. **IFGF Investments:** monitors the total investments, compared to current net revenue - CNR (RCL). Paved and well-lit streets, efficient transportation, well-equipped schools, and hospitals are examples of municipal investments able to increase workers' productivity and promote population welfare.

**IFGF Cost of Debt:** corresponds to interest and amortization expenses in relation to the total real net revenues - CNR (RLR). The index evaluates the budget share committed to the payment of interest and repayment of loans contracted in previous years.

| IFGF  |   |  |   |  |
|---|---|--|---|--|
| Own Revenue   | Staff Cost  | Liquidity  | Investments   | Cost of Debt   |
| Capacity to obtain revenue                              | Degree of rigidity of the budget                        | Sufficient cash resources  | Capacity to make investments                            | Cost of debt in the long term  |
| $\frac{\text{Own Revenue}}{\text{Current Net Revenue}}$ | $\frac{\text{Staff Costs}}{\text{Current Net Revenue}}$ | $\frac{\text{Funds to Meet Actual Obligations}}{\text{Current Net Revenue}}$ | $\frac{\text{Investments}}{\text{Current Net Revenue}}$ | $\frac{\text{Interest and Amortization}}{\text{Actual Net Revenue}}$ |
| 22.5%   | 22.5%   | 22.5%  | 22.5%   | 10.0%  |

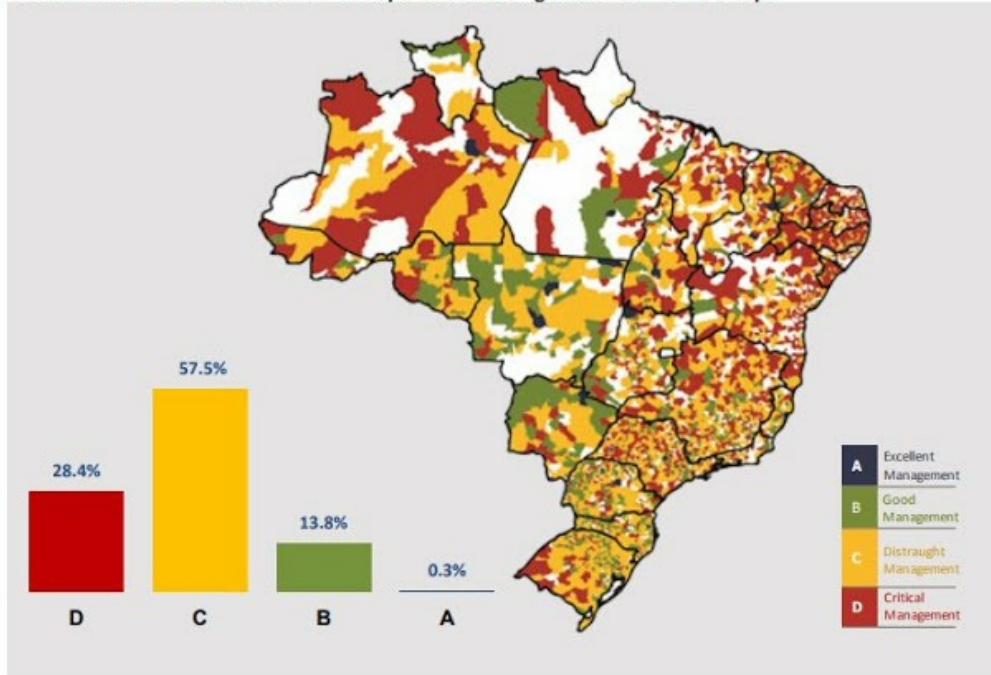
*Chart Attribute: Summary table of indicators that make up the FIRJAN Fiscal Management Index (IFGF) calculation. / Source: [FIRJAN FISCAL MANAGEMENT INDEX 2017 \(ÍNDICE FIRJAN DE GESTÃO FISCAL – IFGF 2017\)](#) Base year 2016, Report Date: August 2017*

The results are easily read either by the indicator or the whole index: scores range from 0 to 1, and the closer to 1, the better the city's fiscal management in the studied year. Four concepts were defined for the IFGF aiming to establish benchmarks to facilitate the analysis:

- Concept A (Excellent Management): Results above 0.8 points.
- Concept B (Good Management): Results between 0.6 and 0.8 points.
- Concept C (Distraught Management): Results between 0.4 and 0.6 points.
- Concept D (Critical Management): Results below 0.4 points.

Another important feature of IFGF is that its methodology enables both relative and absolute comparison, i.e., the index is not restricted to an annual image and can be compared over the years. Thus, it is possible to precisely specify if a slight rank improvement was due to the positive performance of a particular municipality or to the worse results of others. In 2017, the top ten scores went to small towns including Gavião Peixoto, a municipality in São Paulo state with a population of just over 4,000, 87% literacy rate, and a Human Development Index of 0.763. The town, which was the first-ranked, is home to a final assembly plant for EMBRAER aircraft and gets constant investment for its aerospace industry. The second-ranked São Gonçalo do Amarante, located in the Northeastern state of Ceará, benefited from the Pecém industrial and port complex.

GRAPH AND MAP 2: Distribution of municipalities according to the IFGF 2017 concept



Source: [FIRJAN FISCAL MANAGEMENT INDEX 2017 \(ÍNDICE FIRJAN DE GESTÃO FISCAL – IFGF 2017\)](#) Base year 2016, Report Date: August 2017

In Mato Grosso state, a hydropower dam project boosted earnings in Cláudia. In São Paulo state, Indaiatuba is an important economic center, home to large businesses.

Among the other cities covered by FIRJAN's index, a majority are small and medium-sized and live on tourism, including Balneário Camboriú and Bombinhas, in the Southern state of Santa Catarina, and São Sebastião and Ilhabela, in the São Paulo coast.

Only one big city was on the list: Niterói, Rio de Janeiro state. Overlooking Guanabara Bay, the city, which used to be the state capital, is one of its main financial and commercial centers. According to FIRJAN's survey, the key to Niterói's success was a careful fiscal management that allowed the city to keep a high investment level.

Among capital cities, the top five ranked were Manaus, Rio de Janeiro, Salvador, Fortaleza, and Boa Vista. In Manaus and Rio de Janeiro, investments played an important part in the results, with the 2016 Olympic Games boosting public projects in Rio. Campo Grande, Macapá, Goiânia, São Luís, and Maceió had the worst scores.

A total 14 capitals were rated as having “good” fiscal situations, 10 had “poor” ratings, and only Campo Grande had its fiscal situation rated as “critical”. None of the municipalities got “excellent” ratings.

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With reporting by Agência Brasil