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THEDIALOGUE

FEATURED Q&A

Will Brazil's Economy Continue to Deteriorate?

Brazilian President Dilma Rousseff is facing an economic contraction, above-target inflation and single-digit approval ratings. // File Photo: Brazilian Government.

Q Brazilian President Dilma Rousseff said in a video released Sept. 7 that a prolonged government stimulus program was partially responsible for the country's recession. Rousseff also said she was committed to austerity measures championed by Finance Minister Joaquim Levy. What are the main causes of the recession in Brazil, which last week lost its investment-grade rating from Standard & Poor's? What path must Rousseff's government take in order to bring the country out of its economic malaise? Does Rousseff have enough support in Congress to push through needed economic reforms? Is Levy doing an effective job as finance minister or should he be replaced?

A João Augusto de Castro Neves, Latin America analyst at the Eurasia Group: "There is little doubt Brazil is undergoing one of the deepest political and economic crises in recent memory. After several years of relative political stability and impressive growth rates, the country is now amid turmoil with no end in sight. In fact, Brazil is poised to experience another lost (half) decade. The recent loss of investment-grade status by Standard & Poor's reinforces that risk. Against a backdrop of a more unfavorable global economy and a massive corruption scandal at home, political ineptness comes at a higher cost. Brasília's reluctance to improve policymaking well before last year's election raised the bar for the kind of actions that are now needed to keep things from spiraling out of control. A more ambitious fiscal adjustment is just the first step of a long and painful road to restore the country's credibility. Unfortunately, amid growing popular discontent and

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TODAY'S NEWS

BUSINESS

Petrobras Chair Taking Leave of Absence

Murilo Ferreira said he will take leave as chairman of the Brazilian state-run oil company until Nov. 30. The move comes amid a heavy debt burden and massive corruption scandal.

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ECONOMIC

Mexico Opening New Trade Office in Arizona

The office will work to boost Mexican exports and attract new investment to Mexico, officials said.

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POLITICAL

Guatemala's Baldizón Exits Presidential Race

Manuel Baldizón, who had been in a close race for a spot in the country's Oct. 25 runoff election, dropped out of the race, saying it had been marred by corruption. Baldizón's withdrawal leaves comedian Jimmy Morales and former First Lady Sandra Torres to face off in the second round.

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Baldizón // File Photo: Baldizón Campaign.

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POLITICAL NEWS

Baldizón Drops Out of Guatemala Presidential Race

Manuel Baldizón, who had been considered the front-runner in Guatemala's presidential race, ended his campaign Monday and quit his political party just more than a week after the election's first round. In the Sept. 6 vote and with 99.09 percent of the ballots counted, comedian Jimmy Morales emerged as the top vote getter with 23.85 percent of the votes, according to the country's Supreme Electoral Tribunal. Former First Lady Sandra Torres and Baldizón were in a close battle for second place, with 19.76 percent and 19.64 percent, respectively. In order to have won the election in the first round, a candidate would have needed 50 percent of the vote plus one. Election authorities did not announce the final results on Friday as expected, and Baldizón's withdrawal means Morales and Torres will face each other in an Oct. 25 runoff. In an interview Monday with Radio Sonora, Baldizón said the first round "lacked legitimacy," adding that he would not endorse either of the two remaining candidates, the Associated Press reported. "I can't endorse anyone who would participate in a process marred by irregularities and corruption," Baldizón said, without making his allegations more specific. In a news conference to announce his withdrawal, he added, "They asked me to accept the results [but] my dignity and my honor are priceless...I do not endorse this electoral process," Reuters reported. Baldizón's status as the front-runner evaporated amid Guatemalans' backlash against traditional politicians following the resignation and jailing two weeks ago of President Otto Pérez Molina in connection with a corruption scandal involving the country's customs agency. The scandal also cost Pérez Molina's vice president, Roxana Baldetti her job in May. Both have denied wrongdoing. [Editor's note: See **Q&A** on Guatemala in Friday's issue of the Advisor.]

> **"I can't endorse anyone who would participate in a process marred by irregularities and corruption."**
>
> **— Manuel Baldizón**

ECONOMIC NEWS

Brazil's Government Announces Nearly $17 Bn Austerity Plan

Brazil's government on Monday announced a nearly $17 billion austerity plan in an effort to boost consumer confidence and get Latin America's largest economy back on track, The Wall Street Journal reported. The proposals are an almost even mix of tax increases and spending cuts and also aim to plug the country's budget hole. Officials designed the package to produce a primary surplus equivalent to 0.7 percent of gross domestic product next year, Planning Minister Nelson Barbosa said in announcing the plan. The current budget for 2016 is projecting a 0.5 percent primary deficit. Among the main proposals is a delay in public servants' wage increases, a move that the government said would save 7 billion reais ($1.8 billion). The initiative is expected to face stiff opposition from labor unions. Tax increases will also be necessary, Finance Minister Joaquin Levy said alongside Barbosa. "The

Barbosa // File Photo: Brazilian Government.

NEWS BRIEFS

Ferreira Taking Leave of Absence as Petrobras' Chairman

Murilo Ferreira, chairman of the board of Petrobras said Monday that he is taking a leave of absence until Nov. 30, The Wall Street Journal reported Monday, citing a statement by the Brazilian state-run oil company. The move raised questions about possible dissent among board members in light of the company's debt burden and the protracted investigation into its massive corruption scandal. Ferreira attributed his leave of absence as being for "personal reasons." He is not stepping down from his role as CEO of Vale, the mining company said.

Colombia Accuses Venezuela of New Airspace Incursion

Colombia's government on Monday accused Venezuela for the second time in as many days of violating its airspace, saying a military plane flew over its territory, Agence France-Presse reported. A Venezuelan military plane flew over Colombia's northeastern Vichada province on Sunday night, air force Commander Carlos Bueno told reporters. The statement came after Colombia said two Venezuelan warplanes flew across its southern border on Saturday, an accusation that Venezuela's foreign minister denied.

Mexico Opening New Trade Office in Arizona

Mexico will open a trade and investment office in Phoenix, Ariz., in a move state officials said was a symbol of a warming bilateral relationship and increased commerce across the border, The Arizona Republic reported Monday. The office will work to boost Mexican exports and attract investment to Mexico, officials said. Phoenix Mayor Greg Stanton added that the office also may mean more jobs in Arizona.

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fiscal effort on the spending side can only go so far," said Levy. The government is looking to do away with several corporate-tax incentives and is also seeking to increase the capital-gains tax and implement a 0.2 percent tax on financial transactions. The controversial tax on financial transactions would add 32 billion reais $8.4 billion) to the government's coffers and would last "not more than four years," said Levy. The speaker of the lower house of Brazil's Congress, Eduardo Cunha, said there was not enough support among lawmakers to approve the financial transactions tax, Reuters reported. The austerity measures were announced less than a week after Standard & Poor's lowered its sovereign rating for Brazil to junk status. A downgrade to junk territory by one more of the two other major ratings agencies could trigger massive sales of Brazilian assets by investors such as U.S. pension funds.

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with low levels of support in Congress, President Dilma Rousseff's room to maneuver is limited. While additional austerity measures are likely, the outlook for needed structural reforms remains bleak. Nevertheless, there are two things Rousseff can do in order to avoid a haphazard muddle-though for much of the remainder of her government. First, give more power and autonomy to her finance minister, Joaquim Levy. Second, hope that an even more acute crisis will raise the sense of urgency among business and political elites to support structural reforms in Congress. In any case, the next couple of years will be at least as difficult as this one."

Beatrice Rangel, member of the Advisor board and director of AMLA Consulting: "Brazil's current recession is the result of a poisonous combination of failed economic policies and structural weaknesses. On the economic policy front, subsidies and transfers needed to be backed by strong growth in fiscal revenues. Without a sincere and holistic tax reform and lack of discipline to reduce evasion on the part of the central government, social subsidies and transfers to the population grew faster the receipts, thereby causing a fiscal imbalance that will be difficult to rein in. Indeed, behind every transfer and subsidy there is an interest group that favors the ruling party. Once removed, these groups will militate against the heretofore benefactor. And popularity losses are not endearing to former President Lula who commands the ruling party and dreams of being elected president once again. The fact that President Rousseff presented Congress with a deficit-ridden budget and that Brazil lost its coveted investment-grade rating from Standard & Poor's are signals to the intractable difficulties faced by policymakers when confronting reductions in expenditures given the political mobilization power of those interests affected by budgetary cuts. On the structural side of the current crises is a lack of rule of law as seen in the truly horrendous degree of corruption exposed by the Car Wash investigation into Petrobras. Corruption sucked away funds from badly needed investments in trade infrastructure, which is what Brazil truly needs to become competitive in the world."

Luiz Kessler, economist at Oxford Economics: "Declining revenues amid an economy in recession, increasing political noise, persistently high inflation and record low confidence levels are some of the factors behind Brazil's ugly economy. Add to that the disagreement between the Rousseff government and Congress (President Dilma now faces a record low 7.7 percent approval rate), the Petrobras corruption investigation and the government's budget proposal with a 0.5 percent of GDP primary deficit estimate for 2016 (suggesting it is not pursuing needed austerity measures). All these factors hamper the fiscal adjustment, challenge fiscal stability and deteriorate confidence levels, which are at record lows. A fiscal adjustment is needed for a rebound

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BUSINESS NEWS

Barclays Closes Jamaicans' Accounts

London-based Barclays announced last week that it is closing all its bank accounts in Britain that belong to individuals with a Jamaican address in order to reduce risk and focus on its core business, the Jamaica Gleaner reported Friday. This move is tied to a global banking trend of retreating from businesses that are perceived to have a higher risk of association with money laundering. Barclays announced in 2013 that it would move forward with a plan to focus on its core business and limit the number of foreign countries in which it operates from 200 to 70. "As a global financial services provider, we evaluate the services we provide on a regular basis. In 2013, we announced that we are prioritizing the need to reduce complexity and that the business will be focusing on a core set of 70 markets globally," said a spokesperson for Barclays. Customers who worked in the United Kingdom and have since retired to Jamaica and are entitled to a pension will need to make arrangements for pension transfers, direct debits and standing order arrangements, according to the Gleaner. Barclays acknowledged that customers may need some time to make those arrangements, and it has offered a 30-day extension or more for customers who request it. The Jamaica National Building Society, or JNBS, has offered transactional services to Jamaicans who have been affected by Barclays' decision.

> **"As a global financial services provider, we evaluate the services we provide on a regular basis."**
>
> **— Barclays spokesperson**

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in confidence and to pave the economic recovery. However, as the recession continues, revenues drop. Finance Minister Joaquim Levy faces opposition both from the Workers' Party and from the right. His inability to make much of an impact on the deficit is a reflection of the broader weakness in the government. To make the austerity plans more complex and tougher, approximately 90 percent of the government's spending is mandatory. As discretionary spending only accounts for 10 percent, the country should pursue structural reforms, such as lowering mandatory spending. Low confidence among businesses and consumers is reflected in lower private investment, which hampers growth. Deterioration in the labor market coupled with persistently high inflation lead to a squeeze in real wage growth as workers lose their bargaining power and see deterioration in disposable income. Increased uncertainty over the country's ability to meet its fiscal target increases investors' risk perception. The real keeps falling in value against the dollar, which should boost exports, but the ongoing slowdown in China also hampers commodity prices. Given his many constraints, Levy is doing the best he can, though he might have underestimated the recession and its implication on revenues. His departure from government would lead to further uncertainty. He is doing a good job, but without support from the government and Congress, it's impossible to achieve his objectives. At the same time, President Dilma is struggling to convince lawmakers to pass important measures to guarantee the country's fiscal stability."

> **"Approximately 90 percent of the government's spending is mandatory"**
>
> **— Luiz Kessler**

Editor's note: The commentaries above were submitted before Brazil's government unveiled its nearly $17 billion austerity plan on Monday.

The Advisor welcomes comments on its Q&A section. Readers can write editor Gene Kuleta at **gkuleta@thedialogue.org**.

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