TIME FOR A ROUTE CORRECTION

With performance less than is necessary to meet Brazil’s infrastructure demands and with funding scarce, investment needs to become more efficient.
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Address
Rua Barão de Itambi, 60
Botafogo – CEP 22231-000
Rio de Janeiro – RJ – Brazil
Phone: 55(21)3799-6840
Email: ibre@fgv.br
Web site: http://portalibre.fgv.br/

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The Ifo / FGV Economic Climate in Latin America indicator (ICE) has been headed downward since April 2013, but Mexico is doing better and Brazil and Argentina are doing worse. According to Lia Valls Pereira Baker, Brazil’s backtracking reflects both a lack of confidence in government policies and a loss of international competitiveness.
**ECONOMY**

**Current account deficit up again**
Brazil posted a current account deficit of US$6.0 billion in July, the central bank said Friday, almost double the June deficit of US$3.3 billion. The cumulative 12-month deficit through July totaled US$78.39 billion, 3.45% of Brazil’s GDP. However, foreign direct investment went up from US$3.9 billion in June to US$5.9 billion, for a 12-month total of US$64 billion. (August 22)

**Brazil now in technical recession**
Second-quarter economic output, GDP, fell by 0.6%, worse than analysts expected, and revised figures for the first quarter now show a fall of 0.2%. A recession is usually defined as two consecutive quarters of contraction. (August 29)

**Industrial output snaps five-month slump**
Brazilian industrial output rose slightly in July after five months of declines. Output at factories and mines rose a seasonally adjusted 0.7 percent, government statistics agency IBGE said. Production had fallen 1.4% in June from May, partly due to the World Cup. Capital goods production jumped 16.7% in July, and intermediate goods such as textiles and chemicals retreated 0.3%. Durable consumer goods, such as furniture and home appliances, rose 20.3%. However, July production was down 3.6% from July 2013. (October 2)

**Inflation accelerated in August**
The monthly inflation rate picked up speed in August, breaching the upper limit of the central bank target range of 2.5–6.5%. Consumer prices rose 0.25% in August after going up only 0.01% in July; 12-month inflation edged up to 6.51% from 6.50% in July. The main culprit for August inflation was higher electricity rates in many cities. (September 5)

**ECONOMIC POLICY**

**Central government has record July deficit**
Despite government promises to improve the fiscal balance, the National Treasury reports the central government ended July with a record deficit of R$2.2 billion—the worst performance for the month in 17 years. The surplus for January through July of R$15.2 billion, 0.52% of GDP, was down 60% from the same period last year. (August 29)

**Policy rate unchanged at 11%**
As expected, the central bank Monetary Policy Committee voted unanimously to keep the policy interest rate at 11%. The October presidential elections may have been a factor in retaining the interest rate; the central bank governor usually changes when a new government takes office. (September 3)

**THE 2014 ELECTION**

**Candidate’s death shakes presidential campaign**
Former governor of Pernambuco and presidential candidate Eduardo Campos died in a plane crash on August 14 at the coastal city of Santos. The death, which occurred barely 50 days before the elections, may change the outcome of elections and the future of the economy. Brazilians mourned the death of Mr. Campos—grandson of a famous leftist politician, Miguel Arraes—who promised a new way to do politics and a more inclusive society.

The centre-left PSB party asked Marina Silva, Mr. Campos’s running mate, to take over as candidate. Analysts believe she may have a better chance of unseating President Dilma Rousseff. However, as a principled environmentalist and a staunch evangelical, Ms. Silva may struggle to win over the country’s powerful farming lobby. Although she is committed to macroeconomic stability, she has as yet said little about her likely economic policies.

Unlike Mr. Campos, former governor of the north-eastern state of Pernambuco who was just becoming known nationally, Ms. Silva already has wide support after coming third in Brazil’s 2010 elections with almost 20% of the vote. She will probably take votes away from Ms. Rousseff, but also have enough backing to knock pro-business centrist Aécio Neves out of the election in the first round. (August 14)

**Neves says his team has “more experience”**
Launching his program for the Northeast region in Salvador city, presidential candidate Aécio Neves (PSDB) touted the experience of his advisors and sought to position himself as a safe option to the PT government. “We have a number of projects discussed widely with the
population that are best for Brazil. Nobody has a more qualified team to execute them so that Brazil can dream of a better future," he said. Asked about the PSB candidate, Neves said he has "great respect for Marina Silva," but he is convinced that his proposals "are better." (August 23)

**Rousseff and Neves slam Silva**

Seeking reelection, Dilma Rousseff (PT) went on direct attack, saying that Marina Silva (Brazilian Socialist Party, PSB) wants to "reduce to dust" the country’s industrial policy. Rousseff also warned that Silva intends to "end the role of the National Development Bank (BNDES)." (September 2)

Meanwhile, Aécio Neves denied rumors that he would drop out of the race and also took the fight to Silva. With former president Fernando Henrique Cardoso beside him, the Brazilian Social Democratic Party (PSDB) candidate said he has "full confidence" that he will make it to the runoff. The press conference also marked a change in tone for his campaign: "Brazil needs to know the real convictions of Marina Silva," he said. Neves accused Silva of having voted against the fiscal responsibility law when she was in Congress. (September 2)

**Rousseff recognizes need for change**

In an effort to neutralize calls for change from campaign opponents, President Rousseff (PT) said in Belo Horizonte city that she will "update policies" and "teams" in a possible second term. This is the first time she has promised changes if re-elected—until now she has left unanswered questions about possible management mistakes in her first term. (September 3)

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**Polls show Silva winning**

According to two polls published in early September, Marina Silva (PSB) would defeat President Dilma Rousseff (PT) in second-round voting in October. In the first round the Ibope poll projects Rousseff getting 37% of the vote, Silva 33%, and Aécio Neves (PSDB) 15%. In the runoff on October 26, Silva would win 46% to 39%. Polling company Datafolha projected first-round shares of 35% for Rousseff, 34% for Silva, and 14% for Neves, and Silva winning the runoff 48% to 41%. (September 3)

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**Oil scandal blows up as election nears**

A scandal involving the state-controlled oil giant Petrobras flared up again over testimony that implicated dozens of top figures in President Dilma Rousseff’s governing coalition in a vast kickback scheme. In a confidential plea deal with prosecutors, a former executive of Petrobras, Paulo Roberto Costa revealed details about the operation, which involved the overbilling of contracts for oil projects and distribution of benefits among officials and politicians. (September 8)
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A LITTLE OVER SEVEN YEARS AGO, Brazilians welcomed the Growth Acceleration Program (PAC). After years of neglect it was a beacon of hope that Brazil’s infrastructure would no longer be neglected. There was hope of reducing the cost of getting Brazilian products to foreign markets, of making our products competitive around the world, of making life easier for the suffering people in Brazilian cities.

Did any of these things happen? Not noticeably. It still costs a Brazilian manufacturer four or five times as much to get a product to market as it costs a South Korean manufacturer. And last year ordinary Brazilians hit the streets to protest about the high costs of simply getting themselves to work.

On average, investments in infrastructure were just above 2% of GDP; it will take twice that much to make up for years of neglect, and more again to catch up with new demand. Last year, 2.4% of GDP was invested in infrastructure; this year only 2.5% is budgeted.

The PAC failed to revive infrastructure because the government took far too long to call in the private sector and grant concessions for roads, railways, and ports. Most PAC money went to social housing programs, and the government was able to spend only part of what was intended for transport.

In 2012 the government finally had a change of heart. Recognizing that the public sector was unable to carry out large projects efficiently, the president launched an ambitious program of infrastructure concessions.

Perhaps not ambitious enough, though. A major problem related to investments in infrastructure is the abysmal inefficiency of the public sector in using budgeted resources. Between 2003 and 2013, it failed to use about US$35 billion of funds authorized for transportation.

Even the president has conceded that she will have to make adjustments in her policies and her team if she is elected to a second term, so there may be hope again. But it will take very significant changes if Brazil’s people and businesses are to get the infrastructure they need and deserve. It will take a comprehensive restructuring of how public works are planned and how they are executed—how projects are assessed and chosen, how to ensure that budgeted resources are used efficiently. Not only must the responsibilities of federal agencies to streamline projects be clarified, regulatory agencies must also be strengthened, and their performance monitored.

With the presidential elections fast approaching, we believe all candidates recognize that raising fixed investment in general and infrastructure investment in particular is critical to increase productivity and growth. Whoever is elected will need to carry out reforms to speed projects, raise productivity, and improve the business environment.

Brazil still has remarkable strengths, especially a sophisticated and resourceful business community and pockets of innovation excellence. The next president should take full advantage of these strengths to pull the country out of the current doldrums and get infrastructure investment back on track.

Whoever is elected will need to carry out reforms to speed projects, raise productivity, and improve the business environment.
THE 2014 ELECTIONS

Brazil’s third way

João Augusto de Castro Neves

THE DRAMATIC EVENTS OF the past few weeks warrant a slight change to the title of last month’s column, Brazil’s third way? The tragic passing of Eduardo Campos and his replacement by Marina Silva adds more uncertainty to the presidential race and certainly raises the odds of a third party success, which would splinter the two-decade-old hegemony of the Workers’ Party (PT) and the Brazilian Social Democratic Party (PSDB). Last month’s title, then, could very well stand without a question mark.

The Marina Silva candidacy of the Brazilian Socialist Party (PSB) undoubtedly represents a significant inflexion point in Brazil’s political landscape. As she transitions from a protest vote candidate to someone who could prove to be a leader, Silva brings to the center of the campaign the diffuse sentiment for change that has swept Brazilian cities since last year’s protests. The transition, however, is far from trivial: some of the attributes needed to gain trust from broader segments of society may clash with those that make her somewhat of an archetype of the “new politics” she advocates.

Silva’s green credentials, for example, have generated significant animosity within the agribusiness sector in the past and also raised industry concerns about more rigid environmental licensing for infrastructure projects. Her decision to invite Beto Albuquerque (PSB) to be the vice-presidential candidate is a good sign. He has ties with agribusiness, and her advisers are clearly seeking to make a statement that her government would look to the private sector to boost investments. Nevertheless, she has a long track record of endorsing stringent environmental licensing to the detriment of such investment projects as hydropower in the Amazon, which raises questions about whether she can fully win over the industrial sector.

Additional dilemmas became clear after the release of her platform. The platform did give clear indications that if she is elected, castroneves@eurasiagroup.net
Silva’s economic team will be market-friendly and look to manage the economy better. The document signals the return to the three legs of macroeconomic management implemented by Fernando Henrique Cardoso and continued through most of Luiz Inacio Lula da Silva’s two terms in office: fiscal discipline, inflation targeting, and a free-floating exchange rate.

But ambitious promises to expand social programs raise questions about fiscal policy under a Silva administration. The fiscal cost of these programs certainly suggests that if elected, she will have to roll back many of these commitments. The promises suggest two possibilities: Either her campaign allowed some of the proposals to be made public without due vetting by her economic advisors. Or her own commitment to fiscal austerity doesn’t run that deep. At a minimum, the fact that Silva is making specific promises in sectors like health and education, subjects on which legislators are highly organized, means she is creating a potential political problem for her administration after the election.

It is in the political realm, in fact, that Silva’s greatest liabilities lie. The same features that make her a very competitive candidate make her a potentially dangerous president. By listing “High Intensity Democracy” as its first pillar to tackle, her platform reinforces the perception that she is convinced of the need to “renew” politics and establish governance on new grounds. In practice, that means she is opposed to engaging in the traditional means of constructing congressional majorities in Brazil’s multi-party presidential democracy by distributing cabinet posts to parties in Congress to lock in support.

The same features that make Silva a very competitive candidate make her a potentially dangerous president.

The platform, moreover, suggests that political reform will be front and center on her agenda after the election. She would eliminate the ability of elected executive office holders to run for reelection, extend the 4-year presidential term to 5 years, introduce public funding of campaigns, and generally implement reforms that could weaken political parties. The platform is also heavy on introducing elements of “direct” democracy, such as more frequent use of plebiscites and referendum.

Needless to say, the odds that her administration will become mired in a difficult political reform with low chances of approval loom very large. Given her unwillingness to negotiate support with parties in the “traditional” way, at a time when difficult economic adjustments should come, getting reforms through without a disciplined congressional base of support won’t be easy. Even though Silva is calling for tax reform, placing a premium on political reform makes the former unlikely to make headway.

The last two presidents who attempted to ignore or change the rules of the game of coalition-building were either impeached (Fernando Collor in 1992) or faced a major political crisis (Lula’s first-term vote-buying scandal).
IS BRAZIL REALLY “AN UNREFORMED LEVIATHAN”?  

In his new book, Brazil: The Troubled Rise of a Global Power, long-time The Economist writer Michael Reid picks out economic, social, and cultural threads from the past that still color the governance of Brazil today.

Anne Grant

Michael Reid, whose previous book was the 2007 Forgotten Continent: The Battle for Latin America’s Soul, lived in Brazil from 1996 to 1999 and still returns regularly from his base in Lima. As is clear from the numerous notes in Brazil,* he also does his homework.

Reid sees the country’s roots, its achievements, its promise, and its contradictions. In Part I, which covers Brazil’s early history, for instance, he notes that in the nineteenth century “The biggest constraints on Brazil’s economic development remained the enormous difficulty and cost of transporting goods around the country.” And “Nor did the First Republic [1893] heed … warnings [of a reporter] of the need for popular education and social inclusion.” Brazil’s World War II economy, he says, was built on commodities; no attention was given to competitiveness.

Sound familiar? In fact, themes familiar to readers of The Brazilian Economy echo through the book. Throughout, too, Reid does not back off from giving credit or criticism where either is due. The result, at least for a non-Brazilian, is a much clearer sense of what Brazil is really like now—and why. In Brazil, for instance, street demonstrations like those so common in France are rare, which is why seeing so many people in the streets in June 2013 was such a shock to the Brazilian psyche. It was fascinating to learn that one of the rare few occurred in 1880, under Emperor Dom Pedro II —when the fare charged by trams in Rio de Janeiro prompted three days of rioting! Although, unlike 2013, the army eventually opened fire on protesters, the fare rise was cut immediately.

Anne Grant, an American lawyer, has been senior editor of The Brazilian Economy since its inception.

Reid does a particularly useful job of setting the context for what Brazil is going through today, before analyzing the current situation in detail. He points out that in the 1930s, in the first ascendance of Getulio Vargas, there was economic recovery but it was deficit-financed. The 1934 constitution was liberal, but it was ignored. He distinguishes Brazil’s military dictatorship (1964–85) from those elsewhere in South America because it maintained a “façade of democracy” and relative due process. And he explains what ultimately led to its undoing because of three sets of distortions that were “especially costly in the 1980s: (1) inflation, (2) currency overvaluation and Brazil’s persistent balance of payments problem, and (3) state interventions in the economy.

In Part II, The Making of Democratic Brazil, Reid begins by explaining the difficult launch of the New Republic: “Begun amid such hope, the New Republic delivered only disappointments,” and points out that when the coalition behind it fractured, “for better or for worse a potential opportunity for a radical rupture with the socio-economic patterns bequeathed by the dictatorship was lost.” He itemizes changes made by the 1988 constitution, though noting that “it confused constitutional principles with policy choices and sometimes involved an absurd level of detail.”

After describing the soap opera that was the Collor administration—“it was somehow characteristic of Brazil’s problems that the man who proclaimed it his mission to modernize his country (and in part did so) practiced the old patrimonial vice of blurring the public interest with private ones”—Reid dissects how the Real Plan conquered inflation and says of the election of Cardoso, “Brazil’s slow accident-prone transition to democracy finally seemed complete.” The litany of lost opportunities for structural reform that follows in the rest of the book explains why it only seemed that way.

The transition from Cardoso to Lula was encouraging. Lula in his 2002 Letter to the Brazilian people reassured them that “stability and control of the public accounts and of inflation are today the patrimony of all Brazilians,” and so it seemed throughout his first term. But, Reid says, “The reality was that the cycle of faster economic growth that had begun with the Real Plan had run its course.” In fact, in his second term Lula adopted “a somewhat more statist economic policy.” Rousseff intensified this. She and her administration accepted that “growth would have to come more from investment than consumption. But as a promised economic recovery failed to arrive in 2012, they seemed to panic.” After dissecting how things then went wrong, Reid commented, “In footballing terms, these policy mistakes were own goals. They offered Brazilians no lasting benefit.”

But Read recognizes that starting with Cardoso, income inequality fell for the first time since the 1960s, and “by guaranteeing that no Brazilian should starve, Bolsa Família (Family Grant Program) set a floor without which the notion of democratic citizenship would have been a mockery.” However, he does point out in what follows that “the new middle class” is middle class only in economic, not in social or cultural terms.
“The protests of June 2013 suggested that Brazil’s social transformation of the past two decades has generated much more demanding citizens.”

Reid makes trenchant comments on Petrobras as a vehicle for politics and about land ownership problems, but does note that “Brazil is an agricultural superpower thanks to sustained increases in productivity,” often with help from state-owned Embrapa, a research operation. He also is encouraged by the evidence of entrepreneurial success in a variety of areas. In this discussion he points out problems with the 1942 Labour Code, which was based on Mussolini’s, which now has 900 articles, noting it is “almost impossible to comply with the code in full.”

In Part III, Prospects, Reid looks at where Brazil has been (its history) and asks tough questions about where it might be going. For instance, in his thorough discussion of foreign policy, Reid simply asks, “What does Brazil really stand for, and what does it want?”

Chapter 13, An Unreformed Leviathan, relies on Reid’s habit of telling detail. “What marketers call social classes C, D, and E, who make up more than 80 percent of the population, spend an average of 3 to 4 hours a day on public transport, in many cases on crowded buses or suburban trains. No wonder they were angry about the fare rise.” But they were angry about other things as well. One demonstrator said, “Stop saying it’s about fares, it’s for a better Brazil.” Reid comments that “[Rousseff’s] initial response was to propose a Constituent Assembly—as if she had just woken up after falling asleep in 1984.”

In 2013, Reid notes, Brazil “boasted the world’s most fragmented system”—the 12-party Rousseff coalition administration brought total ministries up to 39, which adds up to more than three more patronage jobs and reflects “Brazil’s tradition of patronage politics going back to the monarchy.” He points out that “The constitution in the late 1980s decentralized revenue more than it did responsibilities …. The result was a horrendously expensive and inefficient arrangement.” He notes that “In giving something to the have-nots, Lula didn’t take away the privileges of the haves,” and ties some of his and Rousseff’s activities to those of “the corporate state of Vargas and Geisel.” In discussing corruption Reid lays bare the roots of “the voracious cupidity of a predatory class of professional politicians.”

Quoting Mario Henrique Simonsen, Reid sums up his theses by saying, “The great national debate is not between left and right, but between the modern and the archaic.” That remains true.” He continues, “Unless Brazil abandons its recent dalliance with a revival of the corporate state and returns to trying to create an effective regulatory one, it will not be able to meet the demands of its increasingly empowered citizens for more opportunities, better services, and a better quality of life.” Yet depressing though his analysis may be, he is not without hope. “The protests of June 2013 suggested that Brazil’s social transformation of the past two decades has generated much more demanding citizens. That was not before time.”
Time for a route correction

With performance less than is necessary to meet Brazil’s infrastructure demands and with funding scarce, investment needs to become more efficient.

Solange Monteiro

BRAZIL’S INFRASTRUCTURE HAS BEEN a central topic of discussion—and contention—since the Lula administration created the Growth Acceleration Program (PAC) in January 2007. With transport and ports then deteriorating after nearly three decades of low investment, there was hope that Brazil’s economy would regain its dynamism.

Seven years later and with the second PAC program about to end after awarding a large number of concessions for infrastructure, the preliminary results show that the anticipated acceleration of infrastructure projects has not occurred. According to InterB Consulting, infrastructure investment has grown slightly above 2% of GDP, but at least 4% is needed to meet the country’s needs. “In 2013, we recorded 2.4% of GDP; in 2014, the forecast is 2.5%. At that rate it would take 25 years to reach 4%,” says Claudio Frischtak, InterB president.

The investment program is now undergoing a mandatory review. It will be the central topic at the Seminar on Infrastructure and Heavy Construction in Brazil on September 30, in Rio de Janeiro, sponsored by the Brazilian Institute of Economics of Getulio Vargas Foundation (IBRE).
There is no room for inefficiency if Brazil wants to attract investors. High on the reform priorities to accelerate infrastructure investment are reducing excessive red tape, streamlining regulation, and numerous microeconomic reforms. “We have the tools, but we get the execution wrong,” says Eduardo Zaidan, vice president of the Construction Union of São Paulo (SindusCon). “We need a strong business environment to support decisions to invest when the backdrop is lower growth.”

CONSTRUCTION SLOWDOWN
The current uncertainty has had a depressing effect on the construction industry. IBRE staff estimate that in 2014 the construction sector will contract by at least 5.1% and perhaps as much as 8% if sector confidence indices show no significant improvement in the second half of the year. “If these projections are confirmed, construction GDP will have fallen by 0.7% a year for 2012–14 compared to annual growth of 5% for 2005–11,” says Armando Castelar, IBRE coordinator of applied economics. In the most pessimistic IBRE scenario, fixed investment would fall by 8.4% in 2014—the worst contraction since 1996.

Zaidan points out that construction has been slowing down since 2012, and the construction industry has a large weight in total investment—“42% of investment in Brazil goes through the construction sector.” He adds, “The construction activity we see today is a result of decisions taken in the past. If new investment decisions are made slowly, there will be no possibility of a strong rebound next year.”

In the quarter ended in August, the IBRE Construction Confidence Index showed a slight improvement but was still 9.9% lower than in the same period last year. Ana Maria Castelo, coordinator of IBRE construction surveys, says that “The current sluggish activity and uncertainty in the construction industry underscore the limiting factors for business. In August, for the first time, the survey shows more concern about demand than about a shortage of skilled labor.”

MY HOUSE, MY LIFE PROGRAM
One factor weighing on the housing sector is the high price of real estate. “It is true that in the last seven years, mortgage lending increased six fold as a proportion of GDP, and it continues to grow, but there are also limits on household borrowing capacity. Property prices have tripled and incomes have not kept up,” Castelar says. There is also uncertainty about whether the My House My Life program will be renewed. That popular program, which subsidizes housing for low-income households, has financed 3.2 million homes. Zaidan notes that “In 2003, before the program, only 30,000 properties were financed in Brazil.”

José Carlos Martins, president of the Chamber of the Brazilian Construction Industry (CBIC), advocates extension of the second PAC for six months, until the third phase is in place: “The transition from the first PAC to the second took 10 months … That can really disrupt the construction sector.” He also advocates changes in the lending terms to expand the benefits to other income groups: “Today, someone earning R$1,600 pays R$80 in mortgage payments, but someone earning R$1,601 pays nearly R$400. A more gradual schedule of interest rates and subsidies would be better.”

HEAVY WORK
Like residential construction, industry, which is a major factor in demand for heavy construction,
has clearly reduced its fixed investment because it has not been performing well either. Public works and the large number of infrastructure concessions should support fixed investment, but they do not. Armando Castelar and Claudio Frischtak highlight some reasons: (1) The public sector continues to dominate in some infrastructure sectors, and it has major problems of bureaucracy, mismanagement, and corruption. (2) The unstable economic situation, with high inflation, increases uncertainty about the long term. (3) Government puts pressure on concessionaires to reduce their rates of return. (4) Finally, regulatory agencies have been weakened and privatization of public assets has been politicized.

Joisa Campanher Dutra, coordinator of the Center of Studies in Regulation and Infrastructure (CERI) of the Getulio Vargas Foundation, describes
what has been happening with regulators in the last 20 years: “The initial motivation was to build up a competitive market and improve its efficiency. The scenario has changed recently, and the influence of politics on regulation has increased significantly. This does not create a good business environment, or attract new concessions,” she says. Adds Vinicius Benevides, president of the Brazilian Association of Regulatory Agencies (Abar), “More stable regulation is a necessity because, as we know, decisions about investing in infrastructure take into consideration primarily the size of the market, the political environment, and the stability of the regulatory framework.”

“It took more than a year to reorganize the highway system. The concession plan was announced in August 2012 and construction contracts were expected by April 2013. But so far, we have no railways and ports. All this creates uncertainty about the future,” says CBIC’s Martins. Carioca Engineering, a construction company, must live with this uncertainty. The

“The construction activity we see today is a result of decisions taken in the past. If new investment decisions are made slowly, there will be no possibility of a strong rebound next year.”

Eduardo Zaidan

Social housing — Residential developments of My House My Life program, Estácio neighborhood in Rio de Janeiro
company is active in bidding for concessions and public-private partnerships (PPPs). Even though its contracts cover airports, sanitation, oil and gas, and ports and it expects to bring in R$2 billion in revenues this year, it expects its revenues to drop 40% in 2015. Why? Roberto Moscou, general director of the company, explains it’s the slowness of the concession process. “In the case of ports, for example, the law is stranded in the Court of Audit. Who will invest in private port terminals if the rules are not clear?”

Moscou says that, knowing the limitations that are still present in the process, the focus of his company is structured deals and private clients, although he acknowledges that “concessions bring balance to the billing of a construction company, which is cyclical.”

Public procurement is a very slow process, Moscou points out. Carioca Engineering built 20km of the Rio de Janeiro metropolitan beltway. “We could have completed it in a year and a half and we took six years because there were 600 land expropriations to be made,” Moscou says. “The expropriations went slowly, we had to stop the work, and we lost money. In contrast, when we built the port terminal of

Port of Santos — Delay in dredging projects restricts movement of large ships.
the Companhia Siderúrgica do Atlântico (CSA), it was negotiated with the German executives for seven months, but the day after we signed the contract, we were working with all permits in hand.”

The research of economist Carlos Campos of the Institute of Applied Economic Research (IPEA) illustrates how inefficiently federal resources are used, as measured by the difference between resources authorized for fixed investment by the government and state-owned enterprises, and those that are effectively executed. Campos says that “Between 2003 and 2013 the country failed to use R$70 billion of funds authorized for the transportation sector.”

Mauricio Muniz, PAC secretary, argues that “PAC 2 saw a large improvement in planning and execution. Through last April, R$871 billion were executed, about 85% of the total authorized investment. We almost doubled investments compared with PAC 1.”

CBIC’s Martins thinks that to really improve PAC budget execution, it is necessary to improve the whole planning process.

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“Over R$200 billion projected in the Program of Investment in Logistics will only make up for the current deficiencies in infrastructure.”

Rodolfo Tourinho Neto

Rails grow — Expansion of investments in railways is expected
system, starting with the quality of the projects chosen and clarifying the responsibilities of federal agencies to streamline project controls.

**WHO PAYS?**
So far no initiative has provided enough funding to raise public investment in infrastructure, and in coming years the government will have even less fiscal room to fund more investment. In the 2015 budget, the PAC and My House My Life program have additional resources totaling R$65 billion, only a 2.7% nominal increase over 2013.

Rodolpho Tourinho Neto, president of the National Association of the Construction Industry (Sinicon), is skeptical that funding for infrastructure projects will go up much: “Over R$200 billion projected in the Program of Investment in Logistics will only make up for the current deficiencies in infrastructure. But we will still have to meet and finance the future demand for infrastructure.”

The National Development Bank (BNDES), the principal long-term lender in the country, is more optimistic. The bank expects to steadily increase its

**Urban transportation — Bus rapid transit (BRT)**
Transcarioca is part of PAC.

“Today, someone earning R$1,600 pays R$80 in mortgage payments, but someone earning R$1,601 pays nearly R$400. A more gradual schedule of interest rates and subsidies would be better.”

*José Carlos Martins*
disbursements for infrastructure. “Since 2003, disbursements for transport and logistics grew on average 37% per year, reaching R$9.5 billion last year. This year we hope disbursements will reach R$12 billion and will continue to grow between 20% and 30% for at least the next three years,” says Cleverson Aroeira da Silva, head of the BNDES Logistics Department.

Although the BNDES disbursement plans sound encouraging, they also worsen the country’s fiscal situation, Castelar observes. BNDES subsidized loans are funded by large Treasury’s transfers. “These transfers, negligible in the past, reached 9% of GDP. That increases gross public debt,” he warns. InterB’s Frischtak says it is difficult for the private financial system to compete with BNDES subsidized credit. According to BNDES, in July, the bank was financing 377 infrastructure projects totaling R$187 billion, representing 55% of the total cost of the projects. Fritschak says the market has become used to cheap BNDES funding, considering it a compensation for Brazil’s high regulatory risk premium.

Castelar warns that a better balance between the BNDES and other lenders is imperative. “The situation in which almost half the credit in the Brazilian economy is not sensitive to the policy interest rate much more because it only affects the other half of credit in the economy,” Castelar says. Frischtak agrees: “We have a deep financial and capital market, well regulated, which usually works well, but we are not leveraging.” He believes the risk should be shifted from the government to the private sector, restricting the BNDES share of project financing.

**COURSE CORRECTION**

Economists agree that it is necessary to reduce political and regulatory risks, which are clouding the horizon for investment. “When this is done, we will be able to reduce subsided loans and improve the fiscal situation,” says Castelar. Frischat says that “a credible economic policy” would raise the economy’s potential growth, increase fiscal space, and improve the mood of investors.

The good news, Castelar thinks, is that there has been progress in planning, with better analysis and more qualified people. PAC secretary Muniz highlights several improvements in recent years: “The Ministries have strengthened their planning by hiring 720 infrastructure analysts, including engineers, architects, and geologists; setting up plans for transportation and energy; and improving regulatory frameworks.” Castelar says, “We have a lot of waste. … We could save about 30% to 40% of the money simply by managing projects better.”

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“More stable regulation is a necessity because, as we know, decisions about investing in infrastructure take into consideration primarily the size of the market, the political environment, and the stability of the regulatory framework.”

*Vinicius Benevides*
Camargo Corrêa was the first company to bring Shield machines to Brazil, specially designed for digging subway tunnels.

At 3,595 meters long, the Rio Negro Bridge is the largest cable-stayed bridge ever built across a river in Brazil.

Serra do Facão Hydroelectric Power Plant (Goiás), producing enough energy for a city of 1.2 million.

Camargo Corrêa was the first company to bring Shield machines to Brazil, specially designed for digging subway tunnels.

The Laguna Bridge (Santa Catarina) is Brazil’s third largest, roughly three kilometers long, with one cable-stayed stretch 400 meters long.

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IN AN OPEN LETTER to the candidates for the Presidency, released in August, the Confederation of Agriculture and Livestock of Brazil (CNA) says that in 40 years agribusiness “tripled land productivity, integrating the industry in dynamic supply chains.” Currently it represents 23% of GDP and accounts for 27% of the jobs created. In the first half of this year agribusiness accounted for 44.4% (US$49 billion) of total exports.

According to the Center for Advanced Studies in Applied Economics and the Luiz Queiroz School of Agriculture, University of São Paulo (Cepea), in the past 14 years the volume exported by agribusiness grew 230% and its trade balance (US$ 41 billion from January to June this year) has expanded 468%. Because of this rapid growth, cities founded in the 1980s, like Lucas do Rio Verde and Sorriso in Mato Grosso state, have become references in the economic map of Brazil. The questions now are these: What needs to be done to consolidate the results already achieved and to ensure continued growth with greater balance between the agricultural regions of the country? And will there be enough demand to sustain the sector’s growth?

**Non-negotiable issues**

Economist Mauro Lopes, project coordinator, Center for Agricultural Studies of the Brazilian Institute of Economics (CEA-IBRE), says that, agricultural organizations and professional bodies have identified at least 60 important issues that need to be addressed in the short, medium and long term. Four of these are non-negotiable: expansion of infrastructure, especially roads; expansion of agricultural insurance; an active policy of phytosanitary control; and expansion of resources for research. Research is essential to increase productivity and better defend crops against diseases and pests.

“When agribusiness can count on the planned railways, highways, and waterways, it will be able to rationalize distribution … with substantial cost reductions and significant changes in how domestic prices are formed, including more rational use of land and other natural resources,” says economist Geraldo Barros, Cepea coordinator.

The CNA acknowledges government’s efforts to auction attractive road and railway concessions but asks for a plan to expedite transition to an intermodal logistics system instead of the current...
model centered on roads—the most expensive of all forms of transport. Beyond the main highways IBRE’s Lopes highlights the successful experience of public-private partnerships (PPPs) to which farmers bring machines and state governments, such as Mato Grosso state, bring asphalt for paving.

Limitations
The CNA document considers it “unacceptable” that at this stage only 8.7% of Brazilian crops are covered by insurance. It says, “Farmers have taken almost all the risks and uncertainties of agricultural production, especially the volatility of income.” That is why income insurance is a CNA priority.

CNA says that those most vulnerable to these oscillations are medium producers who do not have access to financial markets, find the red tape too difficult if they want to access rural credit, are not eligible for the National Program for Strengthening Family Agriculture (Pronaf), and must deal with competitors within the Common Market of the South (Mercosur).

According to Lopes, it would be possible to add about 15 million hectares to the 76 million hectares (9% of Brazil’s land) that is now under cultivation. The problem, he says, is not finding the land, it is finding the financing. Although the government plans to allocate US$68 million to support the 2014/15 crop, 15% more than in the previous year, the high costs of modern machinery, Lopes says, mean the need for financing is immense and farmers who are not yet customers of the official credit sources face great difficulty in obtaining financing.

Cepea’s Barros notes that investments in agribusiness tend to expand rapidly in years of bumper crops, but in these moments of euphoria, major problems arise: “It is common for producers to make commitments that are inconsistent with their average income flow, increasing the risk of default.” The solution, he says, is “a policy of long-term agricultural investment.”

Lopes thinks that this year farmers have some capital, thanks to five consecutive years of good prices, but they have “low resilience” to stress surprises, such as too much or too little rain. He and his team think a good alternative to the shortage of capital for purchasing machinery would be to adopt the Argentine model where producers avoid heavy investments in machinery by contracting with others to do mechanized planting and mechanized harvesting. But this will require a major change in behavior.
AGRICULTURE

Research and productivity
In the last two decades, total factor productivity (TFP) in agribusiness grew 6.4% per year, according to Barros. He believes this is the main change that supports optimism that Brazil can take a larger major role in the global food market. But he is also concerned that some higher productivity is being bought with heavier land use and deforestation.

The solution, he believes, is public and private investment in research in such areas as more efficient soil management: “The new challenges are continuing advances in productivity and efficiency in the control of new pests and diseases that plague agriculture, bearing in mind environmental and social aspects. An old but still major challenge is to also adapt research to the needs of low-income farmers and their families.” Barros points out that 32% of the rural population is still poor.

Rural poverty is concentrated in the north, particularly the northeast. In the 2012/13 crop year, corn yields in the north and northeast were less than half those recorded in the midwest and the south, where farming is in the hands of large producers.

Embrapa
The star of Brazilian agricultural research is the state-owned Brazilian Agricultural Research Corporation (Embrapa), recognized throughout the world for its achievements.

Ladislaus Martin Neto, Embrapa’s executive director of research and development, recognizes that the problem of regional inequality is severe. He says that some research responds to the needs of poor farmers, but agricultural education services for poor farmers are also needed. That is why the National Agency for Technical Assistance and Rural Extension (Anater) has just been created.

Martin Neto says that in the last five years the government has doubled Embrapa’s budget to US$1.1 billion in 2014, but he notes that at barely 1% of GDP, that is at most half of what most successful countries invest in agriculture. But he is encouraged by an increase of private investments in coordination with public investments. New opportunities will open, he says, adding that the Argentine model — Planting corn in the Pampas region in Argentina. In Argentina, producers avoid heavy investments in machinery by contracting with others to do mechanized planting and harvesting.
development of bioenergetics is still in its early stages.

As an example, Martin Neto cites the Inova Agro Plan, with funding from the National Bank for Economic and Social Development (BNDES) and the Financing Agency for Studies and Projects (FINEP), launched last year to encourage genetic research, modernization of machinery and equipment, and other initiatives. “Today, Embrapa has signed over a hundred cooperation contracts with companies,” he says, valued at about US$1 billion.

Martin Neto says that one current research target is diversification of cultures, combining in the same area, for example, grain crops, pasture, and forest. Brazil has 50–60 million hectares in pasture areas that could lend themselves to better land management, but he recognizes that transforming the approach will require considerable research and use of modern technologies to ensure gains in productivity and efficiency, while still protecting the environment.

Among new technologies being tested at Cepea is the use of unmanned aerial vehicles (drones) to speed up crop monitoring to detect, for example, situations of water stress, imbalances in irrigation, and damage caused by pests and diseases. Embrapa’s Instrumentation Center in São Carlos, São Paulo state, is also doing research on the use of drones.

An alternative to increasing yields in soybeans, today Brazil’s main agricultural commodity, is adding a third major crop to corn and soybean production, though Lopes worries that would increase pest and disease risks. Embrapa’s Martin Neto is more optimistic about a third crop, especially in irrigated areas.

Rural poverty is concentrated in the north, particularly the northeast. In the 2012/13 crop year, corn yields in the north and northeast were less than half those recorded in the midwest and the south, where farming is in the hands of large producers.
New technology in the air — Drones speed up crop monitoring, detecting situations of water stress, imbalances in irrigation, and damage caused by pests and diseases.

He thinks the risk can be reduced by continuous monitoring by experts and prompt action to minimize the risk.

More planning
IBRE’s Lopes questions how Brazil reacts to phytosanitary issues; he worries that “whenever there is a new disease outbreak in either crops or livestock, there is a rush to solve problems too hastily and then struggle to recover markets.” This situation reflects a lack of planning to anticipate problems and take preemptive action.

“It is really necessary to move to a higher phytosanitary standard,” Cepea’s Barros said, not only to avoid the frequent interruptions of trade associated with phytosanitary issues but also to have access to the most demanding markets, “an essential condition to the continued growth of agribusiness.”

Martin Neto acknowledges the problem. Today, he says, more than 150 pests could hit

Brazilian grain production has increased mainly because of higher yields; cultivated area remained broadly the same.

Source: National Food Supply Company (Conab).
Brazil’s agriculture. Embrapa’s strategies are to eradicate pests, seek pest-resistant seeds, and share knowledge with partner countries in order to anticipate and prevent problems. These preventive efforts are now being systematized in a program in which the Ministry of Agriculture participates.

Secure demand
The recent fluctuation in the prices of agricultural products raises the other question: Will there be markets for Brazil’s expanding agricultural products?

IBRE researcher Ignez Vidigal Lopes points out that China still has about a billion people in the countryside, most of whom have to be “urbanized” if they are to be considered part of the consumer market. She points out that the U.N. Food and Agriculture Organization expects by 2050 that Brazil’s food supply will increase 40% so that it can meet the demand of nine billion people around the world.

In 2013, China bought about 23% of Brazil’s agricultural products and the EU bought 21%. Barros estimates that in the next three to five years the market for Brazilian agricultural products will rely on the growth of emerging countries: “In the longer term, Brazilian agribusiness should have as a goal to win markets with higher value added, which are now in the hands of developed countries,” he says. These countries add value by processing the raw material they import, as Germany does with coffee.

Among new technologies being tested at Cepea is the use of unmanned aerial vehicles (drones) to speed up crop monitoring to detecting, for example, situations of water stress, imbalances in irrigation, and damage caused by pests and diseases.
The pessimism continues

Thais Thimoteo

NO MATTER WHERE BUSINESSPEOPLE AND CONSUMERS LOOK, they see no reason to feel optimistic about the direction of the Brazilian economy. The signs of a recession—GDP fell by 0.6% in June and 0.2% in March, two consecutive quarters—uncertainty about the elections, and the prospect of economic adjustments in 2015 have brought Confidence Indexes in 2014 down to the levels seen during the 2009 global crisis. Since December 2013, the Business Confidence indicator (ICE) has fallen by 12%. Manufacturing and construction have consistently had the gloomiest prospects, even though the construction indicator went up in August and manufacturing in both July and August.

Expectations

Although there are more business days until the end of the year, there are not enough to make up for eight consecutive months of decline in the Industry Confidence Index (83.4 points, August), according to Aloisio Campelo, IBRE assistant superintendent of business cycles.

“Confidence was worse than expected in August,” he says. “Street protests and days off because of the World Cup reduced services and commerce activity, exacerbating the decline in demand. But even though there are low expectations for the future, we can expect some improvement in services and commerce in the coming months.” He explains that “In the case of manufacturing, the outlook is worse because inventories have accumulated, and domestic demand is very weak because of competition with imported manufactures. After intense activity to complete World Cup-related projects, construction is not seeing much recovery related to infrastructure and social housing projects.” Campelo also attributes the situation to increased household indebtedness.

The World Cup and the days off briefly spurred consumer confidence in the economic outlook, but after a little more good cheer in July, the Consumer Confidence Index fell again by 4.3% in August, to the lowest level since April of 2009. Viviane Seda, coordinator of IBRE consumer surveys, thinks the disappointing result reflects the dissatisfaction of Brazilians with the state of the economy as a whole.

Consumers are concerned about the labor market, which has shown signs of slackening—something that did not happen in 2009. This year in August, 58% of those interviewed thought it is now more difficult to find jobs. “Not only are there fewer job vacancies, but negotiating wages must also be more difficult,” Seda said. “Consumers’ perception of getting a job today and expectations about future employment have become more negative in the last four months.”
Campelo believes that until the end of 2014 the negative business outlook is almost a given considering the final days of a lame-duck government and uncertainty about the path of inflation. Uncertainty tends to delay investments. In 2015, once the new government defines its policies, Campelo thinks, confidence should rise, though not to the peaks seen after the 2010 presidential election. “There is concern about what commitments presidential candidates will make during the election campaign, and what coalition of parties will support the new government,” he says.

**Investments**

The low level of Use of Installed Capacity of Industry (NUCI) in August (83.2%) also suggests that fixed investments will not materialize, since industrial inventories are still full and there is no demand for machinery and equipment or hiring.

The IBRE forecast of a decline of 6.5% in gross capital formation in 2014 underlines the worrying investment situation, at least in the short term. However, Campelo believes investment will swing up again in 2015. “It is unlikely that fixed investment will fall again next year because it is essentially cyclical, unless we run into an energy crisis or a deep slowdown in the United States and Europe,” he concludes, noting, however, that fixed investment will recover only enough to make up for the losses in 2014.

The IBRE forecast of a decline of 6.5% in gross capital formation in 2014 underlines the worrying investment situation, at least in the short term.
THE INCREASE IN THE percentage services contribute to exported goods reflects the importance the sector is gaining in international trade. In the United States and India, services already account for added value of 50% of total gross exports. For Brazil, the addition is 37%, equivalent to South Korea and Canada. But as a share of the world service market, Brazil’s services exports are small: in 2012, they accounted for 0.9% of the world total, compared with China’s 4.4% and India’s 3.3%. China is the fifth largest exporter of services, and India is the seventh.

In the last decade, Brazil’s trade deficit in services increased almost tenfold: from US$5 billion in 2003 to US$47 billion in 2013. “This deficit already exceeds the income deficit, which last year reached US$40 billion,” points out Lia Valls Pereira, researcher at the Brazilian Institute of Economics. In a presentation at the 33rd National Foreign Trade Meeting last August in Rio de Janeiro, she said she saw no sign of a turnaround: “We are importing more services, but have not been able to incorporate them as a competitive factor in our exports, especially manufacturing exports,” she said, highlighting the low share of spending on royalties and licenses. Last year, the main areas using imported services were international travel (29%), renting of machinery and equipment (22%), and transport (18%).

Nelson Fujimoto is Secretary of Commerce and Services of the Ministry of Development, Industry and Foreign Trade. At the event he argued that the country should not try to limit services imports
but instead should stimulate its service exports. “Some of these imports are the result of more investment in productive sectors: oil sector demand for machinery and equipment, and hiring waterway transportation to carry commodities,” he stressed.

Fujimoto said that two years ago the Ministry improved data collection and the compilation of statistics on the export of services by creating the Brazilian Classification of Services, Intangibles and Other Operations that Produce Changes in Assets and putting in place the Integrated Foreign Trade System. The data now being gathered reinforce the view that Brazil is more competitive in construction professional services—such as engineering, architecture, research and development and technical assistance, which currently dominate its export basket—and in information technology. “We have also identified opportunities to diversify trading partners,” Fujimoto said. “Our services export are concentrated in the United States (31%), followed by the Netherlands (7.18%) and Germany (5.5%). We should be encouraging China to purchase Brazilian services.”

Nelson Fujimoto

According to Valls Pereira, raising Brazil’s share of the world services market will depend crucially on increased productivity and competitiveness, which implies heavier investment in educating and training workers, innovation, and negotiating international agreements on services. “The product fragmentation observed in the services sector clearly shows the need for international trade negotiations,” she said. “Unfortunately, Brazil has done very little in this regard. We have to improve our trade negotiation agenda principally with neighboring countries, if we want to become the hub of the regional supply chain.”

Brazil's service and income balance, 2013

(US$ billions)

Source: Central Bank of Brazil
BRAZIL'S TRADE BALANCE was US$2.4 billion in 2013, after recording double-digit surpluses going back to 2002; trade surplus projections for 2014 are about the same as last year. Because of the declining trade surplus, the current account deficit is around US$ 80 billion and warning lights are on as it approaches 3.5% to 4% of GDP. No currency crisis is expected, but in 2013 the country had to use part of its international reserves (US$6 billion) to finance the current account deficit (US$81 billion).

The trade deficit in oil and oil products, which rose from US$5 billion to US$20 billion between 2012 and 2013, has contributed significantly to the deterioration in the trade balance as a whole. The oil deficit rose because oil rig problems have reduced production and price controls on sales of domestic fuel sales have pushed up fuel imports. Once these issues are remedied, it would be possible to resume higher trade balance surpluses.

**Trade surpluses**
 Improvement in the oil trade balance is essential to improve performance of the general trade balance, but other factors also contributed to the general decline. Between 2002 and 2007, Brazil's trade surplus went from US$13 billion to US$40 billion, peaking at US$46 billion in 2006. In 2003 Brazil's trade surplus with China was US$2 billion, though it fell thereafter. During this period Brazil posted trade surpluses with South America, the European Union, and the United States. In 2008, the surplus fell to US$25 billion as trade surpluses declined in most markets, particularly in the United States, and in trade with China a deficit of US$3.5 billion emerged.

After 2009, Brazil posted trade surpluses with South America and China. Brazil has posted trade deficits with the United States since 2009, because of both declining demand and less competitive Brazilian products. Since 2013 Brazil has posted trade deficits with the European Union and other countries.

The trade surplus with South American countries has declined since 2011, mainly because of the Argentine crisis but also because exports to other countries in the region dropped. To raise Brazil’s trade surplus with neighboring countries means manufacturing exports will have to improve, because they represent 80% of Brazilian exports within the region. This brings us again to the issue of the competitiveness of Brazilian products. Outside the Mercosur countries, the other major economies in the region (Chile, Colombia, and Peru) have signed agreements with the United States, the European Union, and China (except Colombia). As result of these trade agreements, Brazil has lost the advantage of preferential import tariffs.
A near-term boom in commodity prices is unlikely. We do not consider that a slower pace of growth in China, around 7%, will have a major impact on Brazilian exports to that market. Even if Brazil exports of iron ore and soybeans to China declines, diversification of agricultural exports could ensure continued trade surpluses there.

**Pessimistic scenario**

In general, as an economy grows less, imports decline and the trade balance improves. In 2013 Brazil grew by 2.3% and in 2014 growth is expected to be near or below 1%, yet despite lower growth the trade balance has worsened. Appreciation of the exchange rate may have contributed to increase imports, and loss of competitiveness has reduced exports.

Earning trade surpluses of US$20 billion or so will require changes in the composition of foreign trade.

In short, the worsening of the trade balance started before the 2008 crisis. In the past high commodity prices improved Brazil’s trade balance with China, but if Brazil is to post trade surpluses of close to US$20 billion, commodity exports only to China and oil exports elsewhere may not be sufficient. Brazil needs also to address the competitiveness of its exports to improve its trade balance with the United States, the European Union, and other countries.

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**Brazil's bilateral trade balance by country**

(U$ billions)

The political strength of ethics

Joaquim Falcão
Dean of the Law School of FGV Rio

Solange Monteiro, Claudio Conceição, and Bertholdo Castro

THE LAW SCHOOL OF FGV Rio in August published the results of a major study of the Brazilian Supreme Court. Law School Dean and Professor Joaquim Falcão was a member of the National Council of Justice from June 2005 to June 2009 and earlier earned an LLM from Harvard Law School. Here he explains the implications of the Supreme Court conviction of government officials involved in the congressional vote-buying scheme and discusses how the court is now perceived. He also believes that last year’s street protests did not want political reform but better public services, “because the new citizen is not the worker. He is the consumer, a consumer of public services and regulated services.” Falcão says the Supreme Court has stopped discussing “abstract legal doctrines and began to address actual social problems.” He adds that “what unfortunately it has failed to address are the economic issues related to past economic plans.”

The Brazilian Economy—The trial of government officials involved in the congressional vote-buying scheme was historic for its character and popularity. Two years later, how is it affecting the behavior of voters and the presidential candidates?

Joaquim Falcão—I never thought of the trial as something that would have electoral consequences but rather as an improvement of our democracy. What was the improvement? First, the Supreme Court was able to make a decision in a timely manner that responded to national interests. On trial were not only the defendants but also the Supreme Court itself. Society asked: Will the

*The National Council of Justice is an agency of the Brazilian Judicial System created in 2004. The 15-member Council is headed by the Chief Justice of the Supreme Court. Among its responsibilities are ensuring that the judicial system remains autonomous, conducting disciplinary proceedings against members of the judiciary, and compiling and publishing statistics on the Brazilian court system.
Court be able to make a decision?

I thought of the trial as demonstrating what I call the political strength of ethics—not just the authority of ethics, but ethics as an instrument of integrity in public administration. Ethical misconduct is not exactly unique to Brazil. In recent years the chief justice of Spain, the president of Germany, the prime minister of Italy, President Sarkozy of France, high Chinese officials—they have all been accused of ethical misconduct. There is a pressure on the economic, political and legal system worldwide in favor of public integrity. In Brazil, this issue has greatly affected the Workers’ Party (PT). It is not only an election issue. It is something much broader that affected the credibility of the PT government at the time.

Do we now have less tolerance for corruption?

Corruption is not an issue of one individual, one party, even one nation. The congressional vote-buying scheme involved more than the PT; it also had to do with relations between public and private institutions: Congress, political parties, businesspeople, banks, advertising agencies. The government alone does not cause corruption. The challenge in the trial of the vote-buying scheme was whether the Supreme Court would be able to recognize two basic challenges: the fairness of a trial that respects the rights of the defense yet at the same time the defense of public integrity. Convictions had to be seen as having been done in a legitimate way after all rights and defense appeals were exhausted. It was a fair trial. The trial broadcast removed any doubt. Society watched and also judged.

Did the trial improve the public image of the Supreme Court?

The judiciary does justice on behalf of the people. Although justices and judges cannot be replaced by the people, they represent the people as much as the executive and the legislature branches. Courts have to act in tune with the sense of justice of the people. ... If they are not in tune, they run the risk of increasing popular distrust of the magistrates, the institutions, and the Supreme Court. The Supreme Court has regained its lost legitimacy because it got closer to the people’s interests. It has ruled on many issues, such as homosexual unions, drugs, freedom of the press, the racial quota system, among many others. It has stopped discussing abstract legal doctrines and moved on to confront the actual problems of Brazilians.

What the Supreme Court unfortunately has failed to address are economic issues related to past economic plans.1 Chief Justice Joaquim Barbosa tried it but postponed it due to pressure from the executive branch and lobbying from banks. This is bad because when the Supreme Court does not face an issue, it prolongs a situation of legal uncertainty for

“I thought of the (vote-buying) trial as demonstrating what I call the political strength of ethics—not just the authority of ethics, but ethics as an instrument of integrity in public administration.”
creditors and debtors and the business environment.

The Supreme Court has been ruling on issues that the legislature might ignore for political reasons. Is this an appropriate role for the Supreme Court?
The Constitution says that the powers are independent and harmonious among themselves. This is an ideal situation. But the reality is different; there is a permanent tension between the powers. … Democracy is the recognition of conflict and tension, and a nonviolent protocol to solve them.

Tension between executive, legislative, and judiciary is a reality. Often the Supreme Court takes the initiative and is more daring. The legislature can react but has not done so. It has allowed the Supreme Court to be more proactive.

For example, in Congress there is no consensus on issues related to racial quotas or abortion. The churches lobby very strongly against abortion and those in Congress do not want to lose votes. … The drug issue is another example: It was excessive to classify drug users as drug dealers, a crime without bail. As a result the prisons are crowded. … Countries like Portugal, Uruguay, several states, the United Nations, all have said that the current war on drugs has failed. But if you propose any change to decriminalize or prioritize health in the fight against drugs in Brazil, the research shows that the public wants more repression. …

Congress does not want to lead on long-term reforms, which are incompatible with the short cycle of elections. This creates opportunities for other powers, such as the judiciary. It creates a space for more efficient legislation. There can be no vacuum in politics, and the Supreme Court advances.

What do you think about the Supreme Court decision to ban corporate donations to political campaigns and political parties?
We cannot analyze one type of funding alone, as was done with corporate donations to political campaigns. It is necessary to analyze campaign finance as a whole. There are several sources of funds: government fund, the parties, the candidate’s own resources, individual voter donations, businesses, NGOs, foundations. One [source] cannot be banned without assessing the effects on campaign financing as a whole. Congress is responsible for reexamining campaign financing, but because members of Congress are afraid to change it, the issue ended up with the judiciary. The Supreme Court cannot change campaign financing as a whole, because it can only rule on the specific case submitted to it. I fear that if we ban only corporate donations, when we do not have a culture of individual donations to political campaigns, government funding will become absolute. I do not think it is good for the government to interfere
so much in political campaigns. We should consider a campaign financing system with a large variety of sources, competitive, transparent, and regulated. It would be better for democracy.

Do you think that society is prepared to participate in the discussion of political reform, as suggested by President Rousseff after the demonstrations of 2013?

At the time the protesters did not want political reform. Their issue was the quality of public services and corruption in public services. That is why the people went to the street. Against the transport lobby that knows no bounds. ... Voters today want quality public services. They want safety, and health.

The situation is different in schools. Surveys show that parents are happy with the education given in schools, even if the quality in some schools leaves a lot to be desired. But they are not happy with safety, health, and public services—immediate issues that afflict the population, the everyday life of cities, which decides the vote.

What are the main conclusions of the FGV Law School study of the Supreme Court?

The study shows deviations in the Supreme Court’s actual day-to-day performance. For example, the Supreme Court should be a collegial body. But over 90% of the decisions are individual, monocratic. These occupy the time of the justices. It also found that many of the decisions are based not on merit, but on procedural issues. ... For example, the law says that if the justices ask to review a process, they should return it in 15 days. The average is over 300 days. ... It is against the law.

Society provides everything to the justices of the Supreme Court: they have resources, they are well chosen, and society respects them. The justices have to be efficient, to act within the procedural rules, which sometimes they do not. Our data have not been disputed. On the contrary, they have been used by several justices to give new directions.

Do delays in justice create injustice?

Delays in justice create legal uncertainty, which is conducive to injustice. Or to no justice at all. We did a study that classified the types of legal uncertainty. The most important is administrative, resulting from long processing time. You never know when you will get the decision. This insecurity permeates the entire judiciary. Brazilians do not complain that the judiciary decides wrongly, they complain about the time it takes to get a judicial ruling. In social and economic life we need an environment with predictability. (...)

“The judiciary does justice on behalf of the people. Although justices and judges cannot be replaced by the people, they represent the people as much as the executive and the legislature branches.”

1 At stake is a court decision that may require that the country’s banks pay billions of dollars to holders of savings accounts during the Collor (1990-1992), Bresser (1987) and Summer (1989) economic stabilization plans. According to the Brazilian Bank Federation (FEBRABAN), compensation payments could reach about US$150 billion, more than the net worth of the five largest banks. This would reduce banks’ capital, jeopardize financial stability, and possibly require massive government intervention to recapitalize the banking system.
Brazil: the present and the future

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World economic climate improves; Latin America’s worsens.

Lia Baker Valls Pereira  
Center for International Trade Studies, IBRE  
lia.valls@fgv.br

THE IFO-FGV ECONOMIC CLIMATE IN Latin America indicator (ICE) has been headed downward since April 2013. In July, the index fell 6.7% from April as both the assessment of the current situation and expectations deteriorated. Because the indicators are weighted by the share of total trade (exports plus imports) of each country in the region, they also reflect the large weights of Mexico (35%) and Brazil (23%). More detailed analysis also suggests that countries in the region are having different experiences. Mexico was the only large economy that saw its economic climate improve. Brazil’s performance was as bad as Argentina’s, and both were worse than the region as a whole. Mexico’s ICE increased by 4%; Brazil’s fell by 22% and Argentina’s by 24%.

Brazil’s own economic climate indicator has been deteriorating since July 2013. According to a separate survey conducted twice a year on the main obstacles to economic growth, Brazil’s performance reflects both a lack of confidence in government policies and a loss of international competitiveness.

Although Chile’s economic climate declined by 6%, the expectations have improved, which suggests that the economy is recovering. All of Argentina’s indicators worsened, and all of Venezuela’s have been at the bottom since July 2013.

The worsening of some of the major economies in the region explains why the world and the Latin America economic climates have been diverging since April 2013. Improvement in the world economic climate in July was led by the United States and Asia, particularly China and India. The good news in the U.S. may thus be a factor in Mexico’s favorable performance indicators. But then we would expect that the improvements in China’s economic performance would have a positive impact on major commodity exporters like Brazil.

What’s going on?

Signs of improvement in China’s economy have not translated into increases in commodity prices, as they did in 2007–11, so we do not expect the positive income shock that would be associated with an increase in revenue for major commodity exporters. Domestic issues, among them inflation, low investment, and controls on energy prices, will continue to depress the economies of Brazil, Argentina, and Venezuela.

The world economic climate warms as Latin America’s and Brazil’s cool

The Economic Climate Indicator is a quarterly survey conducted by the German Ifo Institute for Economic Research—the Ifo World Economic Survey (WES)—and the Brazilian Institute of Economics of the Getulio Vargas Foundation The ECI is an average of the assessment of the current situation and expectations for the next six months based on the answers of country experts to questions on key macroeconomic data (consumption, investment, inflation, trade balance, interest and exchange rates). The indicators are weighted by the share of trade of each country in the region.

http://portalibre.fgv.br/main.jsp?umPageId=402880811D8E34B9011D985336A53D8D
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