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BRAZIL PRESSES FORWARD WITH ECONOMIC REFORM, SOLIDIFYING A FRESH START

*C. Gabriel Sánchez** and *Augusto Perez***

A BALANCED APPROACH TO ECONOMIC RECOVERY

Brazilian President Lula da Silva (“Lula”) is leading a substantial public effort to maintain the economic momentum established by his predecessors and improve Brazil’s attractiveness to foreign investors. His work extends across the domestic and international agenda and aims to mitigate Brazil’s culture of strong governmental intervention, protectionism, and reluctance to respect and enforce contracts with foreign parties. The debate over Brazil’s instability in financial markets has forced Lula to push economic reform to the forefront of the government’s agenda.

DOMESTIC IMPROVEMENTS PREPARE FOR ECONOMIC GROWTH

Leading this domestic economic reform, Lula, a former union leader, has switched his previous leftist discourse to a more conciliatory tone. Recognizing the advantages of a functioning market economy, he has appointed Henrique Meirelles, former global President of BankBoston, to preside over Brazil’s Federal Reserve. “Inflation is low, under control, and this is a very important

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factor... for sustainable growth,” Meirelles said at a press conference at the Council of the Americas in New York.¹

To further encourage foreign investment, Brazil’s finance minister, Antonio Palocci, has recently announced a program called “Invest Now,” which consists of expedited tax refunds for federal taxes paid by businesses operating in Brazil. These expedited refunds are coupled with significant federal tax relief as well as specific tax cuts on insurance, financial operations, industrialized products, and construction investments. Additionally, an ongoing effort exists to shrink administrative bureaucracy, and the Brazilian Congress has passed a new law modernizing the Judiciary.

To support these federal policies the Lula administration is also addressing the social welfare needs of Brazil by implementing two programs: “Zero Hunger” and “The First Job.” The former is similar to the American system in guaranteeing minimum food standards and meeting basic nutrition needs. The latter grants financial benefits to businesses that hire applicants between the ages of 17 and 24. Together, these programs seek to boost the economy and support Brazil’s growth by providing industry with a healthy and proficient workforce.

INTERNATIONAL FOCUS YIELDS ECONOMIC SUCCESS

Lula’s programs are succeeding in attracting the attention of the international community. Recently, IMF Managing Director Rodrigo Rato stated, “The

¹ *Brazil Inflation Low; Under Control-CenBank Head*, Reuters, (April 13 2005) at <http://www.counciloftheamericas.org/coa/publications/News/April/MeirellesReuters.pdf>.

advances made by the Brazilian government are very impressive ... These courageous policies have paid off. Brazil's vulnerabilities have been reduced and the increased resilience has helped [it] to weather recent global market turbulences. GDP growth is now robust, benefiting from continued strong export performance, a pick-up in domestic demand, and rising wages and employment."² In late November of 2004, Brazilian newspapers reported that GDP had reached its highest level in eight years.

Lula's policies are succeeding in positioning Brazil in global markets as well as in the global political process:

- ◆ Petrobras, the Brazilian oil company, plans to invest US\$7.0 billion abroad to increase exports from and imports into Brazil.
- ◆ Spain has congratulated the Brazilian-Hispanic Forum wherein European businessmen are introduced to investment opportunities in Brazil, such as the port of Santos and the Metro expansion in São Paulo.

The results of these practices are evident. In 2004 Brazil imported US\$52 billion, a 10% increase over the same period in 2003 when imports were US\$47 billion.³

Through the World Economic Forum, Brazil is leading a world effort to fight starvation by sponsoring a tax to fund welfare programs in Africa. Lula has united India, China, and South Africa in forming the G-20, a group of developing nations united against agricultural subsidies in the U.S. and the EU.

² Press Release, IMF (Sept. 03, 2004) *n. 04/186*.

³ This amount does not include foreign direct investment.

Environmental successes are also part of the economic success story in

Brazil:

- ◆With the February 2005 implementation of the Kyoto Protocol on Global Warming, the Brazilian methanol industry has taken center stage for countries seeking early and mid-term solutions.
- ◆China has recently announced an investment of over US\$1.3 billion for the construction of a gas pipeline in eastern Brazil and may invest a further US\$6 billion.
- ◆Japan recently passed a law mandating 3% methanol content for its gasoline, which may represent a substantial opportunity for Brazilian methanol sales to that country.
- ◆The Brazilian Environmental Ministry (equivalent to the U.S. EPA) has prepared a project to lease governmental forests for sustainable uses. This project will create opportunities for foreign investment to establish furniture and other forest product industries to supply domestic and foreign consumption.

OPEN MARKETS CREATE UNLIMITED OPPORTUNITIES

There are very few obstacles to foreign investment in Brazil, allowing

others to enjoy the same successes as illustrated above:

- ◆Small and medium-sized companies are growing in Brazil with sales of more than US\$600 million in 2002. Companies are seeking foreign partners to export their products and services, ranging from jewelry to 'car dry cleaning,' into the U.S. and other markets.
- ◆Many sectors such as healthcare, the environment, transportation, telecommunications, and financial services are growing rapidly and present opportunities for further expansion.
- ◆One particular example is the Public-Private Partnership Act (PPPA), which is designed to fund infrastructure improvements such as energy, railroads,

highways, and ports. The PPPA allows public entities to go to the private sector for the investment capital required for large infrastructure projects.

GETTING THE U.S. TO LOOK SOUTH

Lula and his government are implementing policies and reforms to shift the tendency of the U.S. to look West to China or East to Europe. The Lula administration is working to transform Brazil into a commercial magnet for economic partnerships. The Brazilian Congress is addressing unpopular but necessary issues such as taxes and social security reform. Brazil recently signed the New York Convention, contributing to a rise in arbitration of commercial disputes.

These recent reforms have refreshed the Brazilian investment landscape by creating a more dynamic and competitive economy. Foreign investors have shown a quick and positive response to these changes and have begun establishing a Brazilian market presence through a wide variety of investment structures, helping to boost GDP growth in 2004 to 5.2%.