Brazil-U.S. Business Council

PATRI

POLICY MONITOR

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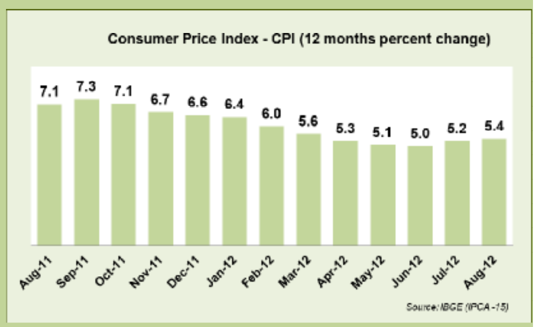
THE WEEK IN REVIEW

On the economic front, the highlight of the week came from Jorge Gerdau, a well-respected Brazilian businessman who also heads the Rousseff administration's Board of Policy Management, a body created to increase the efficiency of federal public administration. **According to Gerdau, the government should soon simplify the PIS and Cofins (social security contributions) collection, benefiting the private sector.** The tax simplification will probably start in the financial industry. Gerdau also criticized the IOF (tax on financial transactions), signaling it could be either reduced or eliminated. The administration also indicated it will send a pension reform proposal to Congress after the October mayoral elections. The Minister of Communications Paulo Bernardo announced that the government will move forward the bidding round for 4G frequencies (700 MHz) for the second semester of 2013, enabling the telecommunications industry to transition from analog TV to digital. Meanwhile, IBGE (statistics agency) reported that **IPCA (inflation index) rose 0.39% in August over 0.33% in July**, due to higher food and services costs. In the 12 months through mid-August IPCA rose to 5.37%. On another note, Marcelo Neri, the creator of the concept of the "new middle class" was confirmed as the new president of IPEA, the most important Brazilian research institute.

On the political front, **after weeks of negotiations with federal employees on strike for wage increases, the administration struck a deal with federal university professors.** Although key agencies such as Anvisa (health regulator) were still affected as of Friday 24th, the movement has shown signs of waning and is likely to end soon due to the government's decision to dock workers' pay for each day on strike. The government also indicated it will send a proposal to Congress to regulate the right for public employees to strike. Meanwhile, the political campaign for the mayoral elections started officially on radio and TV. Former President Luiz Inácio Lula da Silva is back in the spotlight, campaigning for PT (Labor Party) candidates.



Below, key policies that were tracked by PATRI during the week.

Tax & Investment

New Strategic Program for Software and IT Services

Overview

MCTI (Ministry of Science, Technology and Innovation) launched the new Strategic Program for Software and IT Services, a BRL$ 486 million (US$ 243 million) program (known in Portuguese as "*TI Maior*") to boost the sector in the country via credit lines, tax waivers, training grants, infrastructure improvement, and investments in research and development. Last year, the sector in Brazil was comprised of approximately 73,000 companies that earned US$ 37 billion. The program will be in effect from 2012 to 2015 and is divided into five pillars: economic and social development; international positioning; innovation and entrepreneurship; scientific and technological production; and competitiveness. The main measures include:

- **Start-ups:** accelerate the development of technology-based start-ups through a structured network of mentors and investors, funding for R&D, technology and market consulting, and preference with government contracts. The goal is to create 150 start-ups by 2014.
- **CERTICS (National Technology Software and Services Certification):** enable the creation of a procedure to evaluate the quality of Brazilian software.
- **Digital Ecosystems:** promote the integration of software and IT services sectors in strategic areas such as education, defense and cyber security, healthcare, oil and gas, energy, aerospace/aeronautics, major sporting events, agriculture and environment, finance, telecommunications, mining, and strategic technologies such as cloud computing and internet.
- **Education:** create a digital network platform through technical courses and training activities (*Sistema S* and Telecenters).
- **Attraction of Global R&D Centers:** promote research grants, consult global Brazilian and foreign companies R&D centers, give fiscal and tax benefits, and encourage partnerships with the *Sala Inovação,* a government channel to negotiate and develop innovation projects in the industrial sector.
- **Market Intelligence:** create a program in collaboration with the private sector to enable the development of research and reports for different target audiences (IT, Software, and Emerging Technologies, among others).
- **Integrated Investment Funds:** combine programs that support and promote RD&I and investment funds such as FINEP.
- **International Hubs:** offer services to Brazilian IT companies seeking an international presence or foreign companies with commercial and investment interests in Brazil.
- **Competitive Regulatory Framework:** build an agenda with measures to promote the sector and to improve Brazilian legislation, such as the *Lei de Informática*, *Lei do Bem*, and the implementation of a law on personal data protection.

An important goal of this program is the participation of Brazilian and foreign companies in its implementation. For more details on the program, click here.

Land Acquisition by Foreigners

Overview

A new favorable opinion was given on a Substitute for PL 2289/07, which regulates the acquisition and leasing of rural areas by foreigners, adapting to the material of PL 4059/12, which originated in the report of the Subcommittee on Land Acquisition by Foreigners (SUBESTRA) approved by CAPADR (House Committee on Agriculture, Livestock, Supply and Rural Development). The differences between PL 4059/12 and the Substitute presented are:

PL 4059/12	Substitute
Article 2. The rural property acquired by a **foreign company in the country** shall follow the principles of the social function of property and must be expressly authorized by the executive branch as determined by Article 1134 of Law No. 10.406, of January 10, 2002.	Article 2. The rural property acquired by **Brazilian legal entities, regardless of whether they are incorporated or controlled directly or indirectly by foreign private individuals or companies, should be associated with an agro-industrial project that adds value, generates income and employment for the region**, and which conforms to the principles of social function property and must be expressly authorized by the executive branch as determined by art. 1134 Law No. 10.406, of January 10, 2002.
Article 12. Congress may, by legislative decree, by previous manifestation of the executive branch, authorize the acquisition of property by **foreign persons**, beyond the limits specified in this Act, in the case of implementing priority projects judged in light of	Article 12. Congress may, by legislative decree, by previous manifestation of the executive branch, authorize the acquisition of property by **Brazilian legal entities, regardless of whether they are incorporated or controlled directly or**

the development plans of the country.	**indirectly by foreign private individuals or companies,** beyond the limits established by this Law, when dealing with the implementation of an **agro-industrial project that adds value, generates income and employment to the region,** and is considered a priority in light of the development plans of the country.

The Substitute had similar content to the original PL 2289/07. Following are some of the changes that were made:

- Those subject to the law shall include Brazilian legal entities in which a foreign private individual or company participates and Brazilian legal entities for which the majority of capital shares are held or authority is exercised by foreigners;
- The restrictions set forth in the bill apply only to cases where the rural property is offered as collateral for a loan contracted with financial institutions that are controlled by foreign capital in the event of permanent transfer, judicially or extrajudicially, of the property;
- Prohibits lease terms exceeding 10 years, as well as the total or partial sublease of rural property by a foreign individual.

Next Steps

CAPADR has to vote on the bill, which is scheduled for September 5th. The bill still has to be approved by CFT (Committee on Finance and Taxation) and CCJC (Committee on Constitution and Justice).

Amendments to Procurement Law

Overview

99 amendments were presented to MP 575/12, which changes Law 11.079/04 on bidding regulations for the establishment of public-private partnerships (PPP). The goal is to reduce bureaucracy and investment risks, making it more attractive to the private sector. In general, the amendments deal with the taxation of resources offered to private entities by government and the percentage of current revenue that states and municipalities can exceed through PPPs.

Next Steps

A Joint Committee, which still has to be installed, will evaluate the measure on August 29th.

Agroecology and Organic Production Policy

Overview

MAPA (Ministry of Agriculture, Livestock and Supply) instituted the National Agroecology and Organic Production Policy (Pnapo) with the goal to integrate, coordinate, and adapt policies, programs, and activities that contribute to sustainable development and quality of life through the sustainable use of natural resources. Measures for the development of sustainable agricultural practices were being evaluated by the group since 2010. Issues that will be observed by the group include: government procurement, rural credit, fiscal and tax benefits, technical assistance, education and others.

Trade Facilitation

Tariff Reduction for Capital, Informatics and Telecom Goods

Overview

Camex (Foreign Trade Council) announced the extension of tariff reductions of 530 goods until December 31, 2014. The new duty will be 2%. These items include capital, informatics and telecom goods with no national equivalent. According to Camex the import of these goods amount to $1.6 billion and nearly one-third of the products come from the United States.

Editor's Note

Amaury de Souza

PATRI and the Brazil-U.S. Business Council mourn the passing of a friend to both organizations and an influential political analyst. He will be remembered for his exceptional work in the academic, economic and political analysis areas, as well as his books on Brazilian issues.

THE PULSE

MEXICO MAY OUTPERFORM BRAZIL WITHIN THE DECADE

Who is Latin America´s true economic champion? **Since the *Financial Times* hinted that "Mexico is the new Brazil, and Brazil the old Mexico" three weeks ago, the old rivalry reemerged between the two largest economies below the Rio Grande.** The fact that Mexico won the soccer gold medal against Brazil in the London Olympics has added some heat to the headlines. Given the current Brazilian slowdown and Mexican recovery, Brazil´s GDP will probably grow only 1.8% in 2012, while Mexico's is likely to grow 3.8%. As for inflation, Mexico is also in better shape with a projected 3.8% rate in 2012, while inflation in Brazil is likely to amount to 5.1%. Analysts say that if this trend persists, Mexico could outperform Brazil and become Latin America's largest economy by 2020.

Not so fast, argues Brazilian business magazine *Exame*, citing indicators that favor Brazil. First, the country's stock market, valued at US$1.1 trillion, stomps Mexico's US$509 billion market. In 2011, Brazil's GDP of US$2.4 trillion was more than double Mexico's (US$1.1 trillion). When you look at the size of the workforce in each country, Brazil's 105 million people in the labor market is more than double Mexico's 49 million people. Brazil's consumption market, at US$1.4 trillion also dwarfs Mexico's, at US$ 700 billion. Brazil also wins in terms of exports. Despite Brazil's vulnerability to China's purchases of mineral and agriculture commodities, Brazil has a more diversified export base. As its major buyer, the European Union absorbs 21% of Brazilian exports, while the other BRICs combined represent 20%. In turn, Mexico sells 72% of its exports to the United States. **Moreover, besides being bigger, Brazil is also more politically stable than Mexico. However, in order to sustain growth, Brazil needs to reduce red tape and pass reforms to modernize its tax and labor systems. This is challenging, but not impossible.** To sum it up, Brazilians are more worried today about the poor quality of its soccer team than Mexico.

Main Economic Indicators (2011)	BRAZIL	MEXICO
GDP (US$ bn – Purchasing Power Parity)	2.324	1.683
GDP Ranking	8th	12th
GDP per capita (Purchasing Power Parity)	11,900	14,800
Public Debt (% GDP)	54.4%	37.5%
Inflation Rate (Consumer Prices)	6.5%	3.5%
Trade Balance (US$ bi)	29.8	-1.16
Foreign Exchange and Gold Reserves (US$ bi)	357.9	142
Real GDP Projections	3.0 (2012) 4.1 (2013)	3.6 (2012) 3.7 (2013)

Sources: IMF, INEGI, MDIC