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Financialization, credit rating agencies, and "policy space": The Brazilian experience

Financeirização, agências de rating *e "policy space": a experiência brasileira*

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RESUMO: O artigo examina as restrições impostas pela financeirização sobre o "policy space" doméstico, em especial de economias emergentes, à luz da atuação das agências de *rating*. A hipótese de trabalho é que essas agências, em sua interação com governos, atuam para reduzir o "policy space" a partir da posição que ocupam no sistema financeiro internacional. Nesse sentido, tanto através da atribuição de *ratings* soberanos quanto no plano discursivo, elas operam em prol da implementação de uma agenda de interesse do mercado financeiro. A metodologia do artigo consiste no estudo de caso do Brasil, com base nos *ratings* e relatórios emitidos por S&P Global, Moody's e Fitch Ratings sobre o país, que evidenciam que tais agências dispõem de um variado repertório para promover a agenda ortodoxa neoliberal no processo político e econômico nacional.
PALAVRAS-CHAVE: Financeirização; "policy space"; agências de *rating*; Brasil.

ABSTRACT: This paper analyzes the restrictions imposed by financialization on domestic policy space, especially in emerging economies, in light of the actions of credit rating agencies. The working hypothesis is that these agencies, in their interaction with governments, act to constrain the policy space from their position in the international financial system. Thereby, they operate in favor of the financial markets' agenda through the issuance of sovereign ratings and at the discursive level. The methodology draws on the case study of Brazil, based on sovereign ratings and reports issued by S&P Global, Moody's, and Fitch Ratings, which

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shows that such agencies have a vast repertoire to promote the orthodox neoliberal agenda in the national political and economic process.
KEYWORDS: Financialization; policy space; credit rating agencies; Brazil.
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1. INTRODUCTION

How does financialization constrain domestic policy space[1], especially in emerging economies? This study examines this issue in light of the actions of credit rating agencies (CRAs), which are central actors in the current financial order. Among the myriad actors and institutions that make up what is conventionally known as the "financial market", CRAs have emerged as a kind of black box. Their modus operandi has attracted interest in the academic literature due to their potential impacts on national economies and, consequently, on the fates of governments and citizens.

In particular, throughout the 21st century, studies have addressed the political bias of CRAs' behavior, which can be regarded as one of the political dimensions of the financialization process. In this context, they have shown how the policy space of governments is reduced to the detriment of alternatives to the orthodox neoliberal agenda defended by financial markets enthusiasts (Mosley, 2003; Nölke, 2020; Paula, Fritz, and Prates, 2015). This has relevant implications for national political dynamics and, more broadly, for conflicts between democracy and contemporary capitalism (Rodrik, 2012; Streeck, 2014). Amid clashes between the demands of voters and investors operating in the global financial circuit, governments ideologically unaligned to the financial markets tend to be punished by actors from the international financial system. Regarding CRAs' behavior, this has been shown in both empirical research (Barta and Johnston, 2017; Vaaler et al., 2006) and theoretical studies (Sinclair, 2005; Paudyn, 2014). This is part of a context where financial market actors increasingly influence national institutional arrangements around the world, given their ability to influence national governments to advance the financialization process (Golka and Van der Zwan, 2022).

Against this background, this study brings a detailed analysis of CRAs modus operandi. Specifically, we explore the mechanisms by which they operate to interfere with supposedly democratic national processes. Our working hypothesis is that, in their interaction with national governments, CRAs act to reduce policy space, ben-

[1] "Policy space" is defined by UNCTAD (2014, p. 45), as "the freedom and ability of a government to identify and pursue the most appropriate mix of economic and social policies to achieve equitable and sustainable development that is best suited to its particular national context. It can be defined as the combination of de jure policy sovereignty, which is the formal authority of national policymakers over policy goals and instruments, and de facto national policy control, which involves the ability of national policymakers to set priorities, influence specific targets, and weigh possible tradeoffs". Ocampo (2013), in turn, formulates the concept of "balance of payments dominance", according to which the economic dynamics of peripheral economies is more influenced by boom-bust cycles in capital flows than by traditional shocks in the terms of trade, which contributes to reduce their policy space.

efiting from their strategic role in the international financial system. In this process, through the issuance of sovereign ratings and in the discursive plane, they operate in favor of the liberal orthodox agenda defended by financial markets.

Our research methodology draws on the case study of Brazil, which explores the actions of S&P Global, Moody's, and Fitch Ratings – the three CRAs that oligopolise the rating sector – concerning the recent political and economic processes in this country. The materials we use in the analysis are the sovereign ratings and reports issued by these agencies, which we contextualize in specific moments of Brazil's national political and economic trajectory during the 21st century. The analysis draws from critical theories on the financialization process, in general, and on the modus operandi of these agencies, in particular, with a focus on the political repercussions of both.

This research thus provides two main contributions. On the one hand, it contributes to understanding the political repercussions of the financialization process based on the actions of specific actors who remain little explored in the literature, namely, the CRAs. This is achieved, in part, by analyzing the reports produced by S&P, Moody's, and Fitch – research materials that are still rarely used academically. On the other hand, our Brazilian case study helps clarify the nuances of recent political and economic processes in Brazil from the CRAs' perspectives and actions.

The paper is divided into four sections in addition to this introduction. Section 2 analyses the theoretical bases of this research, exploring what is meant by financialization and then presenting the ongoing debate on the performance of CRAs in the international financial system, with a specific focus on its political repercussions for countries that have been integrated into the global financial system. Section 3 includes our case study of Brazil. It is divided into three subsections based on the situations where the CRAs' behavior can be analyzed via our working hypothesis. Section 4, in turn, continues to develop our analysis by exploring the democratic implications of the context of financialization. The final section concludes the article.

2. RATING AGENCIES AS VECTORS OF FINANCIALIZATION

A basic premise of our argument is that the context of financialization imposes restrictions on the policy space of national governments. Financialization comprises "the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of domestic and international economies" (Epstein, 2005, p. 3). This comprehensive perspective contemplates the various faces of this phenomenon, which manifests itself differently in each country according to its historical trajectory and institutional framework evolution (Stockhammer, 2008). In all cases, however, it is a process that shifts the gravitational center of an economy from the productive sectors to the financial sectors of the society (Chesnais, 1996; Foster and Magdoff, 2009).

Financialization's origins can be traced to what is conventionally called financial globalization, i.e., "an aggregate concept that refers to [the] increasing global linkages [that are] created through cross-border financial flows" (Prasad et al., 2004,

p. 4). There is a vast body of research on the constraints that have been imposed by financial globalization on the autonomy of national governments (Strange, 1995; Rodrik, 2012; Paula et al., 2015). Typically, these are related to the prerogative of investors to move their investments globally to punish or reward governments due to their adherence to the agenda that is commonly known as "neoliberal"[2], which results from the large volume of resources that global investors normally mobilize. This scenario is particularly dramatic for emerging economies, which are monitored with greater caution by financial markets agents (Mosley, 2003) and whose policy space is subject to the vicissitudes of the international conjuncture, particularly the global financial cycle and the economic cycle of commodities, depending on the degree of specialization in a given economy (Campello, 2015).

The resulting democratic deficit is related to the political repercussions of the financialization process. In economic policy management, the orthodox agenda defended by financial markets tends to be privileged, even at the expense of citizens' demands (Palley, 2013). This more significant influence benefits from the size of the financial sector, its institutions, its network operations, and its technical complexity. The interaction between these three factors prompts shifting the delegation of decision-making power in economic policy issues towards the unelected and supposedly technical actors who drive the orthodox neoliberal agenda (Nölke, 2020). Thus, the influence acquired by the financial sector ultimately creates the political conditions that reproduce and deepen the financialization process (Pagliari and Young, 2020).

One of the dimensions of this process is analyzed by Streeck (2014) in terms of a bondholder value, which condition the governmental management of national economies. Its parallel is shareholder value, one of the dimensions of financialization that has been the most explored in academic literature. Here, business management becomes increasingly subjected to the imperative of generating value for shareholders, which directly impacts the management and activities of a company, to the detriment of its productive investments and in favor of its operations in the financial circuit. In the aggregate, as a result, the expansion of an economy as a whole is hindered.

In the case of states, as analyzed by Streeck (2014), the government's effort to protect investors' confidence negatively impacts the claims of its citizens, who have increasingly limited access to the public budget. This is due to the imperative of fiscal austerity and liberalizing economic reforms defended by state's creditors, in line with the neoliberal agenda. Ultimately, the viability of democratic governance in the context of the financialization of capitalism is put into check as

[2] This study does not address the dense debate on the conceptualization of neoliberalism, which we define following Duménil and Levy (2005): It is a mode of social organization that is designed to ensure that the interests of society's upper classes prevail, mainly through financial channels and institutions. This is supported by an ideology that praises the virtues of market self-regulation and proposes the commodification of further areas to optimize the use of economic resources. In this vein, Saad-Filho (2020) states that "the most significant feature of neoliberalism is financialization", while Palley (2013) suggests that "a simple alternative definition is that financialization corresponds to financial neoliberalism".

governments see their actions increasingly restricted by actors who are often external to their state.

Against this background, CRAs may be seen as both cause and consequence of the financialization process[3]. With the expansion and deepening of financial markets, CRAs have played a central role in the dissemination of financial calculative practices (Besedovsky, 2017), as well as in the production of structured finance, whose expansion appears as a hallmark of financialized capitalism (Sinclair, 2021). Furthermore, a relevant perception to our argument is that S&P Global, Moody's, and Fitch mediate the relationship between the states and investors operating in the global financial circuit. This happens through the issuance of sovereign ratings, which help inform investors about creditworthiness and default risk[4]. Consequently, they influence the pricing and maturities of such bonds and impact capital flows in an economy, entailing macroeconomic instability that can negatively affect real economic variables, such as GDP and employment growth (Cash, 2019).

Table 1 shows the grade scales of the three CRAs. Although each rating carries a specific meaning, the distinction between investment grade and speculative grade is of particular relevance, given that, for regulatory reasons, various investment funds are legally required to hold only the assets classified as investment grade in their portfolios (White, 2013). Thus, the loss (obtaining) of investment grade, ceteris paribus, produces an automatic outflow (inflow) of capital from a country.

Table 1: Rating scales of S&P, Moody's, and Fitch

Investment Grade		
S&P	Moody's	Fitch
AAA	Aaa	AAA
AA+	Aa1	AA+
AA	Aa2	AA
AA-	Aa3	AA-
A+	A1	A+
A	A2	A
A-	A3	A-
BBB+	Baa1	BBB+
BBB	Baa2	BBB
BBB-	Baa3	BBB-

Speculative Grade		
S&P	Moody's	Fitch
BB+	Ba1	BB+
BB	Ba2	BB
BB-	Ba3	BB-
B+	B1	B+
B	B2	B
B-	B3	B-
CCC+	Caa1	CCC-D
CCC	Caa2	-
CCC-	Caa3	-
CC	Ca	-
C	C	-
SD	-	-
D	-	-

Source: Prepared by the authors from data from the websites of S&P (2021), Moody's (2021), and Fitch (2021).

[3] Machado and Arienti (2019) analyze the process that made the CRAs protagonists in the order of financial globalization. Observing the institutional changes that permeate the rise and fall of the Bretton Woods order, the authors report the interweaving of the CRAs with the order parameters of financial globalization and financialization, seeking to understand their resilience in the international financial system, even after the financial crisis of 2008.

[4] CRAs also assess the creditworthiness of private debt securities, but this article focuses on their assessment of government bonds.

A relevant point of our argument is that the modus operandi of CRAs should not be seen as strictly technical and politically neutral, although they strive for it to be perceived as such (Sinclair, 2005; Paudyn, 2014). Indeed, the political bias of their behavior has gained prominence in the literature throughout the twenty-first century, especially following the major crises they have been involved in[5]. There are at least three ways to identify this bias.

First, it stems from the neoliberal ideological foundation that informs the variables and parameters they account for in formulating a sovereign rating. Hence, the process results in the attribution of better scores to countries with governments that adhere to the precepts of neoliberalism. Conversely, governments that adhere to a more interventionist and redistributive agenda tend to be punished with lower scores. This produces imbalances in the national political dynamics, as countries are ultimately harmed or benefited due to their government's degree of ideological convergence with the CRAs (Paudyn, 2014).

Second, in addition to the ideology underlying their ratings, quantitative research has shown that CRAs tend to discriminate against countries based on the partisan ideology of their governments. Thus, those ruled by the left-wing (right-wing) parties may receive worse (better) ratings, regardless of the results of the economic policy they have adopted (Barta and Johnston, 2017; Vaaler et al., 2006). This behavior is more prominent in electoral cycles, when the rating can be regarded as a voting instrument of the CRAs to show the candidate of their preference (Vaaler et al., 2005). Moreover, it also functions as an indicator of government performance to the public opinion, which makes left-wing parties to be seen as less competent in economic management (Buenfil, 2017; Paudyn, 2014).

Third, CRAs can also be seen as financial markets' echo chambers in their interaction with national governments. This is because their role in the context of financialization enables the diffusion of the norms, practices, and institutions that are necessary for the expansion and operation of capital markets. Such interpretation is supported by the theory of Sinclair (2005) on the modus operandi of S&P, Moody's, and Fitch.

To understand it, it is necessary to identify the three forms of power exercised by the CRAs. The first one is the classic form of relational power, which is perceived when an actor behaves differently from what he would without any constraints. In the interaction between CRAs and governments, this can be observed when a rating action[6] is conditioned to the implementation of some specific measure, thereby putting pressure on the government to implement it. The second form of power observed by Sinclair (2005) is the structural power of CRAs. This is shown when

[5] For example, the agencies were closely involved in the East Asian financial crisis (1997), the Enron crisis (2001) and the subprime crisis (2007-2008). On the subject, see Sinclair (2005) and Guttmann (2016).

[6] "Rating action" is the technical term agencies use to refer to changes in a rating (downgrade or upgrade) or changes in a rating's outlook (positive, negative, stable).

governments anticipate the latent threat of their relational power and adhere in advance to the policies and/or measures propagated by them to avoid any sanction on the sovereign rating. Finally, and more importantly for this study, the third form of power arises from the epistemic authority of the CRAs in financial markets, given their crucial role in assessing creditworthiness.

Such an understanding reflects the origins of S&P, Moody's, and Fitch as companies. At the beginning of the twentieth century, all three were created to meet the demands of the then-incipient capital market of the United States. In this environment, investors perceived them to be embedded knowledge networks, which have made their actions constitute social facts[7]. Amid financial globalization and the consequent projection of American financial rules, practices, and institutions worldwide, the CRAs began to operate globally. Hence, today, national governments have to relate to a financial structure that overlaps with that of states and is partially governed by CRAs' epistemic authority.

From this situation, Sinclair (2005) extracts two observations that are relevant to this study. First, governments that are ideologically misaligned with the CRAs are ultimately pressured to incorporate the rating actions and information from published reports into their economic policy decisions because they know that the financial agents will do so. Accordingly, this interaction reveals another function of the CRAs in financial globalization: to shape the institutional context where the global expansion of capital markets occurs, thereby propagating the necessary policies for this purpose – that is, the neoliberal ones. That is, they act to homogenize the institutional frameworks of countries that are integrated into financial globalization by suiting the demands of the financialization process.

In light of the discussion thus far, the CRAs' role as vectors of financialization becomes evident. On the one hand, they are diffusers of the agenda that drives this process. On the other hand, they are one of its expressions since, in line with Epstein's (2005) broad definition, they are companies that offer financial services, were forged from the demands of the financial market, and operate in favor of the organization and expansion of capital markets. In addition, they illustrate the technical complexity and network organization with which financial markets work, pressuring for the withdrawal of economic management from political debate.

Having clarified the central elements around CRAs' modus operandi, our working hypothesis acquires greater significance. It is thus necessary to identify the mechanisms through which S&P, Moody's, and Fitch can constrain the policy space of national governments. Two instruments serve this purpose. First, the sovereign ratings, once they influence national political and economic dynamics through their impacts on the capacity of state financing, capital flows, and the public perception of the government's competence. Second, the discursive manifestations of CRAs (their reports

[7] This follows Durkheim's (1982, p. 52) definition of social facts: "they consist of manners of acting, thinking and feeling external to the individual, which are invested with a coercive power by virtue of which they exercise control over him".

and press releases), where they make explicit demands and criticisms to national political and economic management, thereby acting as a channel for both pressuring the government and interfering in national political and economic processes.

3. THE BRAZILIAN EXPERIENCE WITH RATING AGENCIES

This section provides the case study of Brazil to illustrate how CRAs operate to constrain the policy space of governments, especially in emerging economies, to the benefit of the financial market's agenda. The case of Brazil is convenient for two reasons. On the one hand, it is a country with an emerging economy in the context of financial globalization, i.e., in a position of vulnerability regarding global financial dynamics. This resulted from the liberalization of its capital and financial markets that took place during the 1990s and 2000s when the country reached a situation of de facto convertibility of its capital and financial account (Paula, 2011). On the other hand, after integrating into financial globalization, Brazil experienced transitions from governments with different partisan ideologies, which facilitates our observation of political bias in the CRAs modus operandi.

Despite the changes in the orientation of economic policies in the periods analyzed here, a critical background must be highlighted to understand the economy's behavior in periods of turbulence analyzed here. As Biancarelli (2009) points out, some features of external vulnerability have changed in Brazil since 2004 due to both the accumulation of foreign exchange reserves and a deliberate process of external deleveraging of the public sector – even though new sources of vulnerability emerged, particularly in the 2010s with the increased participation of foreign investors in the domestic securities market (stocks and debt securities). In this context, according to Paula and Pires (2017, p. 127), "at the same time, the Treasury restructured the public external debt, and the Central Bank accumulated reserves"[8], guaranteeing the government more significant "policy space" for the adoption of countercyclical policies. This saved the government from having to face a crisis in the balance of payments even at critical times, as in the case of the reversal of the international scenario from 2014 onwards (fall in commodity prices and greater instability in the global liquidity cycle) and the deepening of the economic crisis in Brazil in 2015. But that did not stop the CRAs from acting to restrict government actions in favor of the orthodox agenda.

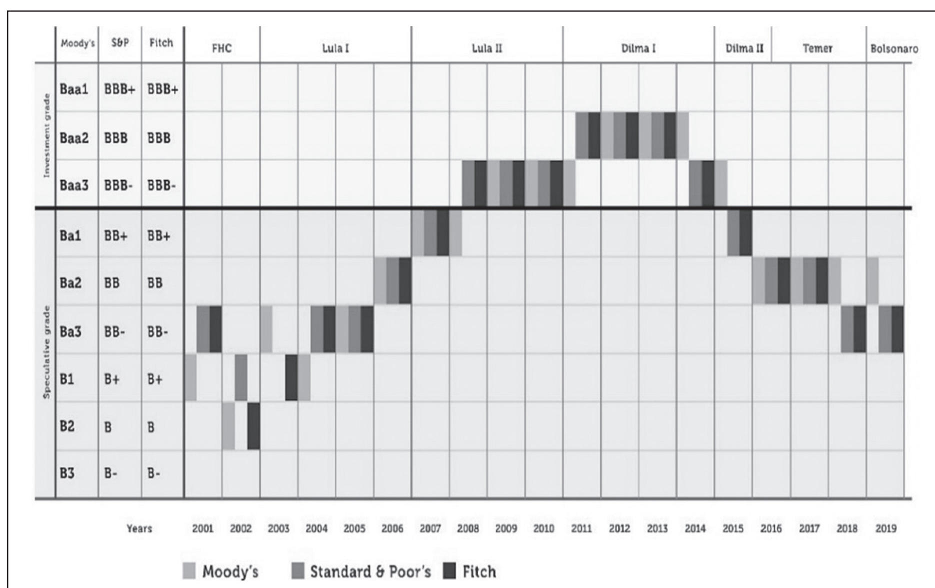
Hence, we focus on three particular moments in the country's interaction with the CRAs. The first is the victory of Lula da Silva, from the Workers' Party (PT), in the presidential elections of 2002. The second is the period between the re-election and impeachment of Dilma Rousseff (2014-2016), also from the PT, in a turbulent moment of the Brazilian political process. Third, we discuss the government of

[8] As Paula and Pires (2017, p. 127) record, the federal government went from a net debtor position of US$ 57.8 billion at the end of 2002 to a net creditor position of US$ 95.9 billion at the end of 2007.

Michel Temer (2017-2018), during which the 2018 presidential election resulted in Jair Bolsonaro's victory.

We decided to exclude the period from 2003 to 2013 from our analysis due to the exceptional international context that was then in force, which reduced the financial market's ability to restrict the Brazilian government's policy space (Campello, 2015). In this period, the combined super cycle of commodities and capital inflows and the well succeeded economic policy enabled the strengthening of the metrics evaluated by the CRAs, which translated into the achievement of the investment grade by Brazilian ratings. Figure 1 shows its trajectory from 2001 to 2019, which constitutes the background of the events we present in the following subsections.

Figure 1: The sovereign ratings of Brazil (2001-2019)



Source: Prepared by the authors via information from the Trading Economics Database (2021).

3.1 Lula's first election (2002)

The 2002 presidential election illustrates how the CRAs use their instruments of intervention to defend the orthodox neoliberal agenda in national political processes. Faced with the imminent victory of a left-wing candidate, Lula da Silva, Brazil was experiencing a crisis of confidence concerning the financial market in a context marked by capital flight, exchange devaluation, and inflationary escalation (Saad-Filho and Morais, 2018). This crisis of confidence, which led the Central Bank of Brazil to raise the Selic rate to 25.0% p.a. in December 2022 (against 15,25% in March 2001), was expressed both in an intense exchange devaluation in 2002 (52.3% p.a.) and in an increase in the domestic public debt, which reached 60% of GDP in December 2021 (against 51,5% in December 2001), and was ac-

companied by a shortening of public bonds' maturities (average maturity fell from 32.2 months in 2001 to 13.6 months in 2022) and a substantial worsening in the federal securities debt profile (60.8% of the total debt indexed to the Selic rate and 22.4% to the exchange rate) (Macahyba, 2021; see also Table 2, in the Appendix). In this scenario, the CRAs acted to constrain the economic agenda of the likely Lula da Silva government.

Between June and October 2002, the Brazilian rating was downgraded four times. Fitch promoted two downgrades, moving it from BB- to B. S&P reduced its rating from BB- to B+, and Moody's reduced its rating from B1 to B2. The justifications for these generally pointed to the risk of a PT victory, which would break from a more market-friendly orthodox economic agenda. In a report published on June 19, for example, Fitch (2002a) explains that "the truth is that, as in 1989, 1994 and 1998, the PT leader is still viewed as a fundamental political risk by the markets, and this can have an important effect on voter behavior". In turn, S&P (2002a), in August, expressed its concerns with the possible abandonment of the neoliberal agenda:

> [...] all the main candidates wish to distinguish themselves from aspects of Cardoso's record, and future policy could be somewhat less "neoliberal". All the presidential candidates are less ideologically committed to privatization, against which there is a general backlash across Latin America in the wake of the Argentine crisis.

Accordingly, following the first round of elections, S&P stated that "Standard & Poor's will be looking for immediate signals from the president-elect with regard to intended macroeconomic policies" (S&P, 2002b). In the same vein, Fitch (2002b), on the eve of the election's second round on October 25, published a new report entitled "All eyes on Lula". In this document, the CRA conditioned the recovery of the Brazilian rating to the appointment of an economic team with credibility in the financial market.

In this context, the PT signaled its accommodation with the demands of the financial market's actors, committing itself to maintain the neoliberal economic policy guidelines that had been implemented by Fernando Henrique Cardoso's (FHC) government. During this process, Lula da Silva signed the "Letter to the Brazilian People", where he committed to respecting the contracts signed by the previous government and the neoliberal institutional framework that had been established during the 1990s (Saad-Filho and Morais, 2018). Meanwhile, the FHC government criticized the CRAs' actions, pointing out their political bias against the PT, to the detriment of the national macroeconomic stability (Agência Brasil, 2002).

Lula da Silva's government began in 2003 by praising FHC's economic policy, choosing a team of orthodox economists to participate in the Ministry of Finance. Under the new Minister Antonio Palocci, the government not only met but increased the primary fiscal surplus target from 3.75% of GDP to 4.5%. As the international economic situation was favorable to Brazil during Lula's first mandate, due to the commodities boom, it was possible to meet the new fiscal target with an increase in both public expenditures and tax revenues – to the benefit of the sovereign ratings to be achieved (Agência Brasil, 2002):

> The Ministry of Finance and the Central Bank of Brazil regret the decision taken by the credit rating agency Fitch to downgrade Brazil's sovereign rating. The decision is extemporaneous and mistaken – extemporaneous due to a preconceived vision of the future design of economic policy; mistaken because it is based on deficient analytical content. The backdrop to Fitch's argument is the political transition in Brazil. It is based, therefore, on what the next government may or may not do.

3.2 The re-election and impeachment of Dilma Rousseff (2014-2016)

After more than a decade of pacification in Brazil's interaction with financial markets' actors, in which PT governments reconciled orthodox macroeconomic policies with their social agenda, the tension reappeared in the second half of Dilma's first term (Carvalho, 2018). Between 2014 and 2016, the CRAs used all the instruments at their disposal to restrict the government's policy space, protecting the interests of the financial sectors (Machado and Arienti, 2020). Three different stages of this modus operandi can be observed.

The first includes the electoral context that resulted in the re-election of Dilma Rousseff. In 2014, the Brazilian rating was downgraded for the first time since 2002, entering a downward trajectory. According to S&P (2014a), the downgrade to BBB- was due to the fiscal deterioration then taking place without any prospect of correction in the electoral context. Shortly after, the CRA declared itself favorable to two opposition candidates in the presidential race, Aecio Neves and Eduardo Campos (S&P, 2014b):

> We believe that the profile of the policies of a second term for Dilma would be similar to her current administration, in which the President would continue to supervise the political decisions. Although we expect certain changes in the team and economic policies, in general, we estimate "more of the same" in terms of the unequal policy. We believe that a government of Aecio or Campos could seek a more consistent and market-oriented economic policy with a more significant initial direction for the confidence of domestic and international investors.

The second stage comprised the critical context that was established during the second term of President Rousseff and lasted until the beginning of her impeachment process. During this period, S&P, Moody's, and Fitch acted to constrain the implementation of economic policy to keep it aligned with the orthodox agenda. Accordingly, they promoted three downgrades of the Brazilian rating[9], which resulted in the loss of the investment grade, associated with a discourse filled with criticisms of Brazil's economic management. When justifying the downgrade to

[9] In addition to the mentioned motivation, these downgrades incorporated the effective reduction in the variables evaluated by the agencies in their rating formulation process.

Baa3, for instance, Moody's (2015) noted that "there is a lack of political consensus in Brazil on the possibility of more aggressively addressing budgetary rigidity, [of] promoting reforms that address the increase in mandatory spending". In turn, S&P (2015), when downgrading the rating to BB+, criticized revisions in the country's primary surplus targets, which suggested "a reduction in the fiscal policy conviction in the President's office".

The return to the speculative level had significant repercussions in the political scenario and among the leading Brazilian newspapers, giving rise to government reactions. On September 23, 2015, for example, *Folha de S.Paulo* (2015a) reported that, in response to S&P's loss of investment grade, the government was trying to approve a package of fiscal measures to "calm down the CRAs and avoid a further downgrading of the country's investment grade". Meanwhile, former president Lula downplayed the event, claiming that "it doesn't mean anything. It just means that we can't do what they want. We have to do what we want" (Infomoney, 2015). On the other hand, senator Aécio Neves, who had been Dilma's main opponent in the 2014 elections, declared that "unfortunately, the loss of Brazil's investment grade and the prospect of a negative review over the next twelve months show that President Dilma's government is over" (*Exame*, 2015).

In this context, as the economic crisis progressed and distributive conflicts worsened[10], the CRAs' interventions in the political process became more evident. For example, S&P, Moody's, and Fitch intensely lobbied the government to recreate the CPMF[11], claiming that the lack of this tax created a "scenario [that was] very bad" for the country's creditworthiness (Folha, 2015b). However, it is worth noting that Brazil had a level of foreign exchange reserves in this period that was ten times higher than in 2002, and its external vulnerability indicators were at satisfactory levels (Table 2, in the Appendix).

The tension escalated when, after downgrading Brazilian rating to BBB-, Fitch declared that a new downgrade would occur if newly appointed Minister of Finance Joaquim Levy (a well-known orthodox-neoliberal economist who had pledged to implement a fiscal austerity agenda amid a strong economic recession) were dismissed (Valor, 2015). At that point, it was clear that his economic policy was not delivering the expected results[12], but Levy's ideological convergence with the CRAs provided him with this unconditional defense.

The Minister of Finance, however, was dismissed during the third stage of the

[10] The real GDP growth rate dropped from 3.8% p.a. on average from 2004-2013 to 0.5% p.a. in 2014 and -3.0% on average in 2015-2016; the consumer price index (IPCA) increased from 5.9% in 2013 to 10.7% in 2015; and the unemployment rate increased from 6.6 % in December 2014 to 12.2% in December 2016 (IPEADATA, 2022 and Table 2, in the Appendix).

[11] The Provisional Contribution on Financial Transactions (CPMF) was a tax that levied on all bank transactions – except for stock trading on the Stock Exchange, withdrawals from pensions, unemployment insurance, wages and transfers between current accounts of the same ownership – and had been in force in Brazil for 11 years, from 1996 to 2007.

[12] As Table 1 in the annex shows, the fiscal primary result (% of GDP) increased to -1.9% in 2015 against -0.6% in 2014, while the real GDP growth rate was -3.15% p.a.

interaction between the CRAs and the Rousseff government, which comprehends her impeachment process (from December 2015 to August 2016). Notably, the choice of Nelson Barbosa, with a more heterodox profile, to replace Levy in December 2015 was criticized by the CRAs. In a report published in December, Fitch (2015a), for example, declared that "the appointment of Barbosa likely signals compromises by the Rousseff administration on its fiscal agenda and [its shift] from severe austerity measures, given the minister's prior support of expansionary fiscal measures".

CRAs' constraints on the policy space would soon translate into the sovereign ratings' trajectory. Throughout the impeachment process, the Brazilian ratings were downgraded four times, sinking into the speculative grade and exacerbating the experienced economic recession[13]. Meanwhile, the CRAs showed sympathy for the neoliberal agenda proposed by Vice-President Michel Temer. In May 2016, for instance, when the Chamber of Deputies agreed to proceed with the process, and the president was removed from office, S&P (2016a) stated the following:

> The new interim government should benefit from an initial vote of confidence from the private sector, given the strength of the economic team, which includes an ex-president of the Central Bank, Henrique Meirelles, as Minister of Finance, and an ex-director of the Central Bank, Ilan Goldfajn, as the president of the Central Bank, in addition to the political signal already sent by Vice-President Temer.

The political bias of CRAs' modus operandi – as well as the controversies that circumscribed the process that resulted in Rousseff's destitution – allows the speculation on their interest in consciously contributing to the rise of a government that was committed to the orthodox agenda. In this vein, Temer promoted an economic policy marked by liberalizing reforms, e.g., labor reform, and by institutionalizing fiscal austerity through, e.g., Constitutional Amendment 95[14]. This would earn him frequent praise in the reports released by S&P, Moody's, and Fitch, as discussed below.

3.3 The Temer government and the victory of Bolsonaro (2017-2018)

The effects of the ideological convergence between the Temer government and the CRAs soon became evident. Immediately after the impeachment, S&P (2016b) answered "Frequently asked questions: Challenges of Brazil after the impeachment

[13] The CRAs' justifications for this always combined elements of the economic crisis with the political instability experienced by the country. Fitch (2015b), for example, promoted a downgrade stating that "Brazil's downgrade reflects the economy's recession deeper than previously anticipated, continued adverse fiscal developments and the increased political uncertainty that could further undermine the government's capacity to effectively implement fiscal measures to stabilize the growing debt burden".

[14] Constitutional Amendment 95 (Dec. 15, 2016) froze primary public expenditures in real terms for 20 years (not including debt interest payments); that is, they are readjusted by the expenditures made in the previous year, corrected for inflation rate (Oreiro and Paula, 2021, chap. 4).

of Dilma Rousseff". This report recalled that an essential difference between Temer and Dilma administrations was "that Temer's economic team benefits from greater credibility in the financial markets, which gives it some time to maneuver". Moreover, in the context of the approval of the EC-95, S&P analyst Lisa Schineller stated that "the initial approval of a limit of public spending is a step in the right direction, but it will still take years, and other difficult reforms will be necessary for Brazil to recover the investment grade" (Folha, 2016). Furthermore, the CRAs praised some of the government's economic measures. For instance, in August 2017, S&P (2017) declared that:

> The solid economic team of Brazil, which includes representatives of banks and public sector companies, gains more broadly the respect of the Executive, the Parliament, and the private sector. The Federal Court of Accounts (TCU) and the Ministry of Finance work together to strengthen the transparency of fiscal accounts. The government has articulated a comprehensive macro and microeconomic agenda, aiming to generate conditions for stronger growth and fiscal performance in the coming years. Congress has already approved part of the agenda: a constitutional ceiling for spending, two phases of the labor reform, the migration law, the reopening of the oil and gas sector with fewer local rules, and a fiscal recovery regime for the highly indebted, [and] without resources, [is] willing to carry out expenditure reform.

However, the CRA's interferences in the political process continued to occur. Two events during the Temer administration exemplify this. First, their explicit demand for a pension reform. Second, their behavior during the 2018 electoral race. These two situations show how the instruments available to S&P, Moody's, and Fitch – ratings, reports, and press releases – were articulated to promote financial markets' interests.

Throughout 2017, the CRAs linked the stability of the Brazilian rating directly to implementing a pension reform. In a report published in August, for example, S&P (2017) stated that "a failure to advance the Social Security Reform would be consistent with a limitation of the ability of the Brazilian political class to approve policies that support economic prosperity and sustainable fiscal policies". In October, Joydeep Mukherji, an S&P analyst, was more direct: "if the government fails to approve the pension reform, or if it indicates that it is trying to buy time to negotiate the changes, Brazil's credit rating may suffer a new downgrade".

This threat became a reality at the beginning of 2018. In January 2018, S&P (2018) downgraded the Brazilian rating to BB-, based on the delay in promoting the reform[15]. In February, when the Temer government decided to close this issue,

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[15] The team of the Minister of Finance, Henrique Meirelles, prepared a pension reform proposal that was sent for discussion and approval in the National Congress. However, its approval became politically unfeasible due to the disclosure of a recording of a private conversation between President Temer and one of the owners of the JBS company, Joesley Batista. Temer was accused by the businessman of

Fitch also reacted by downgrading the sovereign rating to BB. In the report where the action was explained, the CRA made clear its frustration with the non-implementation of the reform (Folha, 2018a).

In the second half of 2018, the CRAs' actions were guided by the electoral race to replace Temer in the presidency. In September, for instance, on the eve of the election, Fitch analyst Todd Martinez declared to Folha (2018b) that "the result of the October elections may cause the market to lose patience with Brazil and decide to allocate its resources elsewhere, given the more remote possibility that the elected government can – or will want to – pass fiscal adjustment in the country". In the same month, Fitch (2018) released a report that projected two possible scenarios for Brazil. According to the CRA, if Jair Bolsonaro, the preferred candidate in the financial markets, emerged victorious, then:

> Brazilian financial markets would likely rally, because Bolsonaro has appointed investor-friendly advisors and pledged support for pension reform and privatization. Market participants also appear to believe that the leftist candidates represent a threat to fiscal stability and growth and would likely show relief in the reduction of uncertainty. With confidence growing, economic activity growth would broadly pick up heading into 2019.

On the other hand, if the PT candidate Fernando Haddad became president, the prognosis was much bleaker:

> Financial markets would likely sell off significantly in light of the leftist candidate's campaign pledge to undo key reforms pursued over the last two years. The real [Brazilian currency] would likely hit historic lows, bond yields would spike, and equities would decline sharply. The sudden drop in financial markets and business sentiment would likely push the economy back into recession, heading into 2019.

As in the 2002 electoral race, therefore, the CRAs acted to constrain the ideologically divergent candidate in the presidential race. In this case, however, using downgrades to price the voters' choice was unnecessary. In line with the expectations of the electoral context, Jair Bolsonaro – a far-right candidate and, until then, federal deputy of little renown – was elected president with the promise of continuing to advance the orthodox neoliberal agenda.

4. RATING AGENCIES, POLICY SPACE, AND DEMOCRACY

The CRAs' actions towards the Brazilian political process offer a fresh perspective for observing the constraints of financialization on the domestic policy space.

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encouraging the payment of R$ 500,000 to former federal deputy Eduardo Cunha so that he would not reveal information on the "car wash" operation.

As we have shown, these restrictions result from the particularities of the CRAs as actors capable of operationalizing such constraints. By mediating states' access to the financial resources available in the sovereign debt markets, S&P, Moody's, and Fitch have a privileged repertoire of tools for promoting investors' agenda. Thus, based on the experience of Brazil, what lessons can be derived from the clash between financialization and supposedly democratic processes?

First, in the previous section, we demonstrated how CRAs act to influence electoral processes through the issuance of both sovereign ratings and reports concerning a country's political and economic context. Confirming the quantitative research presented in Section 2, our analysis showed that left-wing candidates are systematically disadvantaged. This became evident in the three presidential elections and the impeachment process of President Rousseff: in 2002, the CRAs promoted downgrades justified by the supposed threat that Lula da Silva's victory would represent to the interests of the financial market; in the 2014 election, it was clear their support for right-wing candidates, whose agenda converged with that of investors; in the context of the presidential impeachment in 2016, numerous downgrades were added to reports and press releases that constrained the economic policy, which composed the crisis scenario that led to Rousseff's destitution; finally, in the 2018 presidential race, the support for the candidacy of Jair Bolsonaro was revealed in the projections of extreme scenarios for the country. In this case, it cannot be ignored that the optimistic economic scenario projected in the event of Bolsonaro's victory was never close to materializing throughout his first term, as the economy remained semi-stagnant and with high unemployment rates.

This pattern of behavior exemplifies the subjection of national political dynamics to the interference of actors from the international financial system. Since they often promote the orthodox neoliberal agenda, this helps to explain the prominence it has acquired in the national political arena. On the other hand, it underscores one of the mechanisms for the materialization of the democratic deficit that is inherent to the context of financialization.

Second, the oversizing of the financial markets' agenda stems from CRAs' constant participation in the country's political and economic debate. This way of operating goes beyond lobbying, insofar as the sovereign rating is often conditioned to government decisions – which reveals the conscious use by the CRAs of the forms of power they have to punish or reward the government. In the case study of Brazil, this was evidenced (i) in the bargain built around the CPFM, (ii) in their attempt to maintain Joaquim Levy as Dilma Rousseff's Minister of Finance, and (iii) in their pressure for the pension reform in the Temer Government – among a range of other occasions that were not contemplated by our analysis. In this sense, it is worth noting that, between 2003 and 2012, the PT governments chose to maintain the orthodox macroeconomic structure established at the end of the 1990s (Prates et al., 2020) while actively pursuing the investment-grade (Ywata, 2012). This suggests that they were aware of CRAs' epistemic authority, which gave them the desired goal, as shown in Figure 1.

Third, spanning both electoral cycles and political and economic processes more broadly, it is necessary to speculate on the effects of rating actions and CRAs' discourse on public opinion about the competence of governments. Although this

is difficult to measure, right-wing governments were systematically presented as more competent in economic management due to their ideological convergence with the CRAs. Another dimension of the financialization process enhances this effect: in this context, citizens are often also investors, as they may hold financial assets in investment portfolios (Streeck, 2014). This alone would make them more likely to factor in the CRAs' epistemic authority in their assessment of governments.

Fourth, it should be considered that, despite the analyzed political bias, changes in Brazil's ratings also resulted from the improvement or worsening of metrics taken into account by the CRAs in their evaluation of the national creditworthiness. Hence, they reflected the observation of objective variables, such as the trajectory and composition of public debt in relation to GDP, economic growth, inflation, and external vulnerability – in addition to subjective factors, such as "political risk", which lacks definition in the CRAs' documents on the methodology for the sovereign rating. As discussed in Section 2, the problem is that the parameters that guide this assessment are ideologically informed by neoliberal tenets, while the rating formulation process lacks transparency. This adds to the solid political component presented in the CRAs reports where rating actions are explained, which intensifies the controversies surrounding the issued sovereign ratings.

Finally, although this study focuses on the case of Brazil, possible generalizations of its conclusions cannot be ruled out. Since countries integrated into financial globalization are subject to CRAs' actions, their constraints become inevitable – even though they tend to be expressed differently, depending on national peculiarities[16]. This means that their political and economic processes are, to some extent, conditioned by the portrayed modus operandi of S&P, Moody's, and Fitch, to the benefit of the financialization process and the detriment of the policy space of their respective governments, especially in emerging economies.

5. CONCLUDING REMARKS

This study has examined how financialization constrains national policy space in light of the CRAs' actions. Based on the case study of Brazil, we have observed that S&P, Moody's, and Fitch use a varied repertoire to promote the liberal orthodox agenda demanded by financial markets. This contributes to its prominence in national political and economic processes, one of the dimensions of financialization explored in academic literature.

The democratic deficit resulting from the interaction between CRAs and governments fits into the conflict between democracy and contemporary financialized capitalism. As we have shown, CRAs are external actors to the state who actively tries to influence the choice of its government and the agenda implemented by it.

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[16] It should be noted that the CRAs take into account, in their assessments, purely economic variables (such as the level and nature of external debt and the degree of public debt, among other factors), which condition a country's vulnerability to their actions.

Hence, clarifying their modus operandi, especially understanding their political character, is a condition for improving national democratic governance. As it is unlikely that CRAs will change how they interact with the political and economic processes of countries, identifying them as one among several political actors that aim to constrain the policy space in line with their interests, to the benefit of specific social groups, is therefore a feasible goal.

Furthermore, our findings open other promising paths to advance the research agenda on how financialization restricts governments' autonomy. Once the CRAs are only one among several mechanisms operating in this direction, understanding other actors and institutions that constrain the policy space for the benefit of the financial market agenda turns out to be a critical research path. Alternatively, there are other methods to examine the CRAs themselves, whether by expanding the number of cases or situations analyzed or by adopting different methodologies for this purpose. Indeed, today, CRAs should be viewed as black boxes of the international financial system, whose opening will gradually reveal the nuances of their modus operandi and its impacts on national democracy. We hope, with this study, that some of these have been clarified.

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APPENDIX

Table 2: Some macroeconomic indicators, Brazil - 2002-2018

Indicators	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Real GDP growth (%)	3,58	1,23	5,66	3,01	3,69	5,80	4,68	-0,10	6,98	3,74	1,61	2,88	0,46	-3,15	-2,90	1,25	1,76
IPCA (%)	12,5	9,3	7,6	5,7	3,1	4,5	5,9	4,3	5,9	6,5	5,8	5,9	6,4	10,7	6,3	2,9	3.8
Selic rate[1] (%)	25,0	16,5	17,7	18,0	13,2	11,2	13,7	8,7	10,7	10,9	7,1	9,9	11,7	14,2	13,7	6,9	6,5
Foreign exchange reserves (US$ bi)	37.823	49.296	52.935	53.799	85.839	180.334	193.783	238.520	288.575	352.012	373.147	358.808	363.551	356.464	365.016	373.972	374.715
Reserves/gross external debt (%)	18,0	22,9	26,3	31,7	49,7	93,3	104,3	120,6	112,4	113,7	115,5	120,2	106,0	110,2	114,1	120,4	n.a.
Gross external debt/GDP (%)	41,8	38,8	30,3	19,2	15,9	14,1	12,0	12,2	12,0	11,8	13,3	12,7	14,4	18,6	18,2	15,4	17,2
Domestic public debt (% GDP)	59,9	54,3	50,2	47,9	46,5	44,6	37,6	40,9	38,0	34,5	32,2	30,5	32,6	35,4	46,1	51,4	52,8
(%) Selic-linked[2]	60,8	61,4	57,1	51,8	37,8	33,4	35,8	35,8	32,5	30,8	22,2	19,5	19,2	23,6	29,1	32,4	36,8
(%) Reference rate[2]	2,1	1,8	2,7	2,1	2,2	2,1	1,6	1,2	0,8	0,8	0,6	0,5	0,5	0,4	0,4	0,3	0,2
(%) FX-linked[2]	22,4	10,8	5,2	2,7	1,3	1,0	1,1	0,7	0,6	0,6	0,6	0,6	0,6	0,7	0,5	0,4	0,5
(%) Fixed-rate[2]	2,2	12,5	20,1	27,9	36,1	37,3	32,2	33,7	37,9	38,3	41,2	43,3	43,1	41,0	36,9	36,3	34,1
(%) Inflation-linked[2]	12,5	13,5	14,9	15,5	22,5	26,3	29,3	28,6	28,1	29,6	35,5	36,2	36,7	34,3	33,2	30,6	28,6
Primary fiscal balance (% GDP)	3,2	3,2	3,7	3,7	3,2	3,2	3,3	1,9	2,6	2,9	2,2	1,7	-0,6	-1,9	-2,5	-1,7	1,6

Source: BCB (2022) and IPEADATA (2022).
(1) The Selic interest rate is the monetary policy interest rate, i.e, the key tool used by the Banco Central do Brasil (BCB) in the implementation of the monetary policy.
(2) As percentage of the total public debt.