

The Week in Review

Economic Front

Fiscal Adjustment

This week, the Senate approved three Provisional Measures (MP) that were part of the fiscal adjustment and now have 15 days to be signed into law by President Dilma Rousseff. The approved MP's are:

- » MP 668 would increase taxes on imports, thereby increasing the PIS/Pasep rates and Cofins taxes on imports. Currently the PIS average rate on imports is 1.65%, and the average COFINS rate is 7.6%. The increase would bring rates to 2.1% and 9.65%, respectively. Some products have different rates, such as cosmetics, fragrances and hygiene items, whose rates would increase from 2.2% (PIS) and 10.3% (Cofins) to 3.52% and 16.48%, respectively.
- » MP 665 would reduce employee benefits in order to cut public spending. The proposal was approved in a tight vote, 39 for and 32 against. The text reduces unemployment insurance and salary bonuses.
- » MP 664 would further restrict who can apply for death pension and sick leave benefits. The MP now requires two years of marriage or stable union before a surviving spouse is entitled to death benefits, with at least 24 months earned towards a prior contribution period. The MP also established new standards limiting the time under which a survivor is eligible to receive a pension, with younger survivors receiving less time for pension eligibility. The MP stated that for disability and sickness payments, the employer would have to pay for up to 30 days leave, instead of 15 days as is the case today,

BRL\$69.9 Billion in Expenditure Cuts

Nelson Barbosa, Minister of Planning, Budget, and Administration (*Ministro do Planejamento, Orçamento e Gestão*), announced 2015 budget reductions of BRL\$69.9 billion, the largest cut in recent years, which includes a 35.4% cut in discretionary spending. Finance Minister Joaquim Levy, although scheduled to participate in the announcement, did not make an appearance for the announcement. He had been advocating an expenditure cut between BRL\$70-80 billion.

Minister Barbosa gave no details as to which programs will be affected with the expenditure cuts, stating that each ministry must adjust its own budget. As already stated by other members of the economic team, Barbosa made it clear that adjustment measures that are not approved by Congress may be compensated for with larger cuts or new tax increases. Some information to take into consideration:

- » **Federal Tax Collection:** Even with the fiscal adjustment effort, the government revised downward by BRL\$16.3 billion forecasted revenues for 2015 because of the economy's poor performance.
- » **Bidding Round:** The 13th bidding round for oil and natural gas blocks is expected to raise BRL\$2 billion.



- » **National Broadband Plan:** This program is considered one of the priority programs and had its budget fully maintained regarding the construction and launch of geostationary satellite and the expansion of the fiber-optic network.
- » **National Plan for Exports:** Cuts will probably be announced in the second half of June.

On the Political Front

Official Visit to Mexico

On Tuesday and Wednesday, President Dilma Rousseff made the first official Brazilian state visit to Mexico. She met with President Enrique Peña Nieto, addressed the Mexican Congress, and took part in the Brazil-Mexico Business Seminar, which brought together entrepreneurs of the two countries. Mexico and Brazil aim to increase the productivity and competitiveness of each country through greater integration with Latin America. To this end, both countries believe that commercial exchange issues, productive integration, and the free movement of people and capital are essential to the entire region.

Highlights of the bilateral agenda:

- » Identify new perspectives on bilateral trade and reduce barriers to Brazilian products entering Mexico;
- » Progressively expand trade liberalization;
- » Relaunch the Binational Commission, established in 2007, which aims to deepen the dialogue and cooperation between both countries in political, economic, commercial, and financial areas.

Treaty highlights:

- » Signature of the Cooperation and Investment Facilitation Agreement (*Acordo de Cooperação e Facilitação de Investimentos - ACFI*), with the same standards as the ones Brazil already has with Mozambique and Angola, which would leverage the internationalization of Brazilian companies to offer greater security to investors in participant countries.
- » Signature of agreements in areas such as air services, environment, fisheries and aquaculture, tourism, and tropical agriculture.

Science and Technology Minister in Washington, DC

Minister of Science, Technology, and Innovation Aldo Rebelo made an official visit to the United States to participate in events and debates with the public and business sectors in Washington, DC.

On Tuesday, the delegation participated in a debate at the Center for Strategic and International Studies, which included topics on the agenda of U.S.-Brazil cooperation in areas such as energy, health, biotechnology, computational infrastructure, and internet governance. Afterwards, Rebelo met with the president of the Inter-American Development Bank, Luis Alberto Moreno.

On Wednesday, Minister Rebelo and the director of the Office of Science and Technology Policy at the White House, John Holdren, opened the Brazil-U.S. Innovation Forum hosted by the Brazil-U.S. Business Council and the U.S. Chamber of Commerce. Government representatives and Brazilian and North-American entrepreneurs discussed four major issues: "Investments in Research and Development in Brazil: Obstacles and Benefits;" "Cooperation For Innovation in Biomedicine and Health;" "Information Technologies;" and "Cooperation in the Area of Innovation." The goal of the Forum was to discuss possibilities to deepen cooperation between the two countries through projects involving the private sector.

On Thursday, the minister met with directors of the Smithsonian Museum and American Aerospace Agency representatives. The purpose of the meeting was to discuss cooperation on programs in the area of science education such as mathematics and engineering.



Political Reform

On Tuesday, a proposed amendment to the constitution (PEC) 182/2007 aimed at reforming the political system in Brazil was voted on by the House floor. Several matters were discussed, among them the way in which legislators are elected, the financing model of political campaigns, and reelections.

- » The political reform bill would establish a majority voting system, so-called *distritão*, which would affect how most candidates for the House of Representatives and council members would be elected. This direct voting system was rejected by a large margin in the House, with 210 favorable votes (when the minimum to approve a proposed amendment to the constitution is at least 308 votes or 60% of all representatives). As such, the current proportional voting system was maintained. This was a big loss to the Speaker of the House, Representative Eduardo Cunha (PMDB/RJ), since he is a big advocate of the majority voting election model.
- » Another issue discussed was the private financing of political campaigns, which was rejected at first, then was approved on Wednesday with 330 favorable votes. Currently, campaign funding is mixed, with both public and private financing.
- » The House also approved the end of re-election for president, governor, and mayor, with 452 votes for and 19 against. Thus, the current rules will be valid for mayors elected in 2016 and for the president and governors-elect in 2018. Namely, those who were elected in 2012 and 2014 and are not serving a consecutive second term may still seek re-election in 2016 or 2018.

To be approved, the proposed amendment to the constitution still has to go through a second round of voting in the House, and after that, by the Senate, where it also needs 60% of the votes in order to pass. House speaker, Eduardo Cunha has already said that no other issue will be voted on in the House until they complete the Political Reform session.

Priority Agenda for the Congress

Speaker of the House Eduardo Cunha (PMDB/RJ), and Senate President Renan Calheiros (PMDB/AL), announced this week a priority agenda for the two houses.

Highlights include:

- » **PLP 37/15** would rule on the state debt index;
- » **PLS 86/12** would reduce to zero the PIS/PASEP tax on revenue received by states and municipalities, including those transferred from the federal government;
- » **PRS 15/15** would anticipate of revenue arising from oil and natural gas exploration by states and municipalities;
- » **PLS 312/13** would establish the criteria to be used for calculating the transfer to be made by the federal government to the states as compensation for loss of revenue sharing resulting from the elimination promoted by the Kandir Law (which exempts from ICMS the products and services to be exported);
- » **PRS 1/2013** would rule on the unification of the ICMS tax rate at 7% or 4%. Currently, the biggest impasse for the completion of the ICMS reform is the creation of state compensation funds.
- » **PLP 54/15** would rule on the validation of ICMS tax incentives.

Petrobras

The former director of Petrobras' international division, Nestor Cerveró, was sentenced to five years in prison for money laundering. The decision was made in the first instance on Tuesday by federal Judge Sergio Moro, the judge responsible for ruling on the Car Wash Operation case. This is Cerveró's first conviction. He is also a defendant in another criminal case and is already in jail in Curitiba, waiting trial. According to the complaint made by the Federal Public Ministry (MPF), Cerveró unlawfully acquired a luxury apartment in Rio de Janeiro with money he received as a bribe while at Petrobras, a charge which is being investigated in another court case.



Senate Soccer Probe

On Thursday, the Senate approved the creation of a Parliamentary Investigation Commission (CPI) to investigate the scandal that resulted in the arrest of seven FIFA leaders including the former president of the CBF José Maria Marin, who is suspected of corruption, money laundering, and extortion in commercial schemes involving competitions like the *Copa America*, *Libertadores*, and *Copa do Brasil*. The CPI should be published on Friday in the Senate Gazette if none of the 26 senators withdraw their signatures from the request form. The request to open a CPI was made by former soccer player and now-Senator Romario Faria (PSB-RJ), who intends to investigate potential misconduct surrounding the World Cup held in Brazil in 2014.

Task Forces

Innovation

Exploration Rights to Brazilian Satellite: On Tuesday, Anatel held the auction for exploration rights to a Brazilian satellite, which will be used for a 15-year period with the possibility of a one-time extension for the same period. The auction's objective is to increase the availability of satellite capacity in Brazilian territory and to ensure the transport of telecommunication signals. The following companies won the bid:

- » Eutelsat do Brasil Ltda., part of the French company *European Telecommunications Satellite Organization*
- » Hispamar Satélites S.A., a Spanish company that holds 20% of the Brazilian telecom company *Oi*
- » Star Satellite Communications Company, a United Arab Emirates company
- » Telesat Brasil Capacidade de Satélites Ltda., a Canadian firm

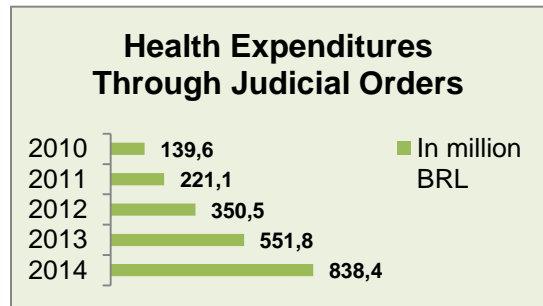
Defense & Security

International Treaties: [Bill 62/15](#), which would ratify text of the Treaty for the Establishment of the Quota Arrangement for BRICS Reserves (*Tratado para o Estabelecimento do Arranjo Contingente de Reservas dos BRICS*), and [Bill 63/15](#), which would approve the text of the agreement on the New Development Bank (*Novo Banco de Desenvolvimento - NBD*), were approved on the House Floor and will now be sent to the Senate. Expectations are that the treaties will be in force by June 8th, when there will be a meeting of BRICS legislators in Moscow.

Healthcare

Second Judicial Health Journey: Last week, the second Journey of Health Law, held by the National Justice Council (*Conselho Nacional de Justiça - CNJ*), approved 23 basic guidelines with technical information that will provide input for the judges when making decisions in lawsuits about rights to healthcare. Among the guidelines highlighted is one that rules on the requests for medicine, prostheses, or non-standard procedures by the Ministry of Health. In these cases, the guideline recommends the subpoena of the physician responsible for the patient so that they can provide information on the relevance and need of the non-standard procedures. The physician must also sign a statement declaring if there is a conflict between his professional and other interests, whether personal, commercial, or financial. Still concerning public health, a guideline was approved prohibiting the granting of injunctions to authorize access to medicines and materials not registered by the National Health Surveillance Agency (*Agência Nacional de Vigilância Sanitária - ANVISA*) or for off-label use (medicines approved by ANVISA, but which are used in ways other than those described in the package insert). All listed guidelines can be found [here](#).

According to CNJ, in June 2014, there were 392,921 lawsuits with requests for medicine, treatments, hospital beds, among others. According to data released by the Ministry of Health, federal and state administrations spent BRL\$ 314 million in health products and medicine not registered at ANVISA. Another common situation is requests for medicines that are already marketed in the country but which do not appear in the list of drugs supplied by public administration.



The Pulse

Fiscal Adjustment Faces Political and Economic Resistance: What Lies Ahead?

Most analysts knew from the start that Finance Minister Joaquim Levy's fiscal adjustment plan would face difficult political and economic resistance and therefore be difficult to implement in its entirety. Nonetheless, even though expectations were cautious regarding achieving the key target of a primary budget surplus equal to 1.2% of GDP, many believed that something close to a 1.0% goal was manageable and would still send a positive signal to the markets and investors.

After the intense opposition Minister Levy has received in recent weeks, including from those at the core of President Rousseff's Worker's Party (PT), it seems increasingly clear that the 2015 fiscal adjustment may prove to be disappointing. Expenditure cuts have been smaller than expected, and government priorities have not shifted to align with the need for long-term economic growth: it has been politically expedient to slash investments far more than current expenditures, for example.

Given the now expected shortfall in reaching the budget targets, it should be no surprise that by July or August, Minister Levy may propose more tax increases to sharpen the revenue side given a political environment that does not support reducing expenses further. Another option would be to attract private investment in order to create jobs and accelerate economic growth, which would also boost revenue. Investor confidence in the Rousseff Administration, however, is lacking, in part because it has not sent the necessary strong message of resolve needed to reassure investors.

In fact, the government is sending mixed messages to investors. In a recent meeting with oil producers in Texas, for example, Minister Eduardo Braga suggested that the sector could count on the government reducing protectionist/nationalist policies, only to be contradicted by President Rousseff a few days later. Last week's friction between Finance Minister Levy and Planning Minister Nelson Barbosa was another example of a major discrepancy in messaging. The source of Brazil's problems resides less with Congress, as many believe, given its own internal turmoil, and more with the Planalto, which has not been able to convince the markets that the economic crisis is being adequately addressed.

As a result, markets have reacted negatively again. Those economic indicators that were improving in recent weeks (e.g., exchange rate exchange, stock exchange, inflation expectations), have worsened, albeit only slightly. Nonetheless, a turnaround seems a distant hope still, and it may not be until August or September that it will be possible to have a clearer perspective of what lies ahead.

BRASÍLIA
SAF Sul Quadra 02, Lote 04.
Edifício Via Esplanada
Salas 103 a 106

CEP 70070-600
Fone: (61) 3327-2606
Fax: (61) 3327-1619

SÃO PAULO
Rua Olimpiadas, 134, 5º andar, Cj 52.
Condomínio Alpha Tower
Vila Olímpia

CEP 04551-000
Fone: (11) 3079-4533
Fax: (11) 3079-2202

WASHINGTON, DC
1101 17th St.
NW Suite 1010

Phone: (202) 822-6420
Fax: (202) 822-6423
www.patri.com.br
relgov@patri.com.br

