Brazil Focus –
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Weekly Report
Nov. 5-11 2016

Looking Ahead ➔ What to watch for?

- **14th Nov.** -- IBGE to post full PNAD report for 2015
- **15th Nov.** -- National Holiday [Republic Day]
- **15th Nov.** -- APEC summit meeting in Arequipa, Peru
- **16th Nov.** – “Conversation with Pedro Parente”, W. Wilson Center, 10:00. a.m.
- **18th Nov.** -- Central Bank to post IBC-Br for 3rd Q/2016, % QoQ
- **18th Nov.** -- SRF to announce October federal revenues
- **20th Nov.** -- Zumbi Day – Afro-Brazilian Consciousness Day [holiday in some cities]
- **21st Nov.** -- Labor Ministry – Caged data, new jobs created in October
- **21st Nov.** -- IBGE to post IPCA-15
- **21st Nov.** -- IBGE to post PME unemployment data for October,
- **22-23 Nov.** -- 195th Meeting (last in 2016) of Copom ➔ Selic rate
- **23rd Nov.** -- OECD Education Ratings, Brazil ranked ___
- **28th Nov.** -- FGV to post November IGP-M ➔
- **29th Nov.** -- Public Account data for October
• **30th Nov.** -- IBGE to release GDP data for 3rd Q /2016
• **1st Dec.** -- World Anti-AIDS day
• **1st Dec.** -- Trade Balance data for November
• **2nd Dec.** -- Fenabrave ➔ November auto sales

**Sorry this issue is a bit late, but we were traveling on 11-12 Nov.**

1 - POLITICS

1.1 - Student “occupy” movement

In mid-October students in Paraná began “occupying” secondary schools protesting PEC 241 that would put a “cap” on federal expenditures (allegedly this would have a very negative impact on the education and health sectors) and also against the MP that would reorganize secondary education in Brazil. These student leaders claimed that this movement had no party “tutelage” – but the press quickly discovered that this movement had been organized by leaders of the PT, PCdoB and PSoL.

This “occupy” movement was expanded to 139 cities in 19 states. On 5-6 November, INEP administered the ENEM-National High School Evaluation Exam (similar to the SAT in the US). Because this exam was to be administered in “occupied” public schools in many of these 139 cities, these exams were “postponed” until an alternate date (3-4 December) – involving some 240,000 students who had signed up to take the ENEM.

1.2 - Federal government “froze” RJ accounts

On Monday, 7th November, the federal government froze all bank accounts of the state of Rio de Janeiro in lieu of its default (outstanding debt) to the federal government of R$ 170 million.

On 1st November, Governor Luiz Fernando Pezão (PMDB) reassumed his post after many months leave battling cancer. He immediately imposed severe austerity on the state – cancelling many programs, reducing the size of the state cabinet, increasing the state pension fund payments by state workers, reducing the pension benefits of retired state workers, etc.

1.3 - Succession – The next Chamber President

The next President of the Chamber of Deputies will be elected on 1st February 2017, after Congress reconvenes after the holiday recess period. In principle, the current Chamber President Dep. Rodrigo Maia (DEM-RJ) can not be reelected. He was elected in September to replace Dep. Eduardo Cunha (PMDB-RJ) who was suspended by the STF in May and later cassado [expelled]. Because he
was elected to complete the remaining five months of Cunha’s mandate, Maia is seeking a procedural ruling allowing him to be elected to a “full” mandate.

The so-called Centrão or Centro Democrático is articulating to elect Maia’s replacement and held a preliminary meeting at the home of Dep. Jovair Arantes (PTB-GO) on 8th November and will meet again on 22nd November. Maia mobilized enough votes to defeat the Centro Democrático back in December. Apparently, again the PMDB will be the “swing party” for this election and its current floor leader Dep. Baleia Rossi (PMDB-SP) commented that any such discussions are “premature”. ⇒ Stay tuned!!

1.4 - Repatriation – A second round?

The window of opportunity to “repatriate” legitimate funds held by Brazilians overseas closed on 31st October and produced R$ 46.8 billion in taxes (15%) and fines (15%). It is possible that this window might be opened again in 2017 with higher levels of taxes and fines. The main “promoters” of this initiative are Senate President Renan Calheiros (PMDB-AL) and Sen. Romero Jucá (PMDB-RR). Jucá had mentioned the possibility of allowing relatives of politicians (especially federal deputies) to participate in a second phase, but Calheiros later affirmed that that would not be necessary. It is estimated that if a “window” is again opened in 2017, some R$ 20 billion might be “collected”.

1.5 - Bolsa Família

In an attempt to reduce expenditures, the federal government is using a “fine-toothed comb” to weed out persons who receive social assistance program benefits when they are not eligible (don’t meet the criteria to be included) – mostly incomes larger that the stated maximum and receiving more than one benefit.

Brazil’s largest social assistance program – Bolsa Família is a case in point. This review found that 1.1 million (8%) of the 13.9 million families presented “irregularities” and were either suspended or eliminated from this program. Of the latter, 469,000 benefits were cancelled and 654,000 were suspended (blocked) in lieu of verification of documents. During this three-month period, the families suspended must present documentation to prove their continued eligibility.

According to the Ministry of Social and Agrarian Development, as of 7th November, some R$ 2.4 billion in benefits had been either cancelled or blocked.

1.6 - Lava Jato

1.6.1 - Lula as Witness

On 8th November, Lava Jato Judge Sérgio Moro set the date for former President Lula to be heard as a witness requested by the defense lawyers for former deputy Eduardo Cunha. Lula will be able to give his testimony via video conference from the offices of the federal judge in his home town, São Bernardo do Campo, SP. The other witness requested by Cunha – President Michel Temer – is free to decide the date to give his testimony.
1.6.2 - Operation Dragão

On 10th November, the Federal Police carried out the 36th Phase of the Lava Jato investigation with 18 warrants – two arrests of operators/money changers, Adir Assad and Rodrigo Tacla Duran and 16 “search-and-seize” warrants in Paraná, São Paulo and Ceará. Assad is already under arrest in Curitiba and Duran is overseas. According to federal prosecutors, two of the Petrobras construction firms – UTC and Mendes Junior passed on/through Duran R$ 34 million between 2011 and 2013. Duran is accused of operating 12 secret off-shore bank accounts for Odebrecht.

1.6.3 - Judge Moro accepts accusation against Sílvio Pereira

On 11th November, Judge Sérgio Moro accepted accusations against former PT Secretary-General, Silvio Pereira, former CEO of OAS Léo Pinheiro, former Petrobras Director Renato Duque and two employees of GDK Engenharia (César Roberto Santos Oliveira and José Paulo Santos Reis). According to plea bargaining testimony affirmed that Silvio Pereira received R$ 486.160,00 from OAS between 2009 and 2011.

1.6.4 - Judge Moro decided to try Claudia Cruz

On 9th November, Judge Sérgio Moro decided to begin the trial of the wife of former Deputy Eduardo Cunha – Claudia Cordeiro Cruz – on 14th November when her interrogation will begin. Cruz is accused of laundering at least US$ 1 million via Swiss bank accounts of illicit bribe funds from Petrobras received by her husband.

1.6.5 – Judge Zavascki authorized 2nd inquest Sen. G. Hoffmann

On 10th November, STF Judge Teori Zavascki authorized the installation of a second inquest against Sen. Gleisi Hoffmann (PT-PR) regarding “passive corruption”. Back in September, she and her husband Paulo Bernardo were investigated by the STF of receiving R$ 1 million in illicit funds from the Petrobras corruption/bribery scheme to finance her election in 2010.

1.6.6 – Lula got very “nervous”

Facing the eminent publication of a story in the weekly news magazine IstoÉ highlighting part of the plea bargaining testimony by former Odebrecht President, Marcelo Odebrecht, that his firm had transferred up to R$ 8 million in “cash” to former President Lula, on Friday, 11th November (one day before the weekend edition of IstoÉ hit the streets (on 12th November), Lula lashed out in a public statement against the Federal Police, Federal Prosecutors, the press and Judge Sérgio Moro as part of a “diabolical conspiracy” against him, saying he did not have to prove his innocence, but that the conspirators must prove “their innocence”.

1.6.7 – Odebrecht ➔ Dilma

According to “informed sources”, the plea bargaining testimony by Marcelo Odebrecht and other directors of Brazil’s largest construction firm, cited impeached president Dilma Roussef.
times – including her role in intermediation of illicit Petrobras funds transferred to the PT as “Caixa Dois” campaign finance (off the books campaign contributions) for her reelection in 2014. This story can also be found in the recent edition of IstoÉ.

1.7 - Chamber finalized Pre-Salt vote

On 9th November, the Chamber approved the presented by then Senator José Serra (PSDB-SP) that removed the obligation that Petrobras to invest at least 30% in ALL pre-salt petroleum exploration projects – thus alleviating excess spending by a cash-strapped Petrobras in this area and increasing by private sector investments, perhaps from US$ 20 billion to US$ 50 billion. This had been one of priorities of Pres. Temer’s legislative agenda.

1.8 - Senate CCJ approved PEC 241

The constitutional amendment that would place a “cap” on all federal expenditures (now called PEC 55) was approved by the Senate CCJ on 9th November after defeating amendments attempts by Senators Randolfe Rodrigues (Rede-AP), Roberto Requião (PMDB-PR) and Vanessa Grazziotin (PCdoB-AM).

Now, this PEC goes to the full Senate for discussion and two rounds of voting – perhaps approved by the end of November.

1.9 - Political reform

On 9th November, the Senate approved (on a first round vote) a PEC presented by PSDB Senators Aécio Neves (MG) and Ricardo Ferraço (ES) that would impose a threshold of 2% of the valid vote in proportional elections and 2% in at least 14 states. Parties that don’t achieve this “threshold” (barrier) would not receive any allotment from the national party fund and not have access to “free” radio/TV propaganda time. Also, this PEC also will prohibit election coalitions in all proportional elections (state & federal deputies and city council). Apparently, small and mini-parties would be able join forces in “party federations” to achieve the threshold barrier – but would have to band together for the four-year legislative period. The first round vote was 58-to-13. The second round of voting is scheduled for 23rd November. If approved by the Chamber, this reform could reduce the number of parties to 10 or 11 in the Chamber.

1.10 - PT “re-organization”, re-foundation??

A great and “grand” discussion is on-going in the PT regarding its re-organization (or re-foundation) after its large defeat in the October municipal elections. Two alternatives are on the table 1) a direct election (PED) of the new party directors involving all formal members of the party nationwide; and 2) the election of the new party directorate would occur at a national party congress (an indirect election) that would be easier to “control”. Lula supports the second alternative that would involve a “concertación” – an “agreement” among the several factions of the party. Lula hopes that this will avoid the exit of many dissatisfied of PT deputies.
2 – FOREIGN RELATIONS & TRADE

2.1 – Two STF judges in Washington

Two Brazilian Supreme Court Judges – Teori Zavascki and Gilmar Mendes -- were in Washington on Monday, 7th November, to participate in an event promoted by the Brazil Institute at the Woodrow Wilson Center ➔ “The Challenges of Brazil's Election System”.

The discussion evolved into other areas ➔ foro previlegiado and whether a deputy or senator should be allowed to become president of his/her respective Chamber if they are being tried at the STF.

Judge Zavascki affirmed that he is in favor of reducing the number of politicians “covered” (protected) by the foro previlegiado – whereby deputies, senators and cabinet ministers can only be judged by the Supreme Court. He said that they should be tried by a first level federal court, like any other Brazilian citizen. Some of these cases have been at the STF for up to 18 years.

Judge Mendes in turn discussed the case of prohibiting a deputy of senator from becoming the President of his/her respective chamber (in the lice of succession to occupy the Presidency of the Republic if they were being judged by the STF. Last week, after a majority of six STF judges had voted in favor of this prohibition, Judge Dias Toffoli interrupted the deliberation of this case by requesting more time to study the case. Mendes was not present at this session and did not mention his position. However, he said that if the President of the Senate or the Chamber had a case under deliberation at the STF, he/she should not be allowed to occupy the Presidency of the Republic in the constitutional line of succession.

The commentator – US federal District Judge Peter Messitte – compared the roles of the US and the Brazilian Supreme Courts, saying that the US Supreme Court does not judge penal cases, only constitutional questions and that any deputy of senator accused of a crime is judges by a federal district court judge (“like me”).

2.2 – WTO rules against Brazil

On 10th November, the World Trade Organization condemned Brazil’s recent “industrial policy” measures as illegal within WTO rules. The target was tax incentives, such as exemptions from the IPI (industrial products tax, for certain industrial sectors decreed by then Pres. Dilma Rousseff. Brazil will appeal – but this is one of the worst reverses Brazil has suffered at the WTO. This panel (complaint) was requested by the EU and Japan regarding these incentives for the telecommunications, auto and technology sectors. The US, Argentina, Australia, China, Indonesia, Russia and South Korea also joined this battle against Brazil. Japan and the EU claimed that these incentives were a “disguised subsidy” for these industrial sectors – that also included subsidies for exporters.

3 - REFORMS

Nothing this week.
4 – PRIVATIZATION & REGULATION

Nothing this week.

5 - ECONOMICS

5.1 - BNDES to return R$ 100 billion to government?

Between 2008 and 2014, the federal government “loaned” R$ 450 billion to the BNDES so that the development bank could inject funds into the economy in the form of “subsidized” loans at very low interest rates to selected private sector firms in an attempt to promote economic growth and economic recovery.

In February 2016, the BNDES affirmed that after repaying part of the principal and interest, it still owed the government R$ 513.6 billion including correction for inflation. Recently, the TCU ruled that the BNDES should return R$ 100 billion to the government – R$ 100 billion ➔ R$ 40 billion in 2016, and R$ 30 billion in 2017 and another R$ 30 billion in 2018.

5.2 - GM forecasts increased sales

On 8th November, GM’s CEO for Brazil, Carlos Zalenga, predicted that sales of autos and light trucks would increase from an estimated 2.1 million in 2016 to 2.4 million in 2017.

5.3 - Petrobras could receive US$ 20 billion from government

It is possible that Petrobras might receive US$ 20 billion from the federal government in lieu of declining oil prices (from US$ 100 to US$ 57 per barrel since an oil-for-stock swap in 2010. This question will be decided by an independent panel of experts hired by Petrobras and ANP.

5.4 - October inflation

On 9th November, IBGE announced the IPCA for October ➔ +0.26% (up from +0.08% in September) based on increased fuel and transportation prices. The IPCA posted +0.82% in October 2015. In spite of October increase, the 12-month accumulation was down +8.48% ➔ +7.87%.

5.5 - September retail sales

On 10th November, IBGE released data for September retail sales ➔ down by -1.0% MoM and -5.9% YoY – after declines in July and August.

5.6 – Petrobras posted R$ 16.5 billion deficit in 3rd Q/2016
On 10th November, Petrobras posted its accounting for 3rd Q/2016 – with a R$ 16.458 billion deficit. In 3rd Q/2015, Petrobras had posted a deficit of R$ 3.8 billion. In 2nd Q/2016, Petrobras posted profits of R$ 270 million. So far in 2016, the accumulated deficit is R$ 17.3 billion. The main sources of this third quarter deficit were the declining US$, a revision of premises, the recent PDV (Voluntary resignation program), and the provision funds regarding US court agreements in New York. Also, earnings were down by -14% vs. 3rd Q/2015. In this period, Petrobras received R$ 2.388 billion from disinvestments and R$ 2.4 billion from asset sales.