LATIN AMERICA ADVISOR

A DAILY PUBLICATION OF THE DIALOGUE

www.thedialogue.org

Wednesday, January 10, 2024

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THEDIALOGUE

FEATURED Q&A

How Much Will Brazil's Tax Reform Spur the Economy?

Brazil's Congress last month approved a landmark reform of the country's consumption taxes. // File Photo: rawpixel.com.

Q Brazil's Congress approved a landmark overhaul of the country's byzantine tax system in December, marking a major victory for President Luiz Inácio Lula da Silva, who said the reform will "facilitate investment." The overhaul includes a merging of five consumption taxes into two value-added taxes. What are the most important parts of the reform? What are the main benefits and drawbacks of the reform? How will it affect investment in Brazil, and what industries will be most affected?

A Manuel Orozco, director for sovereign and international public finance ratings at S&P Global: "Following the approval of Brazil's revenue-neutral tax reform, we upgraded our long-term sovereign ratings on the country to 'BB' from 'BB-'. In our opinion, the tax reform extends Brazil's track record over the last seven years of pragmatic policy implementation that will continue to anchor its macro stability. Among the reform's key merits are a substantial reduction of consumption tax codes and their consolidation into a dual-VAT system. These changes will help tax governance for all levels of government in Brazil, as well as substantially simplify tax compliance and the noncumulative features in the Brazilian tax system. That said, the implementation will be very gradual, and most of the structural benefits will only be felt over the long term. The full implementation of the dual-VAT will be in 2033, and the transition period to tax from origin to destiny will last 50 years. As a result, to unlock stronger levels of investment in the short-term, the Brazilian government will need to continue to address its very weak fiscal situation. Consolidating Brazil's fiscal deficits will translate

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TODAY'S NEWS

POLITICAL

At Least 10 Killed in Series of Gang Attacks in Ecuador

At least 10 people were killed in gang attacks in and near Guayaquil, authorities said Tuesday. At the same time, several armed men burst into a live television broadcast, threatening staff members.

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BUSINESS

PDVSA's Board Open for Talks with Citgo

The opposition-headed board of Venezuela state oil company PDVSA said it would participate in talks with Citgo's creditors ahead of an auction to settle claims.

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ECONOMIC

Monthly Inflation in Argentina Likely Jumped 28% in December

Argentina's monthly rate of inflation likely rose 28 percent last month, according to a Reuters poll of analysts. The jump came amid new President Javier Milei's devaluation of the peso.

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Milei // File Photo: Argentine Government.

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POLITICAL NEWS

At Least 10 Killed in Series of Gang Attacks in Ecuador

At least 10 people were killed in a series of attacks by gangs in Ecuador, authorities said Tuesday, the same day that armed men burst into a live television broadcast in Guayaquil, temporarily taking several journalists and other staff members hostage, Agence France-Presse reported. Amid the surge in violence, President Daniel Noboa said the country had erupted into an "internal armed conflict" and issued orders for authorities to "neutralize" gangs, the wire service reported. Of the 10 people killed, eight were slain in Guayaquil, and two were "viciously murdered by armed criminals" nearby in the town of Nobol, according to police. In the incident at the television station, several men masked with balaclavas and brandishing weapons and explosives broke into a live broadcast of the TC Television network during a news program, the Associated Press reported. Some staff members were taken hostage, and the live broadcast showed them being forced at gunpoint to lie on the floor. No one was killed in the attack at the station, and authorities said later that all 13 of the intruders had been arrested and would be charged with terrorism, the AP reported. On Monday, Noboa declared a national state of emergency, allowing authorities to suspend some rights, amid a rise in violence fueled by drug trafficking as gangs fight for control.

ECONOMIC NEWS

Argentina's Monthly Inflation Rate Likely Jumped 28 Percent

Argentina's monthly inflation rate likely skyrocketed 28 percent in December, which would be the highest monthly rise in prices since 1990, according to a median forecast of 20 analysts from Argentina and abroad, the wire service reported Tuesday. The rise in prices last month was driven by new President Javier Milei's so-called "shock therapy," which included a 50 percent devaluation of the country's currency. Argentina has long struggled with a high rate of inflation, which may have topped 200 percent on an annual basis, among the world's highest rates, Reuters reported. The devaluation, which was designed to narrow a large gap between the official exchange rate and the widely used parallel rate, led to sharp increases in the prices for food, transportation and goods including apparel, the wire service reported. "The policy package will lead to a big jump in inflation in December and January, though if everything goes right it should recede in the second quarter to the pre-devaluation levels of around 10 percent per month," Miguel Kiguel, executive director of EconViews in Buenos Aires, told the Advisor in a **Q&A** published Dec. 21.

BUSINESS NEWS

PDVSA's Board Willing to Enter Talks With Creditors

The opposition-led board of Venezuelan state-owned oil firm PDVSA said Tuesday in a statement that it was open to talks with the creditors of U.S.-based refiner Citgo ahead of an upcoming auction of shares to settle claims, Bloomberg News reported. "The board remains open to constructive conversations and dialogue with creditors to reach negotiated agreements," the statement read. Citgo, which is Venezuela's most valuable overseas asset, had been protected by U.S. sanctions, which previously prevented creditors from seizing it. However, a first round of bids in the auction is slated to take place on Jan. 22, and a final hearing over approval of the sale is scheduled for July 15. The total claims against Venezuela amount to approximately $20 billion, and more than 20 plaintiffs have demanded compensation, Bloomberg News reported.

NEWS BRIEFS

Mexico's López Obrador Unveils Pension Reform Proposal

Mexican President Andres Manuel López Obrador on Tuesday announced a new proposal that would ensure pensioners would continue to receive the same amount of pay in retirement that they had made while working, Reuters reported. The reform appears unlikely to succeed, as it would require a constitutional amendment, and López Obrador's Morena party currently lacks the power in Congress needed to push it through. "What I want is for whoever retires to receive a decent pension," López Obrador said, Reuters reported.

Colombia Awards Parex Resources License for Geothermal Project

Colombia has awarded Canada-based Parex Resources the country's first-ever license for development of a geothermal energy project, Reuters reported Tuesday, citing a government resolution. The project will be located in Colombia's Casanare province near a Parex oil and gas project and is expected to generate between 15 and 60 kilowatts of electricity from the earth's heat, Reuters reported.

I Squared Capital to Invest as Much as $400 Million in Brazil's Órigo Energia

Miami-based private equity firm I Squared Capital has agreed to invest as much as $400 million in Órigo Energia, a Brazilian distributed energy generation company, PV Tech reported today. The investment will be used to develop more than two gigawatts of distributed generation photovoltaic projects in 20 states in Brazil. The estimated cost of the project is $1.2 billion, PV Tech reported. The investment will give I Squared Capital a 49 percent stake in Órigo Energia.

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into higher levels of available financing for the private sector and will allow the central bank to continue to ease its monetary policy, both necessary conditions for investment."

Allison Fedirka, principal at Allonia Group and director of analysis at Geopolitical Futures: "The most important part of Lula's tax reform is that it is being done in conjunction with the government's latest fiscal reforms. These changes help create a more predictable behavior for the Brazilian government, more predictable spending patterns and decrease the possibility of extreme measures. They also work toward creating a less complex operating environment for consumers and business. A clear revenue-sharing scheme with state and local governments also helps simplify and solidify government finances and funding for public-private projects. Overall, these moves help create a sense of stability, a key characteristic for attracting investment. The major drawback facing the reforms is the uncertainty and timing regarding implementation. While both legislative chambers strongly approved the big-picture tax reform, additional legislation is needed for follow through and implementation. This will take time and additional political negotiations. Even if all stays on schedule, the changes will not start occurring until 2029 at the earliest, meaning it will be years—possibly close to a decade—before the Brazilian economy reaps the benefits of these changes. Lastly, there will be some level of opposition to the reform. On the business side, companies falling under the category of 'bad for the environment or health'—such as alcohol or tobacco—will feel the strongest impacts given that they can be subject to much higher tax rates. There's also potential for low-income families to oppose the system since it will require them to pay taxes upfront and get relief through cashback programs after the fact."

> **"It will be years—possibly close to a decade—before the Brazilian economy reaps the benefits of these changes."**
>
> **— Allison Fedirka**

Maria Paula Bertran, associate professor of economic law at the University of São Paulo: "There are potential risks for the implementation of the new tax reform. Brazil's complex and onerous tax system has been associated with a high risk of corruption and bribery in tax administration. The implementation of the new tax laws may lead to challenges in navigating bureaucracy, as well as understanding and complying with the revised regulations, and also adapting to changes in tax administration. The slow responsiveness of Brazilian courts and tax authorities to taxpayer inquiries will probably pose challenges during the implementation phase, which can take several years to be solid in terms of understanding. These risks are intertwined with Brazil's complex legal and bureaucratic framework, and they have the potential to affect investment, economic productivity and the overall business environment in the country. In the short run, the tax reform may represent higher risks for investors instead of creating a better environment. And the 'short run' may mean quite a few years."

The Advisor welcomes comments on its Q&A section. Readers can write editor Gene Kuleta.

LATIN AMERICA ADVISOR
is published every business day by the Inter-American Dialogue ISSN 2163-7962

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Latin America Advisor is published every business day, except for major U.S. holidays, by the Inter-American Dialogue at
1155 15th Street NW, Suite 800
Washington, DC 20005
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