Brazil-U.S. Business Council

Brazil Bulletin

Interview: Planning Minister Nelson Barbosa

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Brazil's government will push forward with a much needed fiscal adjustment despite political pressure for more spending and popular resistance against tax increases, Planning Minister Nelson Barbosa said last week. Barbosa spoke with investors and reporters at a meeting in São Paulo. He expressed confidence in the government's 2015 primary surplus goal of 1.2% of GDP and noted that additional tax hikes were unlikely. His overall tone was sober but optimistic. He did not back away when asked whether 2015 was going to be "a tough year." Excerpts follow:

- **On the need for a fiscal adjustment:** "The fiscal adjustment represents a permanent change in focus. The purpose is to boost the primary budget surplus over a period of years. Our plan of action is based on a series of measures subject to periodic revision. The most important objective is to reach the primary surplus target for 2015, a year which promises to be unusually difficult. We are making an effort to correct what has to be corrected."

- **On fiscal policy and spending:** "Our intention is to produce a primary budget surplus equal to 1.2% of GDP, a goal which will require the cooperation of all spheres of government. Within that strategy, the government has given priority to cutting expenditure. It's a question of day-to-day management of government spending."

- **On fiscal policy and taxes:** "At the present time, there is no intention of adopting additional tax measures in order to meet the fiscal target. The adjustment favors spending cuts over tax increases."

- **On other aspects of fiscal adjustment policy:** "The fiscal plan has various aspects, including the relationship between the Treasury and the BNDES (the government has announced an end to Treasury loans to the National Development Bank). Another is symbolized by Executive Orders 664 and 665 (reducing certain welfare benefits), which will have the effect of permanently reducing government expenditure by the equivalent of 0.3% of GDP. These new rules, I would add, help create a welfare system that is more fair and balanced, in line with best international practices."

- **On congressional resistance to fiscal changes:** "Congress is sovereign and will render its verdict in due time. Occasionally, tempers flare but Brazil always ends up moving forward."

- **On inflation:** "Reducing and controlling inflation is among the government's top priorities. There will be a temporary rise in inflation now, but then a significant reduction in 2016."

- **On the Brazilian economy:** "The Brazilian economy typically stages a rapid recovery from crises. Normally, it's back on track after six to nine months."

- **On sales of government assets:** “There could be eventual sales of government assets over the next few years. We could sell shares or even privatize but not this year. For one thing, market conditions are not favorable.”

Top News of the Week

Opposition protests dwarf pro-government rallies in big cities. It was a week of “dueling protests” in Brazil, with opposition groups coming out the clear winner. Pro-government unions and students staged rallies and marches in 24 cities on Friday. Police reports estimated total participation at less than 100,000. It was the opposition’s turn on Sunday, with police reports from all 27 states estimating cumulative turnout at about 1.7 million. More than half of that total was concentrated in the city of São Paulo. There were few reports of violence, although police in São Paulo reported 20 arrests of possible Black Block vandals. Sunday’s demonstrations focused on criticism of President Dilma Rousseff, with only scattered banners and slogans demanding impeachment. Opposition political parties were largely absent, with little speech-making and few formal demands being voiced. The main opposition candidate from the 2014 election, Social Democrat Aécio Neves, issued a brief statement supporting the protests but he did not make a personal appearance. Speaking for the government, Justice Minister José Eduardo Cardozo called Sunday’s protests “democratic and legitimate.” He said the Rousseff administration was “open to a dialog with opposition parties and other segments of society.” He closed by saying the administration will press ahead with a political reform agenda that would put public finance of campaigns at the forefront as a way to reduce corruption in the political system.

Petrobras witness alleges massive illegal fund raising by political parties. Brazil’s ruling PT (Partido dos Trabalhadores) obtained off-the-books campaign funds amounting to between $150 million and $200 million during the decade beginning in 2004, according to former Petrobras executive Pedro Barusco. The money was skimmed from contracts signed by state-run energy company Petrobras, Barusco told a congressional investigative committee last week. He said other parties allied with the PT also obtained illegal funds through the same practice. Top PT officials, including Treasurer João Vaccari, immediately denied the charges. Meanwhile, federal prosecutors continued a separate probe into alleged money laundering and kickbacks at Petrobras. One result was the opening of a formal investigation of two sitting governors and one former governor on charges of skimming Petrobras contracts in order to finance electoral campaigns. Rio de Janeiro Governor Luiz Fernando Pezão, former Rio Governor Sérgio Cabral and Acre Governor Tião Viana all denied the charges.

Rousseff, Obama announce bilateral meeting during April Americas Summit. Brazilian President Dilma Rousseff and U.S. counterpart Barack Obama will hold a bilateral meeting during the two-day Americas Summit, scheduled to begin April 10 in Panama City, Panama. The announcement was made simultaneously by the two governments. It followed a phone conversation Friday between Rousseff and U.S. Vice President Joe Biden. According to the Brazilian government, Rousseff and Biden talked about the need to boost cooperation in areas such as energy, trade and global security. The last meeting between Rousseff and Obama occurred on the sidelines of the G20 meeting in Australia in November, but the brief encounter amounted to little more than pleasantries. A formal visit by Rousseff to Washington is still a possibility for later this year, according to Brazilian diplomatic sources. Such a visit, scheduled for 2013, was scrapped on news of U.S. electronics eavesdropping on Brazilian government officials.

Brazil, Mexico sign new four-year agreement on motor vehicle trade. Brazil and Mexico last week signed a new four-year agreement on bilateral trade in motor vehicles. In negotiating the accord, Brazil backed away from an ambitious free-trade goal cited in previous agreements. Instead, the new accord broadly repeats previous agreements. Bilateral trade in motor vehicles will be tariff-free on the first $1.56

billion over the 12 months beginning March 18. The tariff-free quota is actually slightly lower than the $1.64 billion in force for 2014-2015. In subsequent years, the tariff-free portion will rise by 4% per year through the 2018-2019 trade cycle. In 2019, the two parties will once again aim at a sweeping free-trade agreement.

Business News

Investment News:

Brazilian-based steel multinational **Gerdau** last week announced a major reduction in its investment budget. The company said it will invest 17% less in 2015 than in the previous year for a total of about R$1.9 billion. The company cited poor demand for its products on the Brazilian market for the decision to scale back on projects. Gerdau said it is operating at about 70% of capacity.

Company News:

Despite involvement in the sweeping Petrobras corruption scandal, Bahia-based contractor **Odebrecht** is still doing business with Brazil's government, although indirectly. Last week, Brazil's National Development Bank gave final authorization to a $150 million loan to the Cuban government for renovation of Cuba's main airport. The entire value of the loan will be gradually paid over by Cuba to Odebrecht, which is supervising the project.

Brazilian Calendar

--Wednesday, March 18, Government auction of concession to Rio-Niteroi Bridge, Brasília

Indicators

Foreign exchange rate: **R$3.25 = $1.00**

Personal computer sales plummeted in Brazil in 2014 and are unlikely to recover this year, according to a study released last week by local consulting group IDC. The group put 2014 sales at 10.3 million, down 26% from 2013. The group is forecasting another 3% decline this year. A stronger U.S. dollar is one reason for the decline, given that many components of domestically assembled computers are imported. Sky-high interest rates are another factor, with many consumers only able to purchase a computer in installments.

Conservation, spurred by rate hikes, finally made an impact on Brazilian **energy usage** in February. According to figures released last week by the National Energy Grid (ONS), total usage declined 2.8% in February against the same month a year earlier and 2.5% against January. A sluggish economy, especially in the industrial southeast, also contributed to lower consumption of electric power.

The Brazilian Census Bureau (IBGE) last week released definitive data on **gross domestic product** for 2010 and 2011, based on new methodology approved by the United Nations. The data showed greater GDP growth than previously reported. For 2010, GDP expanded 7.6%, instead of the 7.5% previously reported, while for 2011 growth was 3.9% rather than the 2.7% previously reported. The new methodology includes more detailed information about research, development and investments. It also gives more weight to health, services and construction.

Retailers staged a rebound in January on heavily discounted sales of consumer goods following a disappointing Christmas season. The Brazilian Census Bureau reported a 0.8% month-on-month rise in **retail sales** in January. However, the year-on-year increase was a disappointing 0.6%. The National Confederation of Retailers reduced its projection for 2015 from a 1.7% rise in sales to just 1.0% as consumers continue to struggle with job security worries, inflation and rising interest rates.