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BRAZIL BULLETIN INTERVIEW: Andre Nassif, Fluminense Federal University Economist –"We need to manage the foreign exchange rate so that it directs investment into the areas where it is most needed." Brazil is gradually creeping toward a danger zone - the danger of de-industrialization. The 40% appreciation of the Brazilian Real over the past two years is bringing an increase in cheap manufactured imports while hurting Brazil's ability to win, and maintain, overseas markets for its own products, according to Fluminense Federal University Economist Andre Nassif. Nassif commented on the process of de-industrialization in a recent interview. Excerpts follow:

- On foreign exchange policy: "We need a foreign exchange policy that incorporates a small—say 4% to 5%--*under*-valuation of the Brazilian Real. Instead, we have a 50% *over*-valuation, which undermines exports and manufactured products. Foreign exchange and economic growth are intimately related. We need to manage the foreign exchange rate so that it directs investment into the areas where it is most needed."

- On the ideal exchange rate: "The ideal level for the Real is R$2.90 to the dollar, but not necessarily in the short term. It should be a goal, attained over a period of four or five years. If the government started to just *think* about how to reach the goal that would be a good start."

- On foreign exchange and investment: "The level of R$2.90 would stimulate investment and innovation for growth. But even if we got only as far as R$1.90, or R$1.80 or even R$1.70, that would be a big help. Otherwise, we have to live with the threat of de-industrialization (the process by which manufactured products are substituted by imports because of the appreciation of the local currency)."

- On macroeconomic policy: "Brazil's main problem is macroeconomic, not microeconomic. On the microeconomic side, we have problems such as education, infrastructure and innovation, but we're working on them. The ball is rolling. On the macroeconomic side, we seem to be stuck with high interest rates and an overvalued currency with little room for maneuver."

- On the Central Bank under new President Alexandre Tombini: "Central Bank President Tombini is trying something new. He's trying to deal with inflation the way India deals with it. You use *all* the macroeconomic weapons at your disposal, not just monetary policy. But he's under a lot of pressure to stick to just monetary tightening."

U.S. House of Representatives vote puts cotton accord with Brazil in check. The U.S. House of Representatives last week voted to approve a $125.5 billion agricultural appropriations bill, including a provision eliminating an annual payment of $147.3 million to Brazil as part of a bilateral accord on cotton. The accord was reached last year following a 2009 ruling by the World Trade Organization that U.S. cotton subsidies from earlier in the decade were illegal. The WTO ruling gave Brazil the right to $829 million in trade retaliation measures against the U.S. Such measures could include higher tariffs on goods as well as measures aimed at U.S. intellectual property. Under the accord, Brazil waived its right to trade and intellectual property retaliation in exchange for the annual payment of $147.3 million per year, for two years, to the Brazilian Cotton Institute, along with other U.S. trade concessions. The U.S. farm bill must still be voted on by the Senate and then signed by President Barack Obama. The Obama administration negotiated the 2010 bilateral accord and has strongly defended its provisions. In Brasília, Brazilian Foreign Minister Antonio Patriota said eventual failure of the U.S. to meet future payments under the bilateral accord would render the agreement null and void. "That would promote the resumption of Brazilian trade retaliation," Patriota told reporters. "We are hopeful it will not come to that point."

U.S. takes tentative step to remove obstacles to Brazilian ethanol imports. The U.S. Senate last week adopted an amendment to an economic development bill that would eliminate the $0.54 per gallon ethanol tariff and the $0.45 per gallon blender's tax credit for domestic producers of ethanol. The Senate voted by a lopsided 73-27 in favor of the amendment. The amendment would save American taxpayers some $6 billion per year but would make U.S. corn-based ethanol less competitive in the American market than sugarcane-based ethanol fuels imported from Brazil. The Brazilian Sugarcane Industry Association (Unica) hailed the measure. "It is an important step towards developing a global market for clean energy," said Unica's representative in the U.S., Leticia Phillips. But even proponents of the amendment noted that last week's vote was only a first step. The economic development bill must still be passed by the full Senate and then, with the ethanol amendment still intact, by the House of Representatives. Defenders of the tariff and the blender's subsidy have vowed to fight the amendment in the lower house of congress.

U.S. agrees to remove orange juice dumping surcharge within nine months. Brazil and the United States last week reached an agreement on the removal of U.S. dumping surcharges against Brazilian orange juice. The World Trade Organization in March ruled in favor of Brazil in a case involving the calculations used by the U.S. Commerce Department in determining dumping charges. The WTO ruled that the practice of so-called "zeroing" of base prices was illegal. The U.S. could have appealed the ruling, under WTO rules, but last week agreed to waive its right to do so. Instead, the U.S. and Brazil reached agreement on a nine-month phase out of U.S. anti-dumping surcharges in place since 2008. The surcharges amounted to 5.26% to 8.13% over import prices. Brazil is the world's largest orange juice exporter. Brazilian Foreign Minister Antonio Patriota called the agreement "a definitive victory." The Brazilian Citrus Exporters Association, however, said the accord failed to resolve the broader issue of regular U.S. tariffs on orange juice. The regular tariff is $416 per ton over frozen concentrated orange juice imports. Association President Christian Lohbauer said a major increase in Brazilian orange juice exports to the U.S. will only come when the tariff is reduced or abolished.

Poll shows President Rousseff's popularity intact despite Palocci scandal. President Dilma Rousseff's popularity continues strong despite the resignation of controversial chief-of-staff Antonio Palocci, according to a Datafolha poll last week. The poll showed 49% of voting-age Brazilians calling the Rousseff administration "good" or "excellent," up from 47% in March. The poll was taken shortly after the Palocci resignation last week. The former chief-of-staff quit following allegations of influence-peddling. Only 10% of voting-age Brazilians called the administration's performance "poor," up from 7% in March. The balance of the poll showed Brazilians calling the administration "fair" or declining comment. Datafolha polled nearly 2,200 Brazilians, nationwide. The poll's margin or error is two percentage points.

Tax collections continue robust growth, budget target seems assured. Robust growth in tax collections continued in May, with Brazil picking up R$71.5 billion in federal revenues, the government said last week. Monthly collections in May were up 7.2%, in inflation-adjusted terms, from the same month a year ago. Tax collections for the year-to-date were R$382.9 billion, up 10.7% from the first five months of 2010. Tax officials said Brazil is on target for meeting its 2011 goal of R$619 billion in revenues. The increase in revenues should assure the government's ability to meet its primary budget surplus goal for the year, which is R$117.9 billion, officials said.

Investment News: Mexican-owned telephone giant America Movil SA will invest $1.2 billion in its Brazilian unit, beginning this year, in a bid to maintain the company's second place ranking in the country's mobile phone market. America Movil controls Brazilian mobile phone company **Claro**, which currently boasts a 25% market share. The money will go toward technical upgrades, expansion and better handling of new-generation data services, company sources said. Claro competes with the Brazilian unit of Italy's TIM and with Vivo, controlled by Spain's Telefonica. *** The Brazilian unit of **Burger King** plans to invest the equivalent of $570 million over the next five years, company sources said last week. Investments will be aimed at opening 900 new restaurants during the period.

Company News: State-run energy giant **Petrobras** announced important oil and natural gas finds in the Gulf of Mexico. Petrobras holds stakes in the blocks in conjunction with Exxon Mobile and Eni Petroleum. The discoveries could hold reserves as high as 700 million barrels and are located 400 kilometers southwest of New Orleans. *** São Paulo's consumer protection agency, Procon, last week said it has asked federal electric power regulators to assume administrative control of local utility **Eletropaulo**. Procon made the unusual request following a series of blackouts in Eletropaulo's jurisdiction this year. Federal regulator Aneel had no immediate comment on the request. Eletropaulo said it has invested R$2.5 billion in the past five years to improve service. In a statement, the company said its record for blackouts is better than the average for Brazilian utilities.

Indicators: Brazilian **aluminum production** suffered another setback in May, with year-on-year output down 8.8% at 119,400 metric tons, the Brazilian Aluminum Association (Abal) said last week. Five-month production was down 6.6% at 592,500 tons. Output was in decline because of a smelter closing in Bahia, due to high energy costs, and idle smelter capacity in São Paulo, due to maintenance work.

Other News: In an unexpected move, the Peruvian government last week canceled a joint hydroelectric project on the Peru-Brazil border. Peru dumped the **Inambari dam project**, saying it had not obtained wide backing from local residents. The project had been slated to produce 2,000 megawatts of electricity. Brazil and Peru are pledged to jointly develop five other hydroelectric projects.

Brazilian Calendar for Week of June 20:

- **Monday,** June 20, XI Brazilian Technology and Innovation Conference, Convention Center, Fortaleza, Ceara
- **Wednesday,** June 22, Brazilian Census Bureau (IBGE) release of monthly unemployment data, Rio de Janeiro
- **Thursday,** June 23, Corpus Christie national holiday

R$1.59 = $1.00