



**Brazil - U.S.
Business Council**

Brazil Bulletin

Interview: Amaury Bier, President of Gávea Investment Fund

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Brazil is a long way from recovering the fiscal responsibility—and credibility—built up in the 1990s, according to investment fund manager Amaury Bier. As Finance Ministry Executive-Secretary during that period, Bier helped formulate and implement the Fiscal Responsibility Act of 2000, the capstone of Brazil’s drive toward long-term stability for public accounts. Bier met with investors and reporters at a recent meeting in São Paulo. He said additional structural reforms will be needed to get Brazil’s accounts back on track. Excerpts follow:

- **On fiscal responsibility:** “There has been a complete lack of transparency in public accounts under President Dilma Rousseff. The truth is, we still don’t know the extent of the sleight-of-hand that went into manipulating public accounts during the first Rousseff Administration. The market no longer trusts the government’s numbers.”
- **On rebuilding fiscal credibility:** “The Planning Ministry is trying to re-establish credibility. But the fiscal targets are ambitious and investors are uncertain about the government’s ability to meet them.”
- **On short-term prospects for meeting targets:** “I believe the government will reach this year’s target—a primary budget surplus equal to 1.2% of GDP. Finance Minister Levy will do whatever is necessary to meet this target because his credibility is on the line. He’ll meet the target even if he has to do it by passing some spending on to 2016. But then what? We’ll reach the 2015 target, but only by using emergency measures. The target next year is even more ambitious, 2.0% of GDP.”
- **On meeting fiscal targets over the long term:** “Meeting the 1.2% target this year won’t be enough to fully recover fiscal responsibility, and market credibility. Brazil will need structural changes in order to make fiscal responsibility sustainable. But structural changes take time and their effects are only felt in the distant future. I believe such changes will be made, because they have to be made. In the meantime, to get through 2016 and 2017, I expect the government to raise taxes in order to meet budget targets. You can’t fire employees, you can’t reduce pensions, you can’t cut transfers, so there’s only one thing left to do—raise taxes.”
- **On Brazil and economic growth:** “During the Cardoso Administration (1995-2002) and the Lula Administration (2003-2010), Brazilian growth was on a par with that of other emerging market countries. During the four years of the first Rousseff Administration, Brazil began to lag. This year is going to be negative. Things could be a little better in 2016, and there could be the beginnings of a recovery in 2017.”

- **On inflation:** “We’ve seen a complete loss of credibility on the inflation front. If we don’t solve this problem now, we could see out-of-control inflation for years to come. If we can accept a run up in inflation from 6% to 8%, then why not 9% or 10% or 12%.”

Top News of the Week

Political crisis heats up as police, prosecutors target House speaker, ex-presidents. Federal Police and prosecutors last week extended their probe into alleged bribery and money laundering to two former presidents and the current speaker of the Chamber of Deputies. Police used search warrants to obtain documents and other evidence at the homes of former President Fernando Collor de Mello, now a senator, and PP (Partido Progressivo) National Chairman Ciro Nogueira, among others. Meanwhile, prosecutors announced that witnesses have named Chamber of Deputies Speaker Eduardo Cunha as recipient of some R\$5 million in bribes as part of a network of bribery and favoritism involved in awarding of distribution contracts by state-run oil company Petrobras. Collor, Nogueira, and Cunha all issued statements claiming innocence and criticizing the probe as politically motivated. Separately, prosecutors in Brasília announced they are investigating former President Luiz Inácio Lula da Silva for alleged influence-peddling. They said Lula obtained gifts, including international travel, from contractor Oderbrecht in exchange for his influence in arranging international contracts for the company. Lula vehemently denied the allegations, filing a motion with federal judges to quash the investigation. Speaker Cunha blamed Justice Minister José Eduardo Cunha for what he called “political persecution” and announced that he is formally breaking with the administration of President Dilma Rousseff. Cunha made the break official in a nationwide television address. He also announced that he will expedite a series of impeachment motions against President Rousseff. Spokesmen for the administration said Cunha’s actions could spark what they called “a serious institutional crisis.”

Government proposes sales tax reform, amnesty system for overseas funds. The Administration of President Dilma Rousseff last week proposed a reform of the nation’s patchwork sales tax system. The reform would set a uniform national sales tax of 4%, replacing the current system of different sales tax rates for different products in different states. To compensate states that would lose revenue under the new system, the government proposed creation of a special fund to be fed from tax revenues on assets held overseas by Brazilians. The government would collect revenues for the fund by offering an amnesty on criminal prosecutions to those declaring overseas assets. Government economists estimate such revenues as high as R\$25 billion. Congressional leaders greeted the proposals with skepticism. Small states could lose massive revenues from the plan, according to some members of Congress. Opposition leaders said they oppose the amnesty provision because it rewards criminal activities.

Chamber of Deputies completes action on electoral reform, scraps 5-year terms. The Chamber of Deputies last week completed action on a broad electoral reform. In a stunning reversal, the Chamber scrapped an earlier provision creating five-year terms of office for all elected officials. Congressional leaders said the five-year term had proven unpopular with both voters and politicians. Instead, the Chamber re-instated four-year terms for most officials and an eight-year term for senators. The Chamber, however, maintained its earlier provision scapping immediate re-election bids by executives, re-instating a traditional one-term limit for mayors, governors, and the president and vice president. The Chamber also re-instated the January 1 inauguration date for executive offices. Finally, the Chamber voted a provision severely limiting access to free television time during campaigns for parties joining electoral coalitions. The electoral reform must now be reviewed by the Senate. Both houses of Congress will recess in late July and early August.

Business News

Investment News:

Brazilian **passbook savings accounts** experienced a dismal first half, according to Central Bank data last week. June saw net withdrawals of R\$6.2 billion for first half net withdrawals of R\$38.5 billion. The decline in passbook savings accounts is hurting mortgage availability, the Central Bank noted. Brazilians are taking money out of passbook savings accounts because money market accounts are offering a higher return. They are also making net withdrawals to pay down consumer debt.

Company News:

The **Brazilian steel industry** will suffer a disastrous decline in domestic sales this year, compensated in part by steady exports. The Brazilian Steel Institute last week issued its 2015 forecast for the industry, predicting a 15.5% fall in domestic sales to 18.3 million metric tons. But exports will help maintain production at 32.8 million tons, a decline of only 3.4% from 2014. Exports are being aided by a slow but steady global economic recovery. Domestic sales are being hurt by a steep decline in sales of big-ticket items such as motor vehicles and a stalled construction industry.

Brazilian Calendar

-Wednesday, July 22, Brazilian Central Bank release of monthly current account data, Brasilia

-Thursday, July 23, Brazilian Census Bureau (IBGE) release of monthly retail unemployment data, Rio de Janeiro

Indicators

Foreign exchange rate: **R\$3.19 = \$1.00**

Retail sales declined for the fourth straight month in June, the Brazilian Census Bureau (IBGE) said last week. Sales were down 0.9% against May and 4.5% against June of 2014. Sales declined in most categories, including big-ticket areas such as motor vehicles as well as supermarkets, the IBGE said. Retail sales have been hit by rising inflation, high interest rates, and increased job worries among consumers.

June **tax revenues** produced another disappointment for Brazil's government. Revenues sank 2.4%, in inflation-adjusted terms, from June of 2014 to R\$97.1 billion, the Brazilian Tax Authority said last week. Revenues for the first half were R\$607.2 billion, down 2.9% from, in real terms, from the first half of 2014. Revenues are down mainly because of a sluggish economy. The government's inability to boost revenues, in real terms, could stymie 2015 budget goals.

Brazilian **economic activity** was virtually unchanged in May against April, posting an expansion of a bare 0.03%, according to the Brazilian Central Bank last week. May was better than April, when economic activity declined 0.88%. Nevertheless, economic activity in May was down 3.08% versus May of 2014. Brazil's economy is suffering from a combination of ills, including persistent inflation, high interest rates, and heavy consumer debts. Inflation is running at nearly 9% per year, with the Central Bank's base interest rate at a towering 13.75%, making it harder for consumers and businesses to pay off debts. The sluggish economy has also led to rising job security concerns.

