



Brazil-U.S. Business Council, Brazil Bulletin, Vol. XXI, No. 28
July 11, 2011

BRAZIL BULLETIN INTERVIEW: Octavio de Barros, Chief Economist at Banco Bradesco –“Lula was the demand-side president. Dilma is the supply-side president.” Octavio de Barros, Chief Economist of Brazil’s number three bank of Bradesco, is more bullish on Brazil than the average bank executive. The reason is that Bradesco has detected a rising tide of business investment, enough to insure sustained growth and continued income distribution for at least another decade. Barros spoke to investors and reporters at a recent seminar in São Paulo. Excerpts follow:

- On investments: “We are seeing the biggest wave of business investment since the 1970s. This is actually the driver for inflation right now, not consumption. We under-invested for decades and now we are over-investing. We expect an investment rate this year equal to 19.5% of GDP, up from 18.5% in 2010. Then, we are forecasting 20.1% for 2012. We can reach an investment rate of 23% in the next few years.”
- On investment rate signals: “Productivity is rising faster than GDP, supporting growth. And capital goods demand is up.”
- On government policies and growth: “Lula was the demand-side president. Dilma is the supply-side president. Under President Rousseff, there is a high priority for eliminating the bottlenecks. We are forecasting average GDP growth per year of 4.5% through 2020. We see per capita income rising to \$18,000 by 2020 from \$11,000 in 2010 and there will be much better distribution of income.” \
- On oil and gas: “By 2020, oil and gas will represent 20% of Brazilian GDP, up from 12% in 2010. Frankly, no one really knows what that will mean.”
- On the middle-income trap: “Brazil has to guard against the middle-income trap, the phenomenon by which a country eliminates extreme poverty, produces a decent standard of living for its population and then stops there, not taking the last long step.”
- On labor and inflation: “Some people say there is a shortage of skilled labor. We say there are labor shortages *everywhere* in the economy. Inflation will come down slowly, but it will come down, to 6.3% by the end of this year and then 4.5% by the end of 2012.”

Key U.S. senators reach accord on deal to end ethanol subsidies. A group of U.S. senators last week reached agreement on a legislative strategy that could end ethanol subsidies this year. Senators Dianne Feinstein (D-Calif.), Amy Klobuchar (D-Minn.) and John Thune (R-SD) said they have reached agreement on ending the 45 cent-per-gallon tax credit for blended ethanol in gasoline and the 54 cent-per-gallon tariff on imported

ethanol. The deal fits in with congressional efforts to cut government spending and a government drive to reduce U.S. dependence on crude oil. Sponsors of the agreement are still seeking support in the full Senate and the House of Representatives. The policy opens an opportunity for Brazilian ethanol producers. Brazil's sugarcane-based ethanol has been largely uncompetitive in the U.S. market because of the subsidy and the tariff. In the shorter term, however, Brazil might encounter problems in meeting eventual U.S. demand. Shortages of ethanol in the Brazilian market have led to price hikes, contributing to an already worrisome inflation level.

Transportation minister Nascimento resigns amid corruption charges.

Transportation Minister Alfredo Nascimento resigned last week amid charges of bribetaking, influence-peddling and incompetence in management of highway and railroad projects. Two other Transportation Ministry officials also resigned. Nascimento and the other officials have denied the accusations, saying they will cooperate with federal investigators. In a related development, President Dilma Rousseff suspended signing of any new Transportation Ministry public works contracts for at least 30 days. The ministry's executive secretary, Paulo Passos, was named interim minister. Press reports said Mato Grosso Senator Blairo Maggi was offered the post by President Rousseff but turned it down because of possible conflicts-of-interest. Maggi holds extensive real estate and industrial holdings in his home state. Both Nascimento and Maggi are members of the Republican Party (PR).

Monthly inflation eases in June, but annual rate still above target. Brazil's monthly inflation rate eased in June to 0.15% from 0.47% in May, but a high basis of comparison from 2010 left 12-month inflation at a stubborn 6.71%. Under Brazil's inflation-target program, the country is committed to a 2011 inflation rate of 4.5%, with two percentage points of leeway. That makes 6.5% the upper limit of the target range. Officials have pledged to take whatever monetary and fiscal measures are necessary to pull inflation below 6.5% by the end of 2011. Such pronouncements make another interest rate hike later in July all but certain. Brazil's Selic base rate is already a towering 12.25%. Economists, however, believe monthly inflation rates in July and August will be quite low, possibly even negative. Food and fuel prices, for example, actually declined slightly in June. Most economists are predicting year-end inflation of about 6.2%.

Motor vehicle figures still strong versus 2010, but show month-on-month decline.

Brazilian motor vehicle production and sales showed continued robust growth against 2010 performance but were down in June against May levels, according to figures last week from the National Motor Vehicle Manufacturers Association (Anfavea). June sales were up 16%, year-on-year, at 286,912, but that figure represented a 4.5% decline from May. Sales were down, month-on-month, on consumer credit curbs, Anfavea said. June production was 272,630, up 3.3% from June a year ago but down 3% from May. Exports reached \$1 billion in June, up 12.5% from June of 2010, but representing an 8% decline from May. Economists said month-on-month performance could stabilize or decline in the coming months as Brazil's government seeks to cool the economy and fight down inflation. First-half sales were 1.64 million, up 9.5% from the first half of 2010. First-half

production was 1.59 million vehicles, up 3.6% from last year. First-half exports reached \$5.7 billion, a hefty 18.4% gain from the first six months of 2010.

Utilization of industrial capacity rises slightly in May, says CNI. Utilization of Brazil's industrial capacity rose slightly in May to 82.4% from 82.2% in April, following two straight months of decline, the National Confederation of Industries (CNI) said last week. Utilization of installed capacity in May of 2010 was 82.8%. Overall, the CNI said recent figures showed that Brazil's economy is cooling slightly, in line with government curbs on consumer credit and cuts in federal spending. Utilization of industrial capacity hit a three-year high of 83.4% in February of this year. Industrial sales in May were off 1.3% from April, although they were still 6.7% higher than in May of 2010. Brazil's government has been seeking to moderate the country's growth in order to pull down inflation, currently running at more than 6.5%.

Investment News: Brazil's largest paper and pulp company, **Fibria**, said last week it will invest some \$9.6 billion in efforts to nearly double its pulp capacity to 10 million metric tons per year by 2025. Capacity is currently 5.25 million tons. Half the investment total will come from company revenues and the other half from the debt market. *** **Telecom Italia** last week announced the purchase of a Brazilian fiber optics company owned by U.S. utility AES for 700 million euros. The company will be absorbed by Telecom Italia's Brazilian unit, TIM SA to enhance the mobile phone company's technological base. *** The Brazilian government last week issued \$550 million in new **overseas bonds** maturing in 2021. It was the first issue under the administration of President Dilma Rousseff. The bonds brought a yield of 4.188%, the lowest ever for Brazilian sovereign paper.

Company News: Brazil's largest sugar and ethanol group, **Copersucar**, will promote an initial public offering of shares later in July, the company said last week. Copersucar will offer 108 million shares to both domestic and overseas investors. The company expects to raise at least R\$2 billion from the offer. Copersucar sold 5.2 million metric tons of sugar and 3.6 billion liters of ethanol in the most recent fiscal year.

Indicators: Brazilian **electric power consumption** rose 2.8% in May from the month a year ago, with residential consumption leading the way at 5.0%, the National Energy Research Corp. (EPE) said last week. Industrial consumption was up only 1.0%, showing effects of a spreading deceleration of the economy. Energy use for the first five months of the year was up 3.8% from the same period in 2010. *** Brazilian **crude oil output** in May fell 0.2% from May, 2010 but rose 1.0% from April to 2.072 million barrels per day, the National Petroleum Authority (ANP) said last week. Output is expected to continue its expansion through the end of the year as more offshore platforms come on stream. Natural gas output climbed 7.4% from May, 2010 and 6.6% from April to 62.7 million cubic meters per day.

Other News: In its **bi-monthly report** on the economy, released last week, the Finance Ministry reinforced expectations for modest growth and persistent inflation. Brazil's GDP should expand by only 4.5% this year, down from 7.5% in 2010. Inflation will close

out the year at 5.6%, down only slightly from 5.9% last year. Brazil's investment rate will rise modestly to 19.5% of GDP from 18.5% in 2010. The report forecast a rise in consumer spending of 5.9% this year, still robust but down sharply from 10.3% in 2010.

Brazilian Calendar for Week of July 11:

- **Tuesday, July 12** - Brazilian Census Bureau (IBGE) release of monthly retail sales data, Rio de Janeiro
- **Wednesday, July 13** - Sixth Annual Tourism Fair, Parque Anhembi, São Paulo

R\$1.56 = \$1.00

Copyright 2011, Brazil-U.S. Business Council.