Brazil Focus –
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Weekly Report –
Aug. 29-Sept. 4 2015

Looking Ahead ➔ What to watch for?

- 5th Sept. – Brazil vs. Costa Rica – soccer game, Red Bull Arena, Harrison, NJ
- 7th Sept. – Labor Day (National Holiday in US)
- 7th Sept. – Independence Day [National Holiday, Brazil]
- 8th Sept. – Brazil vs. US – soccer game, Gilette Stadium, Foxborough, MA
- 8th Sept. – FGV to post August IGP-DI ➔ %, % in 2015, 12-months ➔ %
- 9-10 Sept. – XIX Annual CAF Conference – Washington, DC
- 10th Sept. – IBGE to release industrial employment data for July ➔ % MoM
- 11th Sept. – *Caged* data for August ➔ new jobs created *versus* in July
- 14th Sept. – IBGE to announce retail sales data for July, % MoM,
- 14th Sept. – Central Bank ➔ IBC-Br (index of economic activity) for July, % MoM
- 14th Sept. – IBGE to release PNAD (National Sample of Households) report
- 18th Sept. – IBGE to post IPCA-15 ➔ +% vs +% in August
- 19th Sept. – State Holiday in Rio Grande do Sul [*Farroupilha Day*]
• 23-24 Sept. -- Pres. Dilma to attend the 70th UN General Assembly session
• 23 Sept. -- SRF to announce tax collections in August ➔ R$ billion, +% YoY
• 25th Sept. -- IBGE to announce August unemployment ➔ %
• 29th Sept. -- Public Accounts data for August
• 29th Sept. -- FGV to post September IGP-M ➔ % versus % in August
• 30th Sept. -- August Industrial Growth ➔ % MoM & % YoY
• 1st Oct. -- Trade Balance for September ➔ US$ billion ( % YoY)
• 5th Oct. -- Auto production in September, units sold

1 - POLITICS

1.1 – Suspected Acordão

Last week, during his ten-hour cross examination/testimony before the Senate CCJ on 26th August, PGR Rodrigo Janot Monteiro was questioned several times regarding whether he had negotiated a secret accordão with Pres. Dilma Rousseff in order for her to re-appoint him for another two-year term as chief federal prosecutor. He emphatically denied any accordão [“big” accord or agreement] – saying “To carry out such an agreement, I would have to work this out with the 20-member federal prosecutor team in Curitiba, as well as the federal police investigators and federal judge Sérgio Moro”. The senators present appeared satisfied with the PGR’s answer.

However, this week there are suspicions that such an accordão was indeed established with Pres. Dilma ➔

1) One week before his reappointment, on 20th August, Janot denounced Chamber President Eduardo Cunha (PMDB) at the STF alleging that he had received US$ 5 million from bribes collected in the Petrobras scandal. Simultaneously, the PGR also denounced Sen. Fernando Collor (PTB-AL). The press why Cunha was singled out from a list of some 50 politicians accused in the Lava Jato investigations; and

2) Based on plea bargaining testimony obtained from some executives accused in the Lava Jato investigations who alleged that their firms had been “coerced” to make “legal” campaign contributions to Pres. Dilma’s reelection campaign in 2014 (using illicit funds obtained in the Petrobras corruption scandal), the TSE decided to re-open its analysis of those accounts that had been approved in December 2014 (before the plea bargaining information became available. On 21st August, TSE Vice-President Gilmar Mendes officially requested that federal prosecutors prepare a report based on the information compiled in Curitiba regarding these “coerced” campaign contributions.

On 31st August, after he was re-confirmed by the Senate on 26th August, Janot refused to attend the TSE request saying that “it would be inconvenient for the federal Courts and federal prosecutors to become exaggerated protagonists of a spectacle of democracy” and that “society is not interested in perpetuation of election controversies”. Most analysts concluded that the PRG’s response was “very strange”.
In the case of Deputy Eduardo Cunha, analysts claimed that he was singled out because he had become the main politician in Congress leading opposition to Pres. Dilma and had formally declared this opposition in June 2015. Also, it would be his exclusive prerogative (as Chamber President) to install impeachment proceedings against the President.

In the case of the TSE, if the election court discovered that illicit corruption funds had been contributed to Dilma’s reelection, possibly the TSE might decide to remove the whole PT-PMDB presidential slate from office – President Dilma Rousseff and Vice-President Michel Temer.

1.2 – Lava Jato

The week of 31st August → 4th September, a sub-group of members of the Chamber CPI investigating the Petrobras corruption scandal traveled to Curitiba in an attempt to take testimony of several of the accused in this scandal. In vain – this was considered a “junket” because the accused refused to answer their questions – including José Dirceu and Marcelo Odebrecht.

On 1st September, the Federal Police indicted 14 of the accused → José Dirceu, his brother Luiz Eduardo de Oliveira e Silva & his daughter Camila Ramos de Oliveira e Silva, Roberto Marques [Bob] & Júlio Cesar dos Santos (Dirceu’s employees), Milton Pascowitch & his brother José Adolfo Pascowitch, former PT national treasurer João Vacciari Neto, ex-Petrobras Director Renato Duque, Engevix executives Gerson Almada, Cristiano Kok & José Antunes Sobrinho, and half-brothers Fernando and Olavo Moura (the Hope & Personal firms).

The Lava Jato investigation has now “fingered” a father-son “team” – Sen. Benedito de Lira (PP-AL) and Dep. Arthur Lira (PP-AL) – accused of receiving campaign contributions from the cartel of construction/engineering firms involved in the Petrobras corruption scandal. However, Dep. Arthur Lira is the current chair of the Chamber CCJ → the key “gatekeeper” committee in the lower House. For this reason, the Federal Police have asked for his removal from the CCJ. Detail: Dep. Arthur Lira is one of Dep. Eduardo Cunha’s “boys” and was designated CCJ Chair by Cunha.

1.2.1 – 13 indicted on Eletronuclear case

On 3rd September, Federal Judge Sérgio Moro accepted the brief from federal prosecutors and indicted 13 of the accused of perpetrating corruption regarding the contracts for the construction of the nuclear power plant – Angra 3. Those indicted included retired Navy Admiral Othon Luiz Pinheiro da Silva (President of Eletronuclear) and his daughter Ana Cristina, plus executives of two construction firms – Andre Gutierrez and Engevix.

1.2.2 – FUP calls strike against Petrobras

On 1st September, FUP [Petrobras Employees’ Labor Union] called an unlimited general strike to begin on Sunday, 6th September. This is a “political strike” aimed at forcing the state petrol enterprise to revise its disinvestment program (sell off assets) – that will cause sacking of workers.

1.3 – Budget proposal for 2016
On 31st August, the Executive Branch delivered its 2016 detailed budget proposal for 2016. Back in July, Congress had already approved the 2016 LDO (Budget Outlines Law). This proposal was quite complicated and stimulated negative reactions, because it contains a R$ 30.5 billion deficit. This was called “realistic” and “transparent” by the Dilma government.

However, at the news conference convoked to present the 2016 budget proposal, the discomfort of Finance Minister Joaquim Levy was quite obvious. Once again he had been “defeated” – by Planning Minister Nelson Barbosa and Casa Civil Chief Aloísio Mercadante. Levy had pressed for a budget proposal with a small surplus or “zero” – with some tax increases and more cuts in expenditures – but his defeat was sanctioned by Pres. Dilma. This was considered by many an “irresponsible budget proposal”. Others said “Finally the government has stopped lying”. Now – the difficult and biting question is – “When will Levy extricate himself from this difficult situation?”

This is a very negative signal for the sovereign risk evaluation agencies – S&P, Moody’s and Fitch -- because it clearly demonstrates that Brazil is not very serious in carrying out a realistic fiscal austerity program to produce a primary surplus in 2016. A group of deputies circulated a petition to deliver to President of Congress Senator Renan Calheiros (PMDB-AL) urging him to return this budget proposal to the President as “unacceptable”. However, Calheiros said that he would not return the proposal and that Congress would have to work to revise same. Chamber President Eduardo Cunha is also against the strategy of devolution. Market reactions in Brazil were very negative. From NY, Fitch Ratings reacted quickly on 1st September

1) The proposed budget deficit shows that Brazil has great difficulty in balancing its public accounts; and
2) The Fiscal scenario is “much worse” than observed in April when Fitch downgrades Brazil to “negative outlook”.

Deputy Ricardo Barros (PP-PR), who is the reporter of the joint budget committee in Congress affirmed that the 2016 budget proposal deficit might reach -R$ 70 billion. Barros added – “It is better to increase taxes rather than be downgraded [to junk bond status]”.

Some analysts have called this desperate Brazilian situation the “perfect storm” that conjugates China, a deficit in 2015, fears of a downgrade, the political crisis, the Lava Jato investigation and a very weak president.

A CARTOON BY CHICO – O GLOBO
Elder statesman, former Finance Minister and ex-deputy – Antonio Delfim Netto has described this situation as a “Fiscal Tragedy”. See ➔ http://www1.folha.uol.com.br/fsp/opiniao/231572-tragedia-fiscal.shtml

On Thursday, 3rd September, the Chamber approved MP 675 that increased the CSLL on financial institutions from 15% to 20% as 1st September 2015. This MP must also be approved by the Senate. After 31st December 2018, the CSLL on banks would return to 15%.

➔ “Lose the battle and lose the war”. This conclusion implies that Dilma 2.0 is a replica of Dilma 1.0 – the same mistakes and the same modus operandi. Instead of cutting (or at least not increasing) expenditures, Pres. Dilma imposed a 2016 budget proposal with increases in expenditures ➔ 1) Increases in obligatory spending (entitlements) of R$ 88.3 billion; 2) Increases in “discretionary spending” from R$ 16.5 billion to R$ 21.7 billion (new hiring and salary increases); and 3) public debt (1.2% of GDP).

1.4 - Dilma Rousseff – A VERY “Lame Duck” president

Another biting [unanswerable] question in Brasília is the tenure of Pres. Dilma Rousseff – “What probability that she will not finish her second term?” Some say 50%, others 85%, and some 35%. Some describe her second term as a total lack of governance ➔ zero governability. This void created y a very weak and incapable president has been quickly filled by a more active Congress that in the first eight months of her second term has rearranged Montesquieu’s concept of “checks and balances” in a presidential system.
Via a PEC that raised the mandatory retirement age for STF judges from 70 to 75 deprived her of the prerogative of naming another five judges in her second term. Other PECs are being deliberated by Congress, for example ➔ all presidential appointments to state enterprises (Presidents and Directors) would have to be confirmed by the Senate AND would have to have at least five years of [private sector] “market experience”.

Pres. Dilma is threatened by two “removal” possibilities: 1) Impeachment (crime of responsibility) that might be based on Congress rejecting her 2014 public accounts (via a recommendation from the TCU); and 2) Removal of the PT-PMDB slate (President and Vice-President elected in 2014 by the TSE after the Election Court examines evidence collected by the Lava Jato investigation that “legal” (declared) campaign contributions from construction/engineering firms involved in the Petrobras corruption case were “coerced” by the PT and came from “illicit” sources.

On 3rd September, during a presentation to SP business leaders, Vice-President Michel Temer (PMDB-SP) said that with such a very low approval rating (7%), Pres. Dilma probably would not be able to complete her second term in office. The organizer of this event then asked – “What happens?” Temer replied – “I can’t anticipate anything . . . What can I say? . . . What can I do?”

Want more? Reportedly, some 50% of the PMDB deputies are now in favor of impeachment. See ➔ http://josiasdesouza.blogosfera.uol.com.br/2015/09/04/impeachment-ja-e-apoiado-por-507-dos-deputados-federais-do-pmdb-de-temer/

Even more? Apparently, the PMDB is on the way toward a “total break” with Pres. Dilma and her government and plans to exit the government coalition – perhaps after its national party convention in November. They calculate that by November the economic crisis (recession) will be much worse to the point of mobilizing classes C & D into massive street protests AND Congress will have rejected Dilma’s 2015 accounts, thus paving the way for impeachment proceedings to be installed OR the resignation (exit) of the President. ➔ Stay tuned!! See ➔ http://painel.blogfolha.uol.com.br/2015/09/04/ala-do-pmdb-ligada-a-temer-blinda-levy-e-pressiona-saida-de-mercadante/

A cartoon by Sponholz
1.4.1 – “Green & Yellow” on 7th September?

On Thursday, 3rd September, the online site of the PT convoked party militants to actively participate in the Independence Day festivities in defense of democracy, Pres. Dilma and Lula, and against any golpe – wearing green & yellow colors. Less than 24 hours later, this convocation (green & yellow) was rescinded – because someone remembered that in August 1992, then Pres. Collor convoked “his militants” [were there any left??] to demonstrate in his favor wearing green & yellow. At that point, the Chamber of Deputies was deliberating whether (or not) to approve his impeachment. The favorable vote to impeach Collor was on 30th September 1992. Instead, the large number anti-Collor militants wore black and many youth appeared with “painted faces”. Obviously, the PT is fearful that the anti-Dilma militants might déjà vu 1992 – and demonstrate wearing black with “painted faces”.

Apparently, Pres. Dilma will be on the reviewing stand for the “patriotic” Independence Day military parade in Brasília next Monday. There is concern that she might be booed and jeered by militant spectators who probably will be wearing black with painted faces.

⇒ Stay tuned for this Parade next Monday!!

1.4.2 – Continued tenure of Finance Minister

On Thursday, 3rd September, Brasília was saturated by rumors that Finance Minister Joaquim Levy was resigning (had resigned) his post because he did not travel to Turkey for a meeting of the G-20 finance ministers. Rather, he was summoned to a meeting with Pres. Dilma with the presence of Casa Civil Chief Aloisio Mercadante and Planning Minister Nelson Barbosa – billed as a meeting to decide the government’s strategy to approve the 2016 budget proposal by Congress and policy changes to “balance” this proposal and avoid a “built-in” budget deficit.

Apparently, Levy was convinced to stay on and later in the day embarked for the G-20 meeting in Turkey. The problem is that Levy was “defeated” on the final draft of the 2016 budget proposal and frustrated by “quick policy turnarounds” by Dilma plus “defeats” inflicted by the Chamber of Deputies where Dilma has no control over the government coalition “majority”. Mercadante (ironically) was
the “designated” spokesperson to announce to the press that Levy would continue as Finance Minister – at 5:40 p.m.

Had Levy left the Dilma government, a “downgrade” by S&P, Fitch and Moody’s would have been moved up to October 2015 from the “possible” date in early 2016. However, the market reacted swiftly to all this uncertainty – the US$ FX rate jumped up to R$ 3,76 in SP and might reach R$ 4,00 by the end of the month. Stay tuned!!!

1.5 – Pres. Dilma suspended Paulo Bernardo appointment

On 27th August, Pres. Dilma decided to suspend the appointment of former Communications Minister Paulo Bernardo (PT-PR) to be the new co-Director of the Itaipu Bi-National hydro power complex. This post is considered a “rich political plum” for any Paraná politician. The Reason? Paulo Bernardo’s wife, Sen. Gleisi Hoffmann (PT-PR), had been accused of receiving bribe (illicit) funds from firms accused in the Lava Jato investigation (Operation Pixuleco 2) to finance her campaign for governor in 2014.

1.6 – Gender Gap in Brazil

On 4th September, IBGE released its Demografia das Empresas research report based on data collected in 2013 that showed that on average women earn -40.5% less than men at the same functional levels in these firms – Men (R$2.118,66) and Women (1.507,69). Also, unemployment among women is 9.6% and among men in 6.6%.


2 – FOREIGN RELATIONS & TRADE

2.1 – Foreign Trade

On 1st September, MDIC released Brazil’s foreign trade data for August ➔ a surplus of +US$ 2.689 billion. Imports continued to decline (due to FX changes) and posted US$ 12.796 billion (-33.7% YoY). Exports also declined by -24.3% YoY ➔ US$ 15.485 billion. In 2015, the trade surplus is now US$ 7.297. The first 8 months in 2014 posted a trade deficit of US$ -4.10 billion. The same period in 2011 posted a surplus of US$ +29.8 billion and +US$ 19.4 billion in 2012.

With the release of the 2016 annual budget proposal with a -R$ 30.5 billion deficit and the negative news from China – on 1st September the FX rate topped R$ 3,70 per dollar – the highest rate since 2002. If the FX rate continues to increase, imports will decline even further in September.
3 - REFORMS

3.1 – Administrative Reform

As reported earlier, Pres. Dilma is contemplating reducing the number of posts in her cabinet (by perhaps ten) and the number of political appointments. Suspecting that his Central Bank position might lose cabinet status, Alexandre Tombini communicated to the President’s office that the loss of cabinet status by the Central Bank would remove its Supreme Court ‘cover’ (whereby cabinet ministers can only be prosecuted by the STF). Thus, the Central Bank President could be sued and prosecuted by first level federal courts. This would expose the CB President to a “wave” of these suits by persons and firms discontent with Central Bank decisions. Indirectly, Tombini indicated that if this “reform” occurred that he would resign.

3.2 – Political Reform

On Wednesday, 2nd September, the Senate approved a measure to prohibit campaign contributions from businesses and firms. The Chamber had already approved a PEC allowing contributions by firms but only to parties and no longer to individual candidates. If this bicameral “ping-pong” continues with no solution before 2nd October, there would be no impact on the 2016 municipal elections. Perhaps now the STF might finalize its deliberations to declare such contributions unconstitutional.

4 – PRIVATIZATION & REGULATION

4.1 – Enel to invest US$ 600 million in Solar Farms

On 1st September, Enel Green Power announced plans to invest US$ 600 million in new solar farms in Brazil. Last week the Italian utility won contracts to sell power from three solar farms in northern Brazil and is now the largest supplier of solar generated electricity in Brazil. The three sites are in Horizonte MP (103 Mw), Lapa (158 Mw), and Nova Olinda (292 Mw) to come online in 2017. Aneel plans another 1,000 Mw solar power auction in November 2015.

In 2014, Enel Green Power posted a 32 billion kWh generation capacity worldwide from water, sun, wind and geo-thermal sources – enough to supply some 11 million households.

5 - ECONOMICS

5.1 – Copom maintained basic Selic rate

Meeting on 1-2 September, Copom decided to maintain the Selic rate at 14.25% -- in spite of the FX rate with the US$ approaching R$ 4,00 and inflation at nearly 10.0% (double the Central Bank’s target (4.5%). Most observers agreed with this decision, reasoning that an increase in the Selic rate would make Brazil’s recessive economic situation even worse.
5.2 – Industrial Production

On 2nd September, IBGE announced the IP data for July -8.9% YoY & -1.5% MoM. This was the 17th consecutive decline in Brazil IP. The accumulated 12-month retraction by sector was capital goods (-16.8%), consumer goods (-6.2%), intermediate goods (-3.2%), food (-6.2%) and beverages (-6.2%).

5.2.1 – Auto Production

On 4th September, Anfavea released the auto production data for August 216,500 units (-18.2% YoY and -3.5% MoM). In the first 8 months in 2015, 1.73 million units were produced (-16.9% YoY). In August, auto sales posted 207,300 (-23.9% YoY & -8.9% MoM).