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FEATURED Q&A

# Will Brazil's Central Bank Succeed at Taming Inflation?

Brazil's central bank, led by Roberto Campos Neto, last week hiked its benchmark interest rate by the largest amount in nearly two decades. // File Photo: Brazilian Government.

**Q** **Brazil's central bank on Oct. 27 raised its benchmark Selic interest rate by an aggressive 150 basis points to 7.75 percent, its biggest rate hike in nearly 20 years and its sixth consecutive hike this year. The increase came a day after the country's statistics institute reported that annual inflation had surpassed 10 percent, with a 1.2 percent monthly rise in consumer prices, the quickest pace since 1995 for mid-October. The previous week, Brazil's real weakened to a seven-month low against the U.S. dollar, trading at about 5.7 reais to the greenback. What is the outlook for economic growth and inflation in Brazil with less than a year to go before the country's presidential election? How much is President Jair Bolsonaro's government expected to ramp up spending before the vote, and how would that affect the economy? Which business sectors are expected to do best in the coming year in Brazil, and which will struggle the most?**

**A** **Joel Korn, president of WKI Brasil and senior international partner at UPITE Consulting Services:** "The central bank's steep increase in the Selic rate was expected, and the upward trend should continue in the coming months in pace with rising inflation, which is now at a double-digit level and significantly above this year's target of 3.75 percent. September inflation was the highest since 1994, driven primarily by price hikes in food, fuel oil and energy tariffs. Moreover, the absence of a clear commitment for fiscal discipline, combined with the uncertainties of congressional approvals for new sources of revenue, is manifested by the likelihood of noncompliance with the mandatory ceiling for public expenditures. Political motivations

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The U.S. House of Representatives approved and sent to President Joe Biden the Renacer Act, which increases pressure on Nicaraguan President Daniel Ortega amid his crackdown on the opposition ahead of the country's planned election On Sunday.

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Ortega // File Photo: Nicaraguan Government.

POLITICAL NEWS

# U.S. Congress Passes Measure to Increase Pressure on Ortega

The U.S. House of Representatives on Wednesday approved legislation, which the Senate previously passed, to increase pressure on Nicaraguan President Daniel Ortega amid his widespread crackdown on the country's opposition, Agence France-Presse reported. The House passed the legislation, known as the Renacer Act, in an overwhelming vote of 387-35 with strong bipartisan support. The Senate approved the measure in August and passed amendments to it on Monday. The bill now goes to President Joe Biden for his signature. The Renacer Act calls for coordination with Canada, the European Union and Latin American and Caribbean countries on imposing sanctions against people obstructing free elections in Nicaragua and also against those committing human rights abuses in the Central American country, AFP reported. It also broadens supervision of loans to Nicaragua from international financial institutions and calls for reviewing Nicaragua's participation in the free-trade agreement involving the United States, Central America and the Dominican Republic. Also, the legislation adds Nicaragua to a list of countries subject to visa restrictions, and it requires additional intelligence reports on activities of the Russian government in Nicaragua, including reports on sales of Russian military equipment to Nicaragua, AFP reported. The U.S. Congress' approval of the legislation came just ahead of Nicaragua's planned presidential election on Sunday. Ortega is running for a fourth consecutive term, and his government since late May has pursued and imprisoned or forced into exile nearly any potential candidate who could pose a serious challenge to him. "With Ortega and [First Lady and Vice President Rosario] Murillo there is no future for Nicaragua; rather they regressed by rejecting the path of democracy," Lucía Pineda Ubau, journalist at 100% Noticias in Nicaragua, told the Advisor before the House of Representatives' passage of the Renacer Act. "They bet on repression to sustain power." Congress' passage of the legislation also came as a group of human rights organizations, including Amnesty International and Human Rights Watch, condemned Sunday's planned elections, saying they "do not guarantee human rights." The human rights groups cited an atmosphere of repression, forced disappearances and restrictions on civil and political rights, AFP reported. Over the past months and as recently as Tuesday, the Advisor has repeatedly sought commentary on the situation in Nicaragua from the country's ambassador to the United States, Francisco Campbell, but he has not responded to the inquiries.

# Int'l Criminal Court Launches Probe of Venezuelan Forces

The International Criminal Court is launching a formal investigation into allegations of torture and extrajudicial killings by Venezuelan security forces under President Nicolás Maduro's government, the first time a country in Latin America is under probe for possible crimes against humanity from the court, the Associated Press reported. ICC Chief Prosecutor Karim Khan announced the investigation on Wednesday following a three-day trip to Caracas. Standing alongside Maduro, Khan said he was aware of political "fault lines" and "geopolitical division" in Venezuela but added that his job was to uphold the principles of legality and rule of law, not settle scores, the AP reported. "I ask everybody now, as we move forward to this new stage, to give my office the space to do its work," he said. "I will take a dim view of any efforts to politicize the independent work of my office." Khan did not detail what exactly the investigation will encompass. However, it comes after a lengthy preliminary probe beginning in February 2018 that looked into allegations of excessive force, arbitrary detention and torture by the country's security forces during a crackdown on 2017 anti-government protests. Human rights groups and the U.S.-backed opposition celebrated the ICC's

NEWS BRIEFS

## Chilean Presidential Candidate Boric Tests Positive for Covid-19

Center-left Chilean presidential candidate Gabriel Boric said Wednesday that he has tested positive for Covid-19 and would self-isolate, Reuters reported. The announcement came less than three weeks before the country's election. Boric is running just behind far-right candidate José Antonio Kast in recent polls, and surveys indicate the two could face each other in a runoff in December.

## Mexican Judge Orders Jailing of Former Pemex Chief Executive Lozoya

A judge in Mexico on Wednesday ordered the former head of Mexican state oil company Pemex to jail as his case is decided, a year after he was extradited from Spain on corruption charges, the Associated Press reported. Emilio Lozoya led Pemex under former President Enrique Peña Nieto, who was in power from 2012 to 2018. Lozoya provided testimony about bribery and corruption involving legislators and former administration officials.

## Commodities Traders File Suit Against Brazilian Coffee Producers

Commodities traders including Louis Dreyfus, Olam and Volcafe are filing suit against hundreds of Brazilian coffee farmers who did not deliver on pre-agreed sales, exposing the merchants to losses, Reuters reported today, citing sources and documents. A 60 percent price surge this year has prompted some farmers to default on sales, affecting coffee supply that was already being disrupted by shipping delays and reduced availability of labor, according to the report. Farmers are reportedly defaulting on pre-agreed sales in a bid to re-sell the coffee at current higher prices.

announcement. "Today's announcement of formal ICC investigation makes clear: #Venezuela is failing to bring to justice those responsible for grave human rights violations and crimes against humanity," Geoff Ramsey, director of the Venezuela program at the Washington Office on Latin America, said on Twitter following the news. "Today's announcement of a formal investigation … is a step toward justice in #Venezuela," he added.

**BUSINESS NEWS**

# ING Announces End to its Financing of Peru Oil, Gas Trading

Dutch lender ING will no longer finance the trading of oil and gas in Peru over concerns about the industry's impact on Indigenous people in the country's Amazonian region, Reuters reported today, citing a company policy document. The move comes after a similar decision earlier this year to stop financing oil trade in Ecuador, an announcement ING made in January alongside Switzerland's Credit Suisse and France's BNP Paribas. The Dutch bank does not directly finance oil and gas exploration and production in Peru, but it has previously financed those who move it out of the country. "Indigenous people living in the Sacred Headwaters of the Amazon in Ecuador and Peru have called on banks to stop financing oil development in the region, as it poses a threat to them and the surrounding ecosystem," the new policy said. A spokesman for ING told Reuters the bank had updated its policy but declined to give any details about ING's financial exposure in the region. "Measures such as these are good headline-makers but marginally helpful at best," Jose L. Valera, partner at Mayer Brown, told the Energy Advisor in a Q&A published Feb. 12, following the banks' initial announcement about Ecuador. "Oil production in the Amazon region presents very serious issues, and the best way to mitigate or eliminate them is by addressing the root cases," Valera added.

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for further spending, particularly in social programs, as the country approaches the 2022 elections reinforce negative market expectations and project escalating interest rates and continued currency devaluation. President Bolsonaro will be increasingly focused on populist measures to boost his chances for re-election. Also, vested interests in the leaders of the Senate (a potential opposition candidate for president) and the Chamber of Deputies (who is aligned with Bolsonaro) will heavily influence Congress' inaction on sensitive legislation. This scenario reinforces the heavy reliance on the central bank's tight monetary policy to mitigate inflationary pressures and signals a continued weak economy in the coming year. Social programs should induce a surge in consumer demand, although their effectiveness will be short-lived, given the inflation-related impact on purchasing power of the targeted low-income population. The informal economy should expand further as the current stubborn 14 percent unemployment rate subsists. Exports, particularly in the agribusiness sector, will evidently continue to benefit from exchange devaluation pressures, while new direct investments will be largely restricted to specific opportunities in infrastructure, productivity enhancements and transactions focused on strategic consolidations. The winner of next year's presidential election will face a huge challenge to reposition the country's economy and restore the confidence of consumers and investors."

**A** **Allison Fedirka, director of analysis at Geopolitical Futures:** "Unfortunately for Brazil, there's little reason to believe 2022 will be much better than 2021. Prospects for growth remain limited, and abating inflation poses a real challenge such that there are already warnings of potential stagflation in the year ahead. Brazil entered the pandemic with a fragile economy that was midway through executing its recovery strategy. This strategy relied on structural reforms (including limits on government spending), efforts to increase the economy's attractiveness to investors and dependence on global trade to spur economic growth. When the pandemic hit, the subsequent slowdown of trade, massive drop in foreign investment and need for emergency government spending all worked against the very strategy Brazil had employed. Now, the government has limited means to address the crisis. It will focus on fighting inflation, reducing import vulnerabilities and enacting social welfare programs. The last measure could endanger the country's fiscal stability and discourage investors, but it will be done because it's one of the few tools available to the government. The country has relied heavily on exports of agriculture and raw materials over the past 18 months. These are vulnerable to current supply-chain complications and facing difficulties: namely, the cost of input materials (such as fertilizer), container shortages for export and volatility in trade with China. The price of energy, shortage of key inputs and potential electricity shortages have also created operational headaches for Brazil's industry."

**"Unfortunately for Brazil, there's little reason to believe 2022 will be much better than 2021."**
**— Allison Fedirka**

**A** **Gary Clyde Hufbauer, senior fellow at the Peterson Institute for International Economics:** "Something unusual happened last week. The Brazilian central bank sharply raised its policy interest rate by 150 basis points—a jolt not seen in a quarter-century—and the Brazilian stock market continued to sell off, not because the rate increase

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was too much, but because it was too little. The stock market dreads a return to the inflationary spirals of yesteryear, once common in Brazil, and it clamors for the central bank to decisively arrest the current 10 percent inflation rate. The central bank will likely heed this call from an unusual quarter and soon lift the policy rate from 7.75 percent to above 10 percent. The price of correct but aggressive monetary policy will be no growth, or even negative growth, in 2022—shades of Paul Volcker's Fed in the 1970s. If central bankers elsewhere are paying attention, they too will raise policy rates before their own inflationary spurts get entrenched. Meanwhile, the best Brazil can hope for in 2022 is a strong global economy (growth of more than 3 percent) that lifts demand and prices for primary commodities—such as iron ore, coffee, soybeans and petroleum. Brazil's huge service economy and manufacturing sectors face a difficult year. Ultimately, these misfortunes can be attributed to irresponsible fiscal initiatives and a poor response to Covid-19, putting the entire burden on the central bank to arrest inflation."

A **Welber Barral, senior consultant at BMJ Consultores Associados and former Brazilian foreign trade secretary:** "Brazil's economic prospects for 2022 are not very promising. GDP growth will not reach 1.5 percent, after a recovery of 5 percent in 2021. If the central bank's tightening hand is apt to curb inflation, it should reach less than 5.5 percent. Higher interest rates are the central bank's main measure to reduce inflation by cooling domestic demand. This is not a good prospect for the Bolsonaro administration, which expected the economic recovery to increase its popularity in 2022. Traditionally, election years induce more spending in Brazil at the federal and state levels. Due to compliance with laws determining a ceiling for annual expenditures, the administration is attempting to approve a constitutional amendment to postpone the payment of judicial decisions (precatórios) against the Treasury. If this amendment is approved, the administration would have financial space to increase its social program of minimum income. However, the obvious consequence is a growing federal public debt for the next administrations. This fiscal uncertainty is directly affecting market expectations in Brazil, provoking an exceptional volatility in the exchange rate and contributing to higher inflation. The current level of devaluation of the real is attracting investment for long-term projects in Brazil. Renewable energy and infrastructure are benefiting from these investments. Exporting industries (mostly in the agricultural and mineral sectors) are doing very well with the high international demand. On the other side, retail and services are still struggling to return to 2019 levels, while inflation and unemployment work against their immediate expectations."

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— Welber Barral

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