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BRAZIL BULLETIN INTERVIEW: Roberto Giannetti da Fonseca, International Affairs Director of the São Paulo Federation of Industries (Fiesp) "Brazil is losing out on the world economic recovery because of the strong Real." Brazil's foreign trade position is increasingly fragile, with exports sustained only by high commodities prices and imports crowding out domestic manufacturers, according to Fiesp executive Roberto Giannetti da Fonseca. The economist and trade expert spoke recently with specialized reporters at Fiesp headquarters. Excerpts follow:

- On foreign trade accounts: "The trade balance is still favorable. The first quarter surplus ($3.2 billion) was much higher than the first quarter of 2010 ($882 million), but that was due entirely to higher international commodities prices. The trade surplus is fragile. Without higher commodities prices, there would have been a deficit of $5 billion to $7 billion."

- On trade in manufactured products: "When it comes to manufactured products, we're running a deficit in the trade account. That deficit could reach $100 billion this year. This has become a structural deficit. Our industries are vulnerable because of high labor costs, taxes and rising raw materials costs, all of this in addition to an overvalued Brazilian Real."

- On Brazilian exports: "Brazil is losing out on the world economic recovery because of the strong Real. On the domestic side, we're experiencing a robust economic recovery but imports are getting the greater part of the benefit. About two-thirds of the increase in consumption is being met by imports."

- On de-industrialization: "We're seeing a process of substitution of domestic manufactured products by imports. This is the classic process of de-industrialization."

- On Brazilian investments overseas: "Some Brazilian companies are actually opening factories in Asia. We're seeing this in textiles, footwear and auto parts. So, in effect, Brazilian auto makers are now importing parts, even though the auto parts companies are Brazilian."

- On effects of high commodities prices: "Higher commodities prices also mean higher raw material costs for manufacturers. High cotton prices, for example, are hurting textile industry margins."

Moody's upgrades Brazil rating on "capable handling" of fiscal policy, inflation. Moody's Investors Service last week upgraded Brazil's sovereign credit rating by one notch to Baa2, or two notches above investment grade. The Moody's rating for Brazil is now equal to that of Standard & Poor's and Fitch. In making the ratings change, Moody's Senior Credit Officer Mauro Leos cited Brazil's "capable handling" of fiscal and monetary challenges. Brazil's government has been wrestling with 6.5% inflation and a slowdown in economic growth. Measures taken by the government so far this year include interest rate hikes and cuts in federal spending. Leos called the policy choices "highly responsible," assuring that Brazil will meet primary budget surplus targets for the year and pull down inflation by 2012. Finance Minister Guido Mantega said the ratings upgrade was "evidence that overseas perceptions about Brazil are highly positive."

Unemployment rate steady in May at 6.4%, likely to decline in second half. Brazil's unemployment rate remained steady in May against April at 6.4%, the Brazilian Census Bureau (IBGE) said last week. Unemployment in May of 2010 was 7.5%. "The trend is for the unemployment rate to decline in the second half of the year," said Cimar Azeredo, an IBGE economist. Second-half jobs performance tends to improve on seasonal factors such as the grain and oilseeds harvest, enhanced foreign trade and a year-end rise in manufacturing and retail activities. Average salaries of fully registered employees rose 1.1% from April and 4% from May of 2010 to R$1,566. Further wage gains are likely as skilled labor becomes scarce, economists said. August should see tense wage talks when nationwide contracts come up for workers in three key segments of the labor market—banks, oil and steel. Contracts for more than one million workers in the three segments expire on September 1.

BNDES reaches accord with Japanese state-run bank on $3 billion credit line. Brazil's National Development Bank (BNDES) last week reached agreement with Japan's Bank for International Cooperation on a $3 billion credit line from the Japanese institution. The money will be used for re-lending by the BNDES to Brazilian joint ventures involving local companies with Japanese partners. A large number of Brazil-Japan joint ventures are likely ahead of the 2014 World Soccer Cup and the 2016 Rio de Janeiro Olympics. Loans will carry terms of up to ten years. Spokesmen for the two banks said loans will be focused on joint ventures in the area of local and long-distance transportation.

Brazilian investments led by capital goods manufacturers, says BNDES report. Brazil gets more bang out of its investment buck than China and India because of the high level of concentration on capital goods, according to a report last week by the National Development Bank (BNDES). Citing consolidated World Bank figures from 2005, the report showed Brazil with an investment rate of 16.3% of gross domestic product, lagging China's spectacular 41.5% and India's 28.5%. But the component represented by capital goods manufacturing, in the Brazilian case, was much higher than for the others, the report said. In 2005, nearly half of all investments, equal to 7.9% of GDP, went to capital goods. In China's case, capital goods accounted for 11.5% of GDP while, for India, the figure was 13.1%. In Brazil's case, the investment rate as of 2010 had advanced to 18.4% of GDP, with capital goods at more than half, or 10.2%, the report found. Biggest buyers of Brazilian capital goods will continue to be the oil and gas industry, heavy construction, steel and motor vehicles.

Investment News: Swiss industrial group **ABB** said last week it will invest an additional $200 million in its Brazilian operations, including opening of a fourth industrial facility. The new factory will be located in Sorocaba, São Paulo state. ABB manufactured a wide range of equipment for industry, power stations and infrastructure projects. *** The **Travelers Group** last week announced the purchase of a 43% stake in Brazilian surety insurance company J. Malucelli for the equivalent of $410 million. Malucelli has a 30% share of the Brazilian market for surety insurance, policies that cover compliance with contract terms of business deals. Travelers Group has an option to buy an additional 6.9% of Malucelli's shares within 18 months.

Company News: U.S. fast food chain **Quiznos** is planning a major incursion into the Brazilian market via a franchising agreement with Brazil Best Food Inc., the companies said last week. The agreement calls for opening of seven Quiznos restaurants this year as part of a plan to eventually open 200 nationwide. *** The Brazilian subsidiary of U.S. home appliance giant **Whirlpool** last week announced it has settled an outstanding issue with Brazil's Banco Safra stemming from a 1989 loan. Whirlpool's Brazilian unit will pay off the loan at a total cost equal to $603 million in installments in 2011 and 2012. The claim originated from an unauthorized loan in 1989 to Embraco, a Brazilian company later bought by Whirlpool. The settlement must still be approved by a Brazilian court.

Indicators: Brazilian **raw steel output** rose 9.6% in May, against the previous month, to 3.3 million metric tons, on rising domestic demand and a surge in exports, the Brazilian Steel Institute (IABr) said last week. Production was up 14.7% against May of 2010. Year-to-date output of 14.8 million metric tons was up 9.0% from the first five months of 2010. Domestic demand during the first five months of the year rose by a modest 4.8% while exports surged 33.4% as the global economic recovery gained strength.

Other News: A number of Brazilian **government websites** were taken off the air for up to several hours last week after systematic attacks from international and domestic hackers. Affected sites include those operated by President Dilma Rousseff, the Brazilian Senate, the Brazilian Census Bureau (IBGE), the Sports Ministry, state oil company Petrobras and several others. Officials said there was no loss of data, operating capabilities or archives. A task force at the Federal Data Processing Service (Serpro) is investigating the attacks. Hackers attacking the Brazilian sites include the international LulzSec group and a domestic group called Fail Shell.

Brazilian Calendar for Week of June 27:

- **Monday, June 27 -** Standard and Poor's seminar on Bonds and Loans Brazil, Hotel Unique, São Paulo
- **Monday, June 27 -** Brazilian Central Bank release of monthly current account figures, Brasília

- **Tuesday, June 28 -** Brazilian Central Bank release of monthly figures for lending volume and interest spreads, Brasília
- **Tuesday, June 28 -** Seminar Projects and Money Latin America, Rio de Janeiro Stock Exchange Conference Center, Rio de Janeiro
- **Wednesday, June 29 -** Brazilian Central Bank issues its quarterly inflation report, Brasília
- **Thursday, June 30 -** Monthly meeting of the National Monetary Policy, review of inflation targets for 2011 and 2012, setting of inflation target for 2013, Brasília
- **Thursday, June 30,** Brazilian Central Bank release of monthly primary budget surplus figures, Brasília
- **Friday, July 1 -** Trade and Development Ministry release of monthly foreign trade figures, Brasília
- **Friday, July 1 -** Brazilian Census Bureau (IBGE) release of monthly industrial production figures, Rio de Janeiro

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R$1.60 = $1.00