

05/23/2014

# The Week in Review

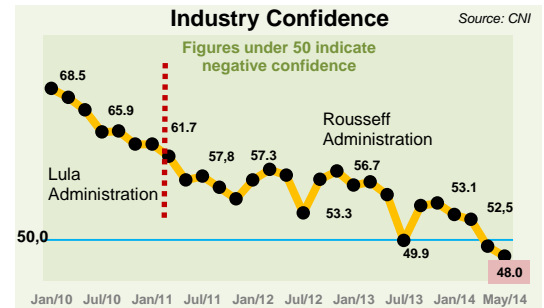
## On The Economic Front

### Industrial Confidence Index:

According to the National Confederation of Industry (CNI), in May the industrial confidence index fell to 48, the lowest index level in five years and the second lowest since the start of the series in 1999. Brazilian business people showed a lack of confidence in the economy and in the companies themselves.

### Mercosur-EU Trade:

President of CNI Robson Braga de Andrade said that the Brazilian industrial sector is advocating for a quick conclusion to the trade agreement talks between Mercosur and the European Union. According to Andrade, Brazilian businesses fear a protectionist backlash from the French agriculture sector, but the Brazilian and French industrial sectors are working together to present the counter point. According to the Minister of Development, Industry and Trade (MDIC) Mauro Borges, Brazil finished its proposal in October 2013 and is now working with Mercosur partners to consolidate a final proposal to be presented to the European Union soon. Quote: "We are prepared to discuss technology transfer and innovation, but an expansion of the bilateral relationship depends on the free trade agreement," said Andrade during the Brazil-France Economic Forum held in Paris.



### Tax Cut Renewal:

During a meeting of business leaders on Thursday May 22<sup>nd</sup>, President Dilma Rousseff indicated that her Administration will support the renewal of tax cuts established by Law 12.844/13, which is scheduled to expire on December 31, 2014. The law replaces a 20% payroll tax (PIS-Cofins) with a 1% or 2% tax on domestic sales for labor-intensive industries, such as home appliances, machinery and information technology. However, according to *Folha de S. Paulo*, because of concerns over fiscal constraints, the current tax benefits will likely not be extended to other sectors including retail (see more on the Campaign Trail below).

### Drought:

On Tuesday May 19<sup>th</sup>, president of the Brazilian Enterprise for Energy Research (EPE) Maurício Tolmasquim downplayed the risk of power rationing during the World Cup and added that today Brazil is in a much better position than in 2001, when the country also faced a severe drought that resulted in power outages and electricity rationing. Quote: "The press has been publishing a large number of studies that show a high risk of an energy deficit. I am just going to say that if one uses the same risk analysis methodology for 2014 that was used in 2001, a comparative risk of deficit in the Southeast region would be 6.7% today relative to 28% in May 14 years ago."

## On The Political Front

### Campaign Trail:

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As part of her business sector rapprochement strategy, **President Rousseff** inaugurated Embraer's new plant in Gavião Peixoto (SP) on Tuesday May 21<sup>st</sup>. The Brazilian Air Force (FAB) commissioned the aircraft manufacturer to build 28 KC-390 cargo planes, a BRL\$ 7.2 billion (US\$ 3.26 billion) deal including logistics support, spare parts, and maintenance. According to Embraer, the 10-year contract has the first cargo plane scheduled for delivery at the end of 2016. Quote: "No one can doubt that the defense industry is strategic to Brazil," said Rousseff, adding that "we are a country of superstars in soccer and technology, in which [Brazil] has the know-how and capability to produce an airplane on the scale of the KC-390."

Meanwhile, **PMDB**, Brazil's largest political party and **President Rousseff's** main ally, has indicated that it will support her reelection bid and also seek to retain Vice President Michel Temer (PMDB/SP) as her running mate in the October elections. Quote: "The Party is engaged in a project that stands on the pillars of [the current Administration's] achievements, including the reduction of inequality, increased job creation, income gains for workers, infrastructure modernization, and an increase in the investment ratio to GDP," said Civil Aviation Minister Moreira Franco (PMDB/RJ) in an interview with *Valor Econômico*.

According to *Folha de S. Paulo*, the former governor of São Paulo José Serra (PSDB) dismissed rumors that he will be the vice presidential running mate of **Senator Aécio Neves (PSDB/MG)**. Quote: "I am going to run for some Federal Legislative position — House or Senate. And this is it. Moreover, I will be working with my party to defeat this weird mix of regression and inertia that has dominated the country," said Serra. Neves said that if elected, he would reduce the current number of cabinet positions from 39 to 21 or 22 and also redefine some ministry functions.

The former governor of the state of Pernambuco **Eduardo Campos (PSB)** said that the Administration's congressional maneuver to add the Pernambuco Suape Port to the scope of the Senate Petrobras Probe is a "desperate act." Quote: "It's ok, let them investigate Suape as they wish. Our attitude will be completely different...as it will be our pleasure to show how we have managed Suape well."

### Car Wash Operation:

Supreme Court Judge Teori Zavascki backed down from his decision to release the 12 defendants detained for alleged financial crimes including money laundering and illegal exchange rate operations in the so-called *Operação Lava Jato* (Car Wash Operation). He decided to release only Paulo Roberto Costa, former Petrobras director of supply. All others investigated, including the money changer Alberto Youssef, will remain in custody until judge Zavascki reassesses the case.

### Strikes Ahead of the World Cup Games

Following last week's walkouts by bus drivers and the military police in the states of Rio de Janeiro and Pernambuco, this week's strikes challenged the federal, state, and municipal levels of government. On Tuesday May 20<sup>th</sup>, there was a one-day work stoppage by bus drivers and fare collectors that led to millions being without public transportation, causing a 162-mile gridlock throughout the city of São Paulo. On Thursday, some of the civil police forces in 17 states refused to report thefts, traffic violations, and other illegal activities. According to the Rousseff Administration, Brazil will deploy 150,000 military and police personnel during the tournament. (See more in The Pulse, below).

### Petrobras

On Tuesday, senators from the opposition parties did not attend the testimony of Petrobras' ex-president José Sergio Gabrielli at a public hearing held by the Senate Probe that is investigating the state-owned oil company's alleged corruption practices. Neither PSDB nor DEM attended the hearing in which the executive said the refinery in Pasadena, Texas (USA), was "cheap" at the time the negotiations were held. Only three of the 13 members of the Senate Probe represent the opposition: Senators Vania Lucia (PSDB-GO), Cyro Miranda (PSDB-GO), and Wilder Morais (DEM-GO), who were appointed by Senate President Renan Calheiros (PMDB-AL) because both parties had refused to make appointments, hoping to pressure Congress to install a joint probe where they would be better represented.

## Task Forces

### Innovation

**Data Protection:** On Tuesday, Senator Vital do Rêgo (PMDB/PB) introduced draft bill (PLS) 181/14, which would regulate processing activity of personal data in Brazil. The bill would establish, among other things,

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that foreign companies be notified and summoned on all the procedural steps set forth in the law and that any international transfer of personal data can only be performed with countries that provide the same level of data protection provided by this law. The administration has been developing its own proposal, which it had intended to introduce in Congress after the approval of the Internet Framework Bill ([Law 12.965/14](#)). The proposal is awaiting the approval of the Ministry of Planning before it can be sent to Congress.

**DataViva:** A partnership between MIT Media Lab in Massachusetts and the State of Minas Gerais launched an online site, DataViva, containing public data from 2002 to 2012 on the Brazilian economy, with 2013 data being compiled. The site provides an interactive map of the formal economy and will allow users to search through multiple levels of government data.

## Tax and Investment

**Regional Airports:** During the inauguration of the third passenger terminal at São Paulo's Guarulhos Airport on Monday, President Rousseff said the Administration will send to Congress bills to stimulate regional aviation in the country. The idea is to exempt all regional airports from paying airport fees as well as subsidize airplane tickets to ensure regular service with those airports. **Quote:** "We will subsidize 50% of the seats (up to 60 seats per aircraft) to bring the price of the plane ticket down, similar to bus fares, to facilitate air transport access. The funding for all of these actions comes from the private concessions of the major national airports," said President Rousseff. The Administration will invest BRL\$ 7.3 billion in the expansion of 270 airports scattered across the country to decentralize and facilitate the flow of air passengers. Feasibility studies for 163 airports have been concluded, and engineering designs are being prepared. Bidding begins in June and will continue throughout 2014.

**Oil and Gas Bids:** Petrobras signed 41 concession contracts for blocks acquired in the 12th Round of Bidding organized by the National Agency of Petroleum, Natural Gas, and Biofuels (ANP). On Tuesday Magda Chambriard, General Director of ANP, ruled out the possibility of a new bidding round for oil and gas this year because a contract was only signed this week from the three bids conducted in 2013. As for the new pre-salt bidding rounds in the Libra fields, Chambriard said they will most likely only begin auctioning in 2016. **Quote:** "I think it is unproductive to ravage the market with huge opportunities without those opportunities being more mature," said Chambriard.

## Trade and Regulation

**Cotton Case:** The Brazilian Ministry of Foreign Affairs (MRE) scheduled a meeting with the United States Trade Representative (USTR) and United States Department of Agriculture (USDA) as part of an ongoing process to reach an agreement on the World Trade Organization (WTO) cotton case. The meeting will be held on Friday May 23<sup>rd</sup> in Washington, D.C and is one of several that have occurred between the two countries in an attempt to resolve the issue before Brazil formally requests a compliance review panel at the WTO.

**Differentiated Government Procurement Law:** Both the House and the Senate approved the original Provisional Measure ([MP](#) 630/13, sent by the Administration, which facilitates the contracting of public engineering construction projects through the Differentiated Government Procurement Law (RDC) and expands its use to prison projects. The alternative presented by Senate Rapporteur Gleisi Hoffmann (PT/PR) in her report was rejected. It would have extended RDC to any public service or construction project procured by federal, state, or municipal levels of government. Due to lack of agreement between party leaders, members of Congress chose to approve the original proposal and in turn, accelerate the processing of draft bill ([PLS](#)) 559/13, which revokes the RDC and establishes new rules for public procurement based on recommendations made by experts in public governance and representatives of the Administration and the private sector.

**Brazil-Uruguay Offshore Agreement:** Brazil and Uruguay signed an offshore naval agreement on May 16<sup>th</sup>. The objective of the agreement is to integrate the maritime industry supply chains of the two countries and extend the reciprocal recognition of local production of the shipbuilding industry to include services. The agreement was signed during the Second Plenary Meeting of the High Level Group Brazil - Uruguay (GAN), in Montevideo. The agreement does not require congressional approval. According to Heloisa Menezes, Secretary of Production Development of the Ministry of Development, Industry, and Foreign Trade (SDP/MDIC), within Mercosur, the integration agreement is second in importance only to the production supply-chain agreement on automobiles.

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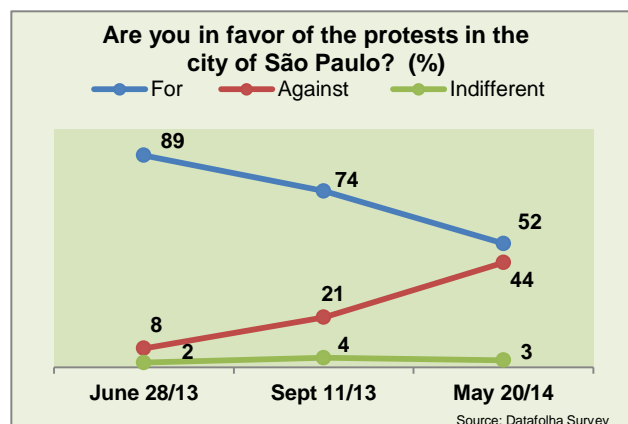


# The Pulse

With only a month until the World Cup begins, strikes and protests in Brazil are threatening to spread throughout the country as an expression of dissatisfaction with government corruption and extensive state spending on stadiums

A pressing political question facing Brazil at this moment is how widespread and serious the anticipated World Cup protests might be. In June 2013, immediately prior to the Confederations Cup – effectively a trial run of the World Cup – hundreds of thousands of Brazilians gathered in cities, catching government, politicians, the media, business, and academia by surprise. The protests reflected a broad dissatisfaction with all levels of Brazilian government, but centered on the elaborate and expensive preparations for the World Cup that stand in stark contrast to the low quality of public investment in transport, health, education, and other public services.

The demonstrations eventually subsided, diminished in part by a popular dissatisfaction with the more serious tone some of them took on, especially by violent actions by a small minority of groups (some calling themselves “black blocs”), which frightened many citizens who had joined the earlier, more peaceful demonstrations (see graph). Nonetheless, a deep popular malaise persists. Recent public opinion polls show that one-quarter of the voters are undecided about the election, are dissatisfied with the current candidate choices, and may nullify their ballots in the October presidential election (voting in Brazil is mandatory). Nearly 60% of voters say they do not identify themselves with any of the country’s more than 30 political parties.



The contrast between the high-quality stadiums and services required by FIFA (the world soccer association) and the poor conditions of buses, hospitals, and schools has catalyzed a citizenry that has become increasingly empowered politically and economically over the last 20 years, and continues to have rising expectations for social inclusion programs and better public services. As a result, public approval for hosting the World Cup has fallen from 79% in 2008, when FIFA chose Brazil, to 48% this April.

However, it is far from clear whether this collective state of mind will be reflected in the protests and demonstrations scheduled for the next few weeks. It is also not easy to predict how many strikes planned for this period will succeed and how much they will affect the image of either the World Cup or the Brazilian government. Last week’s protests were relatively small, but some degenerated into rioting, looting, and vandalism, unimpeded in those cities in the Northeast where police were on strike.

The vast majority of Brazilians thrives on soccer and disapproves of violence. Although this does not guarantee a World Cup free of serious disruptions, it may reassure many that a positive outcome can result from the tournament. This is an important point, because in the larger political picture, perceptions of the success or failure of the World Cup may be one important factor that influences the outcome of Brazil’s national elections.

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