

# The Week in Review

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## On the Economic Front

### Fiscal Target

On Wednesday President Dilma Rousseff decided to lower the primary surplus target to BRL\$8.7 billion (0.15% of GDP) from the original target of BRL\$66.3 billion (1.1% of GDP). The government also announced an additional spending cut of BRL\$8.6 billion this year. Finance Minister Joaquim Levy said the government was not abandoning fiscal discipline but was unable to meet revenue targets. (See *The Pulse* below)

## On the Political Front

### Parliamentary Investigation Commissions Created

House Speaker Eduardo Cunha created three new Parliamentary Investigation Commissions (CPI). The first will investigate loans from the National Bank for Economic and Social Development (BNDES); the second will investigate mistreatment of animals; and the third will investigate cybercrimes in the country. Cunha also authorized the creation of a fourth CPI, to investigate alleged irregularities in the state pension funds, which will take place after August 7<sup>th</sup>, when the CPI on prison systems concludes. Only five CPIs can be open at any given time. The fifth CPI currently open is investigating the Petrobras “kickback” scandal.

### Vice President Makes Visit to U.S.

Vice President Michel Temer, also national president of the PMDB party and the head of President Rousseff’s relations with Congress, held talks this week with local businesses in New York on the political and economic scenario of Brazil. The trip happened less than a month after President Rousseff made her official visit to the United States, where she participated in negotiations with President Barack Obama and also met with entrepreneurs and foreign investors.

### House Speaker Splits with Government

House Speaker Eduardo Cunha announced last week that he would withdraw his support for President Rousseff because of differences over the Petrobras corruption probe. His loss of support could result in a setback to her legislative agenda at a critical time in Brazil’s history. Eduardo Cunha blamed Rousseff’s administration for involving him in the scandal, which has engulfed some of Brazil’s most important political and business leaders, including members of the president’s own Workers’ Party. Rousseff has not been implicated in the scandal and her party leadership has repeatedly denied wrongdoing.



# Task Forces

## Trade

**Employment Protection Program:** The Ministry of Labor's Committee on the Employment Protection Program (PCAP) released the rules and procedures required of companies in financial difficulty in order to participate in the employment protection program (EPP). The EPP is available to all industries and companies of all sizes. Created on June 7<sup>th</sup> by Provisional Measure 680 (Medida Provisória – MP), the EPP allows companies in financial distress to reduce the number of hours worked by employees by up to 30%, with a proportional reduction in wages, for a period of up to one year. Under the rules of the program, companies must:

- » Ensure that employees have used all of their vacation periods and received overtime;
- » Sign a specific collective agreement with employees, providing for the reduction of hours and salary;
- » Demonstrate that the company has economic and financial difficulties. Their Net Employment Indicator (ILE)—the difference between admissions and dismissals—must be equal to or less than 1%.
- » After all these requirements have been gathered, the applicant must file the request with the Ministry of Labor electronically at the MTE official site. A copy of the document, as well as the ratio of workers included in the program, must be sent to the ministry with submission of the form.

## Tax & Investment

**Tax Litigation Reduction Program:** The Executive Branch issued Provisional Measure 685/2015, which creates the Tax Litigation Reduction Program (PRORELIT). Through the program, companies who have tax debt as of June 30<sup>th</sup>, 2015 and have related administrative or litigation issues may use credits from tax losses and negative base on social contribution calculated until December 31, 2013 and declared until June 30, 2015. For this, the company must decline to continue with the litigation in progress and submit a request by September 30<sup>th</sup>, which will be considered an extrajudicial session. To join the program, companies must pay in cash a minimum of 43% of the consolidated amount of debt.

# The Pulse

## Reduced Primary Surplus Targets Signal a Failure in Fiscal Adjustment

The announcement by the Rousseff Administration this Wednesday that even its much-reduced 2015 primary surplus target of 0.15% may not be achievable means that Finance Minister Joaquim Levy's fiscal adjustment plan has effectively failed, and that the economic recovery may be delayed, possibly until 2018. The ambitious 1.19% primary surplus goal set in January by the incoming Levy raised hope that Brazil could find its way back to economic growth by 2016, or 2017 at the latest. However, four key factors frustrated the plan: 1) federal public accounts at the close of 2014 turned out to be far worse than originally thought; 2) the recession caused a much larger shortfall in federal revenue than anticipated; 3) Congress and the administration failed to pass or enact all of Minister Levy's proposed adjustment measures, and; 4) the government failed to cut expenditures sufficiently.

In conceding to the lower primary surplus targets, Minister Levy has lost his duel with Planning Minister Nelson Barbosa. The revised targets are: 0.15% for 2015 (with a band allowing for a primary deficit); 0.7% for 2016 (which only a few weeks ago was considered the minimum for 2015); 1.3% for 2017 and 2.0% for 2018 (which is widely viewed as the minimum effort required to reduce the public debt to GDP ratio). Further, many expect a prolonged and deeper recession given that public revenue and economic growth will suffer from planned federal budget cuts falling heavily on public investment and decreased confidence in the economy likely to diminish consumer spending.

Although the government is still trying to generate revenue with some one-off measures that will be sent to Congress (such as an amnesty program that would encourage—and tax—the repatriation of money sent abroad illegally), it is unclear how much revenue these measures can generate or if Congress will even support them. The consequences are potentially severe: a downgrade of the country's investment grade rating, an



increase in the already high level of public debt, further political weakening and isolation of President Rousseff, and increasing dissatisfaction by the Brazilian people, as seen in the planned mass protests for August 16<sup>th</sup>.

In an attempt to muster a broader range of political forces to address Brazil's increasingly dire economic situation, former President Lula has shown some disposition to establish a dialogue with his predecessor, and former political adversary, Fernando Henrique Cardoso. The two are still the most important political leaders in Brazil, and should they decide to work together, chances would improve for a unified outcome that would allow the difficult choices to be made that are necessary for Brazil to work its way out of a challenging and potentially volatile situation.

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