



Interview: Finance Minister Joaquim Levy

--“We can’t afford to take any chances when it comes to fiscal policy.”—

Finance Minister Joaquim Levy made his most detailed, and vehement, appeal to date for a broad fiscal adjustment at a meeting last week of São Paulo business leaders and reporters. In frank comments, he said success in re-organizing the nation’s finances was crucial to maintaining Brazil’s investment grade credit rating. He cited the need for tax reform, improved labor productivity and resistance against pressure for more protectionism. He described relations with other Cabinet members and with President Dilma Rousseff as cordial. “We’re all playing on the same team,” he said. “And the President is the leader.” Excerpts follow:

- **On the proposed fiscal adjustment:** “We can’t afford to take any chances when it comes to fiscal policy. Our aim is to bring government spending back to the 2013 level. That is going to upset a lot of people, but we’re pressing forward. Everyone must do his part. If we can move forward on both the spending front and the taxation front, then investors will know better where to put their money, and when.”
- **On tax reform:** “We need agreement with Congress on reforming PIS Cofins (welfare taxes) and ICMS (state sales taxes) and that means support from the states, especially through the Senate phase. Such an agreement would bring an immediate surge in investments.”
- **On fiscal responsibility and Brazil’s sovereign credit rating:** “We are going to continue pressing forward with the fiscal adjustment. The decision (by Standard and Poor’s) to maintain Brazil’s investment grade rating was a vote of confidence in the capacity of the government and of Congress to make the necessary adjustments, which are absolutely imperative. February tax collections were a disappointment. This is worrisome in terms of Treasury performance. We are going to monitor this and take whatever steps are necessary. The Fiscal Responsibility Law demands no less of us.”
- **On harmony within the administration:** “There is a climate of confidence between me and President Dilma Rousseff. We’re all playing on the same team and the President is the leader.”
- **On prospects for the economy:** “Over the next few months, I believe there will be a resumption of industrial production as manufacturers respond to domestic demand. This is already happening. If we avoid further risks and move swiftly on the fiscal adjustment, then we will be able to create conditions for a rapid return to growth. Brazil has much in its favor.”
- **On micro-economic policies:** “We need to boost investment and foment competition. When everyone is protected and comfortable, no one feels the need to become more competitive. We need to understand that conditions have changed and that our ability to stimulate the economy through counter-cyclical measures has reached a point of exhaustion. We lost a great deal of

productivity over the last few years and we need to recover it. Global involvement is going to become more and more important for segments such as motor vehicles and capital goods but also for small and mid-cap companies. We have enormous advantages in natural resources and agriculture but, with the current shift in relative prices, we are also going to have to compete in other areas. Even Brazil's domestic market is completely different from what it was 10 or 15 years ago."

Top News of the Week

President Rousseff announces 'working visit' to Washington for June 30. President Dilma Rousseff will meet U.S. counterpart Barack Obama for a 'working visit' in Washington on June 30, the Brazilian government announced over the weekend. The announcement was made following a bilateral meeting between the two presidents at the Americas' Summit in Panama. Rousseff had been originally scheduled for a state visit to the U.S. in October of 2013 but that trip was scuttled by reports of U.S. electronic spying on Brazil's government. Following the bilateral meeting in Panama, Rousseff said the spying episode has been "surmounted." She said President Obama gave her assurances that "friendly nations" will not be the object of U.S. surveillance. More broadly, President Rousseff touched on the probable agenda for the June 30 meeting. She said it will include issues such as global warming, clean energy, including solar energy and ethanol, defense and education. Aides said the agenda is also likely to include expansion of the Open Skies initiative allowing airlines from each country greater access to routes in the other country. Visa liberalization is another likely topic.

Rousseff makes key political change in the face of impeachment pressure. President Dilma Rousseff last week shifted her political affairs coordinator, Pepe Vargas, to the less sensitive post of Human Rights Minister while turning over the political coordination office to Vice President Michel Temer. The move represented a recognition of the increased importance of the PMDB (Partido do Movimento Democrático Brasileiro) and the fast waning popularity of Rousseff's own PT (Partido dos Trabalhadores). Temer is the PMDB's leading figure while Vargas is a PT congressman. Temer's main job will be pushing the administration's legislative agenda, which is bogged down in an increasingly recalcitrant Congress. Both houses of Congress are dominated by the PMDB. The President was once again stunned by highly negative polling results last week. A poll by the Datafolha organization showed 63% of voting-age Brazilians in favor of impeachment. Voters nationwide told Datafolha they are worried about multiply economic problems, including job losses and inflation. Voters are also revolted by continued revelations of corruption at state-run energy company Petrobras. Anti-government protests on Sunday drew about 500,000 Brazilians to the streets in 21 states, with many demanding impeachment.

Weak first quarter performance pulls down 2015 auto industry forecasts. An unexpectedly weak first quarter led the National Motor Vehicle Manufacturers Association last week to drastically reduce its forecasts for 2015 production and sales. Total first quarter production of 663,099 represented a 16.2% decline from the same period a year earlier. First quarter sales of 559,925 were down 15.3% from the first quarter of 2014. Previously, the industry had expected flat sales and production for 2015. As of last week, the industry is now predicting a sharp decline. Production is likely to fall 10% from last year's 3.15 million while sales are likely to tumble 12.3% from last year's 3.5 million. Problems include the January 1 lapse of consumer tax breaks on motor vehicle purchases as well as rapidly rising interest rates.

Business News

Investment News:

Despite political uncertainties and an unsettled economy, 2015 could end up being a good year for private equity investments, according to the **Brazilian Private Equity and**

Venture Capital Association. The association held its annual meeting last week, with directors saying 2015 presents promising opportunities for the kind of long-term investments favored by private equity funds. Reasons include the emergence of a new breed of construction companies and contractors filling the gap left by corruption allegations levied against traditional firms in the sector. Another factor is the reluctance of banks when it comes to business lending. Meanwhile, individual and institutional investors have shunned stocks and bonds, leaving the door open for private placements. Brazilian private equity investments shrank by 18.6% in 2014 to R\$13.6 billion. However, equity funds continued to raise money and are now eager to invest it. Total available funds for private equity and venture capital placements reached R\$36.8 billion at the end of 2014, up from R\$27.2 billion at the end of the previous year.

Fitch Ratings last week downgraded Brazil's sovereign credit outlook to 'negative' from 'stable' but maintained the rating itself at triple-B, an investment grade level. Fitch said the downgrade was due to persistent economic problems in Brazil such as slow growth and rising inflation. A key factor in future credit reviews will be the government's handling of worrisome budget deficits, Fitch said.

Company News:

Brazilian **e-commerce retailers** are expected to slip in 2015, due mainly to macro-economic factors, according to a study last week by A.T.Kearney. In its annual Global Retail E-Commerce report, Kearney listed Brazil as the 21st most active out of 30 countries surveyed. Brazil's ranking is down from 7th in last year's report. According to the report, Brazilian e-commerce is likely to be hobbled this year by high interest rates, inflation and declining consumer confidence. Brazilian e-commerce logged the equivalent of about \$13 billion in sales last year.

Brazilian Calendar

--**Tuesday**, April 14, Brazilian Census Bureau (IBGE) release of monthly retail sales data, Rio de Janeiro

--**Thursday**, April 16, InterNews seminar on Challenges for the Brazilian Economy, Hotel Meliá Jardim Europa, São Paulo

--**Friday**, April 17, Finance Minister Joaquim Levy and Central Bank President Alexandre Tombini attend annual IMF and World Bank meeting in Washington

Indicators

Foreign exchange rate: **R\$3.08 = \$1.00**

The **Brazilian Steel Institute** last week revised its 2015 forecast for domestic steel consumption downward to reflect the country's stalled economy. The institute is now forecasting domestic sales of 19.1 million metric tons, down 8.0% from 2014. In November, the institute had projected a 4% gain for 2015. According to the institute, construction and infrastructure projects have been the hardest hit segments of Brazil's domestic economy. Both are heavy users of steel.

Brazilian monthly and annual **inflation rates** hit their highest levels since 2003 in March, the Brazilian Census Bureau said last week. March monthly inflation hit 1.32% on rapidly rising electric energy, housing and food costs. The 12-month rate reached a dizzying

8.13%. February monthly inflation had been 1.22% for a 12-month rate of 7.7%. Under Brazil's inflation-targeting program, the government is committed to price rises in 2015 of no more than 6.5%. According to economists, the disappointing March figures will likely result in Central Bank-ordered interest rate hikes.

