Weeks Focus –
David Fleischer
Phone/FAX: 55-61-3327-8085
Cell: 9218-2771 e-mail: Fleischer@uol.com.br
Weekly Report –
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Looking Ahead → What to watch for?

- 18th Oct. -- Daylight Savings Time begins in Brazil
  → 2-hour time difference NYC/Brasília
- 20-21 Oct. -- 194th Meeting of Copom → Selic rate
- 22nd Oct. -- SRF → federal tax collections R$ billion in September (+% YoY)
- 25th Oct. -- General elections in Argentina
- 27th Oct. -- Former President Lula → 70th birthday
- 27th Oct. -- The Economist - Brazil Summit, Hyatt SP, “Fighting for the Future”
- 28th Oct. -- IFC & World Bank to publish “Doing Business”, in 189 nations
- 30th Oct. -- FGV to post October IGP-M → +0.% versus +% in September
- 30th Oct. -- Public Account data for September
- 1st Nov. -- Daylight Savings Time ends in the US
  → 3-hour time difference NYC/Brasília
- 2nd Nov. -- National Religious Holiday [Day of the Dead]
- 3rd Nov. -- Trade balance for October →
• 3rd Nov. -- IBGE to report September Industrial Production +0.%
• 3rd Nov. -- Election Day in the US
• 4th Nov. -- New car sales October units, % MoM
• 6th Nov. -- IBGE to post IPCA data for October
• 11th Nov. -- Holiday – Remembrance Day (UK & Canada); Veterans’ Day (US)
• 12th Nov. -- IBGE to post Industrial Employment data for September

1 - POLITICS

1.1 – Impeachment??

The saga of impeachment continues like a telenovela – with new chapters and sub-chapters in the screenplay and actors suffering “ups and downs”.

Late last week, the PSDB, DEM and PPS called on Dep. Eduardo Cunha (PMDB-RJ) to resign his post because of the Lava Jato investigations regarding the receipt of US$ 5 million as a “side payment” from a bidding process for Petrobras equipments (according to several plea bargaining testimonies – in addition to documents provided by Swiss prosecutors regarding Cunha’s bank accounts.

However, the so-called “Opposition” changed its tune early this week when it discovered that they needed Cunha to remain as Chamber President if their Dilma impeachment strategy is to be successful. Thus, on 12th October deputies from these Opposition parties refused to sign the petition circulated by PSOL and Rede deputies to request that the Ethics Committee begin expulsion procedures against Cunha for his lack of “parliamentary decorum”. Some 42 deputies signed including one-half of the PT delegation.

At the same time, Cunha needs continued Opposition support (or at least neutrality) to remain in office and that the continuation of the impeachment effort will work to his benefit.

Some two weeks ago, Cunha outlined his own “rite of impeachment” that outlined the steps (phases) of the impeachment sequence. He explained that the 1988 Constitution gives him (as Chamber President) the exclusive prerogative to decide on requests for impeachment (to defer or reject). However, he explained that once he had rejected an impeachment petition (request), that a deputy or group of deputies could request that the full Chamber examine his decision and could revoke same, and thus install impeachment proceedings in the Chamber. Further, he explained that these impeachment requests could receive “add-ons” (incorporate additional information).

This “Cunha interpretation” of the Constitution enraged the PT and the party filed several injunction requests at the STF against Cunha’s “interpretations”. On 13th October, two STF judges issued temporary injunctions against Cunha’s “interpretations” 1) Teori Zavascki ruled that the scenario whereby the full Chamber could over rule Cunha’s decision to reject an impeachment request and thus install proceedings was not “congruent” with the 1988 Constitution. Cunha then quickly
remembered “a precedent” (to the press) that in 1999, then Chamber President Dep. Michel Temer had denied an impeachment request (against then President Cardoso) and his decision was then taken to the full Chamber, but the Chamber voted to maintain Temer’s decision. 2) Rosa Weber ruled that once an impeachment petition had been filed (protoled) at the Chamber it could not receive and “add-ons”.

To this end, SP jurists Hélio Bicudo, Miguel Reale Jr. and Janaina Paschoal prepared a new pro-impeachment petition and registered same at a cartório [notary] in SP on 15th October that should be delivered to the Chamber of Deputies on 20th October. This new version includes the accusations that Pres. Dilma continues to violate the Fiscal Responsibility Law in 2015 (as her government did in 2014). During the CUT Congress in SP, Lula admitted that this practice continues in 2015, but “Dilma used this to finance social programs”.

Photo: Eduardo Anizelli/Folhapress

Janaina Paschoal, Hélio Bicudo and Miguel Reale Jr. sign new petition.

The PT and the Dilma Government rejoiced at the “victory” but most observers thought this was only a very partial and momentary “victory”. Cunha immediately affirmed that “I still have the exclusive constitutional prerogative to accept (or reject) any such request – this was not contested by the STF judges”. Thus, many thought that Cunha’s outline of impeachment procedures was a conscious “distraction” placed at the feet of the PT and the Dilma government who reacted as predicted.

A Cartoon by Caruso/O Globo, 16-Oct-2015

Pres. Dilma & Dep. Eduardo Cunha: “So, we will fall together?”
In Brasília there are “versions” that the Dilma government proposed a “tit-for-tat” negotiation with Cunha that in exchange for his refusal to approve any impeachment petition, the Government would mobilize a majority on the Ethics Committee to impede any expulsion procedure against Cunha to be initiated. To this end (according to these versions), Dilma’s new Chief of the Casa Civil, Jaques Wagner, secretly met with Cunha at a hanger in the military airport in Brasilia to discuss this offer. The problem is/was that the Dilma Government has totally lost control of its support coalition in the Chamber. Apparently, this bargain offer came to naught. Reportedly, Cunha has at least 15 of the 21 members of the Chamber Ethics Council in his favor.

Also on 13th and 9th October, two other events took place:

1) Pres. Dilma flew to São Paulo where she participated in the opening of the 12th National Congress of CUT (the Labor Union Central linked to the PT) on 13th October in the presence of Lula and the ex-President (now Senator) of Uruguay – José Mujica.

2) Perhaps more “ominous” – On 9th October, the Army Commandant, Gen. Eduardo Villas Boas, speaking to a group of reserve officers (R2) in a video conference regarding what he called “the risk of a severe social crisis in the country”. “We are worried because this might become our [the Army’s] problem”, he said. Continuing, he affirmed “We are living in an extremely difficult and critical situation, a very serious crisis of a political, economic and ethical nature, and with concern that, if this persists, it might be transformed into a social crisis with negative effects for stability”.

Photo: Joel Rosa/Em Tempo
Want More? On 16th October, the Army announced that it its operating budget suffers any further cuts that it would no longer be able to monitor and police Brazil’s frontiers. So far in 2015 (after nearly 10 months), the Army’s budget has suffered 24% “contingency” – not spent (yet) in lieu of fiscal austerity. Sifron (frontier monitoring), for example, has 37.5% of its R$ 2.2 billion “retained” in 2015. This contingency policy has impacted Brazil’s defense industry as well.

1.2 – Cel. Brilhante Ustra dead at 83

On 15th October, Army Coronel (rt) Carlos Alberto Brilhante Ustra died at the Santa Helena hospital in Brasília and reinforced the concept of impunity in Brazil. He had been hospitalized since 24th September with a severe case of pneumonia.

Ustra was in command of the DOI-Codi prison in São Paulo (1970-1974), the largest of the many repression/interrogation/torture centers in Brazil during the military dictatorship (1964-1985).

Ustra (as an accused torturer) surfaced in the Brazilian Press in May 1985 during the first state visit by Pres. José Sarney (to Uruguay). On these visits, Brazilian Presidents usually are accompanied by an entourage that includes members of Congress. In this case, Dep. Bete Mendes (PMDB-SP) took part in this visit. During the big reception party for Sarney, Mendes spotted Brilhante Ustra across the salon. He saw that she had recognized him and so he made his way through the crowd to “chat” with her. As an undergrad student at USP, Mendes had been arrested and taken to DOI-Codi where she was tortured to reveal information about her militant, anti-regime student colleagues. Ustra tried to explain to her that due to his “intervention” she received “light” torture and was not killed. Instead of making a BIG scene during this reception (screaming and pointing her finger as “this torturer”), she remained silent. BUT after returning to Brasília, she published an “open letter” to Pres. Sarney protesting that Brazil was being represented in Uruguay (Ustra was the Brazilian Military Attaché attached to the Brazilian Embassy in Montevideo) by a “notorious torturer, and that he should be recalled immediately.

This created the first military crisis in the new Sarney government. The Army held firm that Ustra would not be recalled and that Mendes’s letter was an offense to Brazil’s Armed Forces. Sarney
did not react and after a few months Ustra returned to Brasília but was “passed over” and not promoted, and thus was forced to retire. This was the “way out” (option) used by the Army.

Ustra resided in the Lago Norte region in Brasília after returning from Uruguay and published several books defending his role in the “glorious” military revolution that “saved Brazil from Communism”.

**Photo: Sérgio Lima/Folhapress**

### Brilhante Ustra testifying before the Truth Commission

In 2012, he became the first military officer accused of torture to be convicted in a São Paulo court – kidnapping, disappearance of a torture victim and ordered to pay a financial recompense to the relatives of Journalist Luiz Eduardo Merlino. These convictions were still under appeal.

In 2013, Ustra was convoked to testify before the National Truth Commission in Brasília where denied the accusations and merely repeated the arguments he had used in his books.

**Video Link ➔** [http://tvuol.tv/bpddDB](http://tvuol.tv/bpddDB)

### 1.3 – Capt. Curió admitted killing 2 rebels in Araguaia

After several attempts to avoid appearing before 1st Circuit Federal Judge Solange Salgado in Brasília, she ordered the Federal Police to use “coercion” to bring Curió to her court. On 14th October, retired Army Major Sebastião Rodrigues de Moura, age 77, known by his nickname Major Curió, participated in a very long testimony/inquest (1:30 p.m. until 11:00 p.m.) where he admitted to had killed two guerrilla fighters during the **Araguaia War** – Antonio Theodoro Castro and Cilon Cunha Brun – and indicated where they were buried. He alleged that the two tried to escape and were shot down and were not “executed”.


Last week, the same judge determined that the PGR investigate the millions of reais spent by a presidential task force in search of the remains of those killed in the Araguaia War. After three years of “investigations”, this task force discovered nothing.

### 2 – FOREIGN RELATIONS & TRADE
2.1 – Daniel Scioli ➔ Brasília

On Tuesday, Argentina’s kirchnerista presidential candidate, Daniel Scioli, visited Brasília in order to garner a PhotoOp with Pres. Dilma Rousseff and support for his candidacy. In route to Brasília, Scioli will stop in Montevideo to receive support from President Tabaré Vázquez. Lula already visited Buenos Aires and participated in several of Scioli’s political rallies. Former Uruguayan President José Mujica and the current Bolivian President Evo Morales have also lent their support. These efforts are to reinforce Scioli’s image as an international leader. The Argentine elections are scheduled for Sunday, 25th October.

A poll conducted by Poliarquia on 2-7 October showed Scioli (Frente para la Vitória) with 37.1% preferences and Mauricio Macri (Cambiemos) with 26.2%. The third candidate, Sérgio Massa, had 20.1%. Thus, Scioli is close to polling 40% with a 10 pp spread ahead of Macri. Under the Argentine election rules, this would assure his election on the first round.

2.2 – Dilma receives support from Unasur

On 13th October, the Secretary-General of Unasur, Ernesto Samper (former President of Colombia) visited Brasília and had a meeting with Pres. Dilma. Samper said the “Unasur supports Pres. Dilma and opposes any attempts to remove her from office. She is honest and was elected democratically and we hope that the Brazilian Congress respects Brazil’s Constitution”.
2.3 – Brazil ➔ TPP, perhaps?

During a trade conference in Brasilia, on 14th October, MDIC minister Armando Monteiro Neto (PTB-PE) affirmed that Brazil “might” decided to join the TPP IF Mercosur “flexibilized” its rules.

3 - REFORMS

Nothing this week.

4 – PRIVATIZATION & REGULATION

Nothing this week

5 - ECONOMICS

5.1 – Yet another downgrade ➔ to the “edge of junk”

This time, on 15th October, Brazil’s sovereign credit rating was downgraded by Fitch Ratings from “BBB” to “BBB-” with a negative outlook ➔ still one notch above “junk bond” [speculative] status. Recently, S&P downgraded Brazil to speculative status.

Fitch affirmed that the rationale behind its decision was: 1) rising government debt burden; 2) increased challenges to fiscal consolidation; and 3) a worsening economic growth backdrop. This economic underperformance will persist due to political uncertainty following the Petrobras corruption scandal and should continue to erode business and consumer confidence, and delay a rebound in corporate investments. The impact of the recession on government revenues was greater that the government anticipated.

Rafael Guedes, Director of Fitch Ratings in Brazil, said that the continued negative outlook means that there is a 50% chance that Brazil might suffer an additional downgrade within two years. Fitch does not normally downgrade by two notches, he added.
At a press conference on 16th October, Fitch Director for Risk Analysis in NY, Shelly Shetty, affirmed that Fitch does not count on the CPMF being included in the 2016 budget and thus is awaiting Brazil’s “Plan B” to cover the large “budget gap” anticipated for 2016.

Moody’s also maintains Brazil with an “investment grade” rating. If Fitch or Moody’s become the second risk agency to downgrade Brazil into the “speculative” category, this would require most investment funds to withdraw their funds from Brazil, which would be a terrible blow to Brazil. Most of Brazil’s politicians don’t understand that “they are playing with fire” by impeding the installation of severe fiscal austerity for 2016 as a way of restoring confidence in Brazil and reversing the worsening economic recession.

Carlos Kawall, Chief Economist at Banco Safra and former Treasury Secretary stated – “Given the rapid deterioration of the Brazilian economy, we need to resolve the fiscal situation for 2016 or we could see debt rise even more quickly. . . We gained some time with Fitch leaving us at investment grade, but not for a lot of time”.

“The Day After” the Opposition affirmed that this downgrade was expected (most investors agreed) and that the blame rested on the disastrous policies of the Dilma government. Dilma’s senate floor leader Delcídio Amaral (PT-MA) said the blame was due to the Congress not passing the president’s fiscal austerity proposals.

S&P also joined the fray on 15th October by affirming that Brazil has more companies at risk of a credit downgrade than any other emerging market. Of the 134 potential downgrades for emerging market firms, 28 are Brazilian.


See http://www.wsj.com/articles/brazil-economic-outlook-has-negative-trend-fitch-says-1444916606

See http://www.ft.com/intl/cms/s/0/8d5e07ca-b3a9-11e3-bc21-00144fabadc0.html#axzz3oettu7or

5.1.1 – Government “concerned”

Reportedly, the Dilma government is extremely worried about a “new ghost” on the horizon – Moody’s -- that this agency might follow the lead of Fitch and downgrade Brazil one more notch, from “Baa3” to “Ba1” (speculative grade) – because all of Brazil’s economic indicators are already at the same level as those in nations rated at this same level (Ba1).

5.2 – Retail Sales decline in August

According to IBGE, in August, retail sales were down by -0.9% YoY and after a major decline of -1.6% in July. The August decline was worse than the median estimate of -0.6% made by 35 economists surveyed by Bloomberg News. This was the seventh straight decline in retail sales. These results reflect the growing unemployment rate, increased inflation, salary reductions, negative job creation and extremely low consumer confidence since January 2015.
The accumulated reduction in retail sales in 2015 is now -3.0% YoY. The worst decline on record was January-August 2003 -5.5%. In August 2015 the 12-month accumulation is now -1.5%. Sales of pharmaceuticals were positive (+0.6% MoM).

5.2.1 – Services also decline

On 15th October, IBGE released the results of its PMS (Monthly Survey of the Services Sector) for August that showed a decline of -3.5% YoY. This shows the impact of the 2015 recession of spending decisions by families – to reduce expenditures for services, similar to the decline in retail sales seen above.

5.3 – Buying power declined

According to the Consultoria Tendências, the buying poser of Brazilians has declined by -7.0% so far in 2015 and by the end of the year should post a -7.7% decline. It is estimates that in 2016, buying power should decline by another -1.6%.

5.4 – Recession hits some states more than others

In a projection prepared by Banco Santander, the data showed that some states are being impacted more by the 2015 recession that others. The worst projections are – Pernambuco (-4.0%), Amazonas and Goiás (-3.8%) and Paraíba (-3.7%). Those impacted less are Mato Grosso do Sul (-1.1%), Espírito Santo (-0.3%) and Pará (0.0%) See [http://oglobo.globo.com/economia/para-sera-unico-estado-sem-recessao-aponta-estudo-17779291](http://oglobo.globo.com/economia/para-sera-unico-estado-sem-recessao-aponta-estudo-17779291)

5.5 – 2015 deficit now at R$ 60 billion

In an attempt to avoid a “crime of responsibility” in 2015 that could be used as grounds for the impeachment of Pres. Dilma, the government has now estimated that the 2015 deficit is R$ 60 billion (1% of GDP). This increase is because the government has paid off all the “loans” from the public banks (BB, CEF, etc.) that were used to finance Dilma’s “social programs”. Obviously, the large defect will not be covered by the CPMF – if and when it is approved by Congress. The estimate of this deficit had been R$ 20 billion.

5.6 – IBC-Br declined -0.76%

On 16th October, the Central Bank released its IBC-Br (Economic Activity Index) for August -0.76% MoM. This index is seen as an indicator (proxy) for Brazil’s GDP. The Central Bank should release the IBC-Br for 3rd Q/2015 on 13th November and IBGE should release the GDP data for 3rd Q/2015 on 30th November.

The 30 economists surveyed by Bloomberg News under-estimated the IBC-Br decline in August (-0.61%). The 12-month decline is now at -4.47% that indicates that Brazil’s GDP might retract even more than the -3.0% decline now predicted by most investors, the IMF and the World Bank. In the January-August 2015 period, the IBC- Br declined by -2.99%
If Brazil suffers two successive years of GDP decline, recession might turn into depression – the worst since the Great Depression in 1929.


5.7 – Industrial employment continues to decline

On 16th October, IBGE released data for industrial employment in August ➪ -6.9% YoY. This was the 47th consecutive month with YoY declines – almost four years!! The decline in work hours paid was even worse ➪ -7.5% YoY. The reduction in the number of industrial workers employed in the January-August period was -5.6% compared with the same period in 2014.