Weekly Report

May 20-26

Looking Ahead ➔ What to watch for?

- **29\(^{th}\) May** -- Memorial Day observed [holiday in the US]
- **29\(^{th}\) May** -- STN, federal debt R$ trillion
- **30\(^{th}\) May** -- IGP-M for May ➔ +0.\%, versus +0.\% in April
- **30-31 May** -- Copom Meeting
- **31\(^{st}\) May** -- IBGE-PNAD Feb-March-April unemployment ➔ %
- **31\(^{st}\) May** -- Central Bank to announce public account data for April
- **31\(^{st}\) May** -- STF to deliberate the end of the *Foro Previlegiado*
- **1\(^{st}\) June** -- MDIC to announce Trade Surplus for May ➔ US$ billion
- **1\(^{st}\) June** -- Fenabrave – auto sales were units in May, - % YoY
- **1\(^{st}\) June** -- IBGE to announce GDP data for 1\(^{st}\) Q/2017 ➔
- **2\(^{nd}\) June** -- IBGE – Industrial Production
- **5\(^{th}\) June** -- Central Bank ➔ FX flow in May
- **6\(^{th}\) June** -- Anfavea vehicles produced in May, - % MoM & - % YoY
- **6\(^{th}\) June** – TSE to begin deliberating case against Dilma-Temer 2014 slate
- 7th June -- FGV to announce IGP-DI for May, + %, versus +0.% in April
- 7th June -- IBGE to announce May IPCA ➔ +0.% versus +0.% in April
- 12th June -- St. Anthony’s Day – St. Valentine’s Day in Brazil
- 14th June -- IBGE, April retail sales data +0.0 MoM but - % YoY
- 15th June -- Corpus Christie – national religious holiday
- 16th June -- Friday “feriado enforcado” – informal holiday
- 18th June -- IBGE, April retail sales data +0.0 MoM but - % YoY

1 - POLITICS

1.1 – Pres. Temer reacts

On Thursday evening, 18th Map, Pres. Temer made what was called a “blind” response on a nationwide TV hookup – before he was able had access to the audio and transcript of the clandestine recording made by Joesley Batista at the Jaburú Palace on 7th March. The next day, the O Globo newspaper ran an editorial on Friday, 19th May calling on Temer to resign. For some reason, Globo decided to call for his resignation while the other newspapers were more “cautious”. Remember: It was the Globo journalist Lauro Jardim that “broke” this story late Wednesday afternoon, via Globo’s website.

See ➔ https://oglobo.globo.com/opiniao/editorial-renuncia-do-presidente-21365443

After the transcript became available, Temer made another TV address at 3:00 p.m. and claimed that the audio recording had been edited/modified and cited the technician used by the Folha de São Paulo that “50 modifications” had been detected. Other press units cited technicians who countered this version that the recording had not been tampered. However, on 21st May, O Globo counter attacked by showing that the “specialist” used by the FSP was an amateur lawyer who was really a real estate broker. The Federal Police will make a complete audit on this tape and have asked the Batista family to supply the recording device used by Joesley Batista to make these recordings. Apparently, two recording devices were used (disguised as “pen drives”). One device was delivered to the Federal Police, and the other was sent from NYC and arrived on 23rd May.

https://www.youtube.com/watch?v=b73znVDDVYw


Temer complained that the recording had been altered and that he never agreed that Joesley should continue to “buy the silence” of Eduardo Cunha and Lúcio Funaro. He also affirmed that his lawyers were preparing a petition to the STF asking that the Federal Police technicians do a “verification” of this audio tape and that the STF suspend the investigation against him. However, on 22nd May, Temer’s lawyers requested that this petition be disregarded by the STF – because of fear of
defeat. Later on Saturday afternoon, STF Judge Edson Fachin announced that he had requested the Federal Police audit of the tape but that he would not suspend the investigation. Rather, he would ask the full STF to make this decision set for 30th May.

On 20th May, the FSP reported that 15 days before Joesley Batista did his recording of conversations with Pres. Temer, on 19th February, Federal Prosecutor Anselmo Lopes took a call from a JBS lawyer who said that the Batista brothers wanted to do plea bargaining. The next day Lopes and Federal Police officer Rúbia Pinheiro gave them some “lessons” as to how the plea bargaining mechanism operates.

Over the weekend, the major parties decided whether or not to abandon the Temer support coalition in Congress. On Sunday, the PSDB decided to “wait and see” regarding the evolution of this episode. This “wait and see” is conditioned on the STF decision on 24th May – whether to cancel the inquest against Michel Temer. Also on Sunday, the OAB called on Temer to resign and prepared an impeachment request that was filed at the Chamber on 25th May. Remember: The OAB also filed impeachment requests against Pres. Fernando Collor in 1992 and Pres. Dilma Rousseff in 2016.

**Detail:** During Brazil’s “Republican Period” (since 1889), only one other President was investigated while in office Getúlio Vargas in August 1954. This involved two gunmen “hired” to murder then ardent opposition deputy against Vargas, Carlos Lacerda. The gunmen’s aim was “faulty” and Lacerda was shot in the foot but his body guard, Air Force Major Vaz was killed.

In the US, the risk analysis agency – Eurasia – gave Pres. Michel Temer 30% chance of “survival”.

When the JBS case broke open last week, everyone got to know Dep. Rodrigo Santos Rocha Loures (PMDB-PR) plus the TV coverage of his arrival at the Guarulhos (SP international airport).
Now we know that he was VERY well connected with Michel Temer (as Vice-President) and then became an important staffer to Pres. Temer after Dilma was impeached.

When Temer named his Justice Minister Alexandre de Moraes to the Supreme Court, everyone wondered why he then appointed Federal Deputy Osmar Serraglio (PMDB-PR) to replace Moraes. Now we know the answer to this question – Rocha Loures was the first suplente [alternate] on the PMDB list for deputy after the 2014 elections in Paraná, and replaced Serraglio as deputy, only to have the STF suspend him from his mandate.

Senator Aécio Neves (PSDB-MG) – On 22nd May, Sen. Neves’ lawyers petitioned the STF to remove the suspension of his mandate dictated by Judge Esdon Fachin. At the same time, PGR Rodrigo Janot renewed his request that the STF issue an arrest warrant for Sen. Neves and Dep. Rocha Loures. Janot affirmed that if Judge Fachin decided not to issue this warrant, that he take this case immediately to the full STF.

Positive Agenda – On Tuesday, 23rd May, Temer’s allies in Congress tried to present the appearance of a “positive agenda”. The Senate CCJ tried to approve the report by Sen. Ricardo Ferraço (PSDB-ES) on the Labor Legislation but was shouted down by the Opposition. The Chamber tried to move toward a vote on the Social Security Reform, but was able to approve only 3 MPs.

CVM – On 22nd May, the CVM-Bovespa stock market “watchdog” began an investigation into whether the Batista brothers had used their own “insider information” to reap illicit profits (of some R$ 500 million) on the FX market and the stock market last week. On Monday-Tuesday, 22-23 May, JBS stocks lost 31.3% of their value. This affected the BNDES and CEF that hold a large number of these shares. One gain compensated the later loss.

Moody’s & Fitch – Both risk analysis agencies in NY downgraded JBS from Ba2 to Ba3 and from BB+ to BB, respectively. S&P is considering downgrading Brazil “soon”.

“Score Card” for indirect election – Both Government and Opposition deputies and senators are discretely articulating/discussing possible candidates for an eventual indirect election for the successor of Michel Temer – if and when he leaves office. The press has developed a “score card” listing these “pre-candidates” in three categories:

The Political Nucleus:

Finance Minister Henrique Meirelles (PSD) ➔

Former Presidnet Fernando H. Cardoso (PSDB) ➔

Senator Tasso Jereissatí (PSDB) ➔

Deputy Rodrigo Maia (DEM) ➔

The Judicial Nucleus:

STF President Cármen Lúcia ➔
STF Judge Gilmar Mendes ➔
Former STF President Nelson Jobim ➔
Former STF Judge Joaquim Barbosa ➔
Former STF Judge Ayres Britto ➔

Other Possible Candidates:
Lula (PT) ➔
Ciro Gomes (PDT) ➔
Marina Silva (Rede) ➔
Dep. Jair Bolsonaro (PSC) ➔
Sen. Ronaldo Caiado (DEM)

The parties that compose the government coalition in Congress are discussing/articulating the successor for Michel Temer in an indirect election by a joint session Congress. Reportedly, these politicians want a current member of Congress and because the Chamber has 513 votes in this joint session (vs. 81 Senators), they would prefer “a deputy”. This week, two names are the most frequently mentioned ➔ Senator Tasso Jereissati (PSDB-CE) and former STF President, ex-Minister of Justice and Defense, and former federal deputy (constituent assembly). Finance Minister Henrique Meirelles is frequently mentioned, but the government bloc would rather maintain him at Finance to help push the reforms through Congress – and maybe become a candidate in 2018 (if the economy improves considerably).

Reportedly, Pres. Temer is convinced that he has no “way out” and might be induced to resign in exchange for a pardon [indulto] signed by his successor – like Nixon negotiated with his Vice-President Gerald Ford before he resigned in August 1974.


One newspaper headline read “The King is dead, but not yet buried” – but with his presidential pen still at hand.


Columnist Elio Gaspari called Temer a “Discardable President”.

See ➔ https://oglobo.globo.com/opiniao/o-presidente-descartavel-21383479

1.1.1 – JBS under fire in the US
The Batista brothers (JBS & J&F) may have temporarily avoided prosecution in Brazil via their plea bargaining testimony (the CVM and TCU are investigating) but they are under fire in the US under the FCPA-Foreign Corrupt Practices Act their firms in the US may be prosecuted because of the corruption practiced in Brazil and several investors in the US are suing for losses incurred because of the devaluation of JBS shares. In Brazil, the Banco do Brasil, CEF and BNDES also suffered losses. CEF and BNDESPar lost R$ 3.4 billion.

Remember: 92.6% of JBS gross income (US$ 42 billion) in 2016 was in the US. J&F has hired the US law firm Baker McKenzie in Washington to for its defense against legal actions against this Brazilian firm in the US.

Reportedly, J&F will sell off several firms in Brazil → Alpargatas, Vigor, Eldorado, Flora and Banco Original.

1.1.2 – JBS used Ibope to “launder” contributions

On 25th May, it was revealed that in his plea bargaining testimony, Ricardo Saud revealed that JBS had used “disguised” contracts with one of Brazil’s important public opinion organizations – Ibope → to “launder” political campaign contributions to the current PMDB floor leader in the Senate, Renan Calheiros (Alagoas) and for then Deputy Henrique Alves (PMDB-RN) for the 2014 elections. Alves was defeated in his bid for Governor, and Renan was able to elect his son as governor of Alagoas. Part of these “laundered” funds was directed to the PMDB in other states by Renan.

1.2 – Lava Jato

Many people are using the phrase “Bye-Bye Lava Jato” because the Federal Police were included in the 44% across the board contingency budget cuts applied to the 2017 budget as part of the austerity measures to try to reduce the BIG deficit in public accounts. This provoked a reduction in the number of Federal Police delegados in Curitiba (from 9 to 4) assigned to the Lava Jato task force as well as a reduction of Federal Police officers and funds to sustain the many police Operations. Many see this as an indirect strategy to end or at least reduce the impact of these investigations.


The most notable federal prosecutor on the Lava Jato task force, Deltran Dallagnol, has just published a new book in support of these investigations.


Moro & Dallagnol on CBS “60 Minutes” → The main figures in the Lava Jato investigation – Judge Sérgio Moro and Prosecutor Deltran Dallagnol were interviewed on the CBS Sunday news magazine program 60 Minutes on 21st May. Moro was compared to the FBI agent who “busted” Al Capone – Elliott Ness.

Lula indicted again – On Monday, 22nd May, federal prosecutors accused Lula of corruption and money laundering regarding a R$ 1.02 million “investments” by Odebrecht and OAS in renovation and “improvements” at the Santa Barbara dacha (sitio) allegedly owned by Lula in Atibaia, SP. This is the sixth accusation Lula faces in federal courts.

1.3 – Operation Panatenaico

In the wee hours of Tuesday, 23rd May, the Federal Police carried out Operation Panatenaico in Brasília. This operation refers to the stadium used in the first Olympic games in Greece in 329 a.c. This same stadium was remodeled in 1895 to receive the first modern Olympic games in 1896.

This case involved the over-invoicing of the renovation and construction of the National Soccer Stadium Mané Garrincha for the 2014 World Cup playoffs in Brazil. This project was originally budgeted at R$ 600 million but in the end cost R$ 1.575 billion (an “extra” R$ 900 million). Allegedly, these bribe payments were made via Terracap (51% GDF & 49% federal government).

In all, 28 warrants were issued by Federal Judge Vallisney Souza de Oliveira of the 10th Criminal Circuit in Brasília – 10 for temporary arrest, three for coercive testimony and 15 for search-and-seize. Two former governors were arrested – José Roberto Arruda (DEM) and Agnelo Queiroz (PT), as well as former Vice-Governor Nelson Tadeu Filippelli (PMDB) who also served as PMDB federal deputy (2003-2007). Filippelli had been appointed as a “special advisor” (staffer) to Pres. Michel Temer (PMDB), in September 2016, who sacked him immediately. The court ordered the embargo of the accounts of these three accused but “only” captured R$ 26 million. Also, former temporary governor (who replaced Arruda), now federal deputy Rogério Rosso (PSD) was accused of receiving bribes. Rosso was the President of the Chamber special committee to decide the viability of Pres. Dilma’s impeachment in 2016 and is the floor leader of the PSD.

When the construction contract was awarded to Andrade Gutierrez (and Via Engenharia) in 2009, Arruda demanded 1% in bribes. Arruda was removed and Rosso was chosen to serve the remainder of Arruda’s term (he also demanded bribes). After Agnelo was elected in 2010, he also participated in the bribe scheme. Filippelli is accused of turning this bribe over to the PMDB presidential campaigns ➔ more “bad news” for Michel Temer regarding the TSE judgment on 6th June.
The prosecution of this case was made possible by plea bargaining testimony in the *Lava Jato* investigation by Andrade Gutierrez employees Clóvis Primo and Rogério Sá.

Most observers of the construction of these soccer stadiums for the 2014 Olympic games suspected corruption (bribes, over-invoicing) in their construction. The Brasília stadium was the “worst” (largest over-invoicing) and it was considered just a matter of time until an investigation would involve this case. Now, it is possible that more plea bargaining testimony by the *Lava Jato* construction firms will produce similar investigations and federal police operations in the other 11 cities that hosted these Olympic soccer games in 2014. ➔ Stay tuned!!


1.4 – Maluf convicted [finally] by STF

After years and years of efforts to remove Paulo Maluf from Brazil’s political elite, finally, on 22nd May 2017 the first STF working group voted 4-to-1 to convict Maluf of “money laundering” and sentenced him to 7 years, 9 months and 10 days in prison. His corruption crimes have already been “erased” by time limits, but money laundering has no “time limitation”. This accusation dates to his term as Mayor of SP (1993-1997) with funds “ripped off” from construction contracts and laundered via NY, Switzerland and the Isle of Jersey.

This five-judge working group is composed by Edson Fachin, Luis Roberto Barroso, Rosa Weber, Luiz Fux and Marco Aurélio Mello. Only Mello voted in favor of Maluf. He was sentenced to seven years in prison.

This means that – convicted in the court of last resort, Maluf might be *cassado* (lose his mandate as deputy) and not be allowed to be a candidate for reelection in 2018 because of the *Ficha Limpa* law. But – his lawyers might appeal this decision to the full STF.

**Remember:** Maluf was placed on the Interpol “read list” (immediate arrest) by a prosecutor in NYC: When he and his wife tried to make a million Euro withdrawal at a Paris bank, the teller stepped on the “red button” and in minutes the financial police arrived and he was “invited” to spend several hours at the police station. The withdrawal was prohibited but Maluf said that the $$ was his wife’s inheritance from her father. ➔ Stay tuned!!

1.4.1 – Dep. Celso Jacob sentenced to 7 years

On and unanimous decision, the STF second working group sentenced Dep. Celso Jacob (PMDB-RJ) to an “open” prison term of 7 years and two months (free during the day but spend the night in prison. He was accused of administrative crimes while he was Mayor of Três Rios, RJ.

1.5 – Violence in Brasília
Wednesday, 24th May, was designated as a “March on Brasília” or “Occupy Brasilia” by the Labor Centrals (CUT, Força Sindical, etc.) and a variety of militant groups. Some 500 busses transported militants to Brasília for the demonstrations against Pres. Temer and against the Labor Legislation and Social Security Reforms.

The militants concentrated around the national soccer stadium and began marching toward the Esplanade of the Cabinet Ministries, Congress and the Three-Power Plaza in the morning. As they approached the central bus station, the local police (PM-DF) and members of the National Security Force began inspecting their backpacks, etc. carried by the militants in search of weapons, bombs, fireworks, etc. This provoked a mad “rush” against the police that was not contained in spite of the contingent of mounted police (horses) and the conflict got nasty as the militants approached Congress. They were repulsed by the police but then attacked several ministry buildings – fires, forced entry, destruction, etc. These buildings were ordered evacuated by federal employees who were very scared for their physical safety.

This was the point where “Plan B” should have been invoked with Army shock troops to contain the out of control militants (infiltrated by violent attackers – Black Blocs). However, “Plan B” had not been articulated and finally near the end of the afternoon the President of the Chamber Dep. Rodrigo Maia (DEM-RJ) made this request to the Minister of Defense, Raul Jungmann. Too late, the militants had already retreated toward the soccer stadium. This action was attacked by the Opposition as “authoritarian” but in reality Pres. Dilma convoked Army troops to quell the disturbances in 2013, and the Armed Forces were called in several time in recent months to “pacify” problems in some states.


As might be expected, tempers were enraged especially among federal deputies, with screams “Fora Temer” and “Lula na cadeia” from both sides. Later things calmed down, and the Chamber deliberated and voted on several measures. .

The “Day After”, 25th May, Pres. Temer revoked the convocation of Army troops to maintain “law and order” in Brasilia. This move came very late, after the fact convocation had produced complaints from the Opposition as well as some politicians in the government coalition that “this action smacked of the Military Regime period (1964-1985)”. In effect, this was a weak effort by Temer to try to show “Yes, I am still in command”.

Violence in Rio – More violence on Wednesday, 24th May ➔ in Rio de Janeiro, in protest against the vote by the RJ state legislature that increased the social security contribution from 11% to 14% for all state employees. These violent acts around the AL-RJ building in downtown Rio were controlled and contained by the PM-RJ with assistance from the National Security Force.
2 – FOREIGN RELATIONS & TRADE

2.1 – The Lula-Sarkozy Submarine Deal

Reportedly, French courts are investigating the accusation of bribe payments regarding the contract to sell four Scorpène attack submarines to Brazil in December 2008 for 6.7 billion Euros. The French PNF chief, Eliane Houlette visited Brazil two weeks ago together with the Ocleiff (Anti-Corruption) chief Thomas de Ricolfis.

The Scorpène is a “conventional” [diesel-electric] submarine made by the DCNS in cooperation with the Spanish Navantia. Chile and Malaysia each have two such submarines and India has acquired six. In Brazil, the DCNS has a partnership with BTP Odebrecht.

2.2 – More flights to Brazil [from Europe]

Reportedly, low cost Irish carrier RyanAir has concluded an agreement with Air Europa to begin regular flights from Spain (Madrid) to Brazil and other destinations in South America and the US. Ryanair CEO, Michael O’Leary affirmed that he wants Ryanair to become the Amazon of international air travel. Air Europe flies the Boeing 787-8 and the Airbus A330-300.

3 – REFORMS

Nothing this week.

4 – PRIVATIZATION & REGULATION

4.1 – HNA to acquire Odebrecht’s share in Galeão

It was reported on 24th May that Odebrecht Transport will sell its share in the Galeão Airport in Rio to the Chinese group HNA – subject to approval by ANAC (within 60 to 90 days). The administration of the Galeão [Tom Jobim] airport was privatized by Pres. Dilma Rousseff in 2013. Odebrecht Transport led a consortium that included the Singapore airport administrator Changi with a bid of R$ 19 billion. HNA should acquire 51% of this consortium and Changi will increase its share from 40% to 49%.

5 - ECONOMICS

5.1 – April Public Accounts

Current Account – Produced a surplus of US$ 1.153 billion, according to Central Bank data released on 23rd May. March also posted a surplus. This was the best April result since 2007. In April,
Brazil’s trade surplus was very large \( \Rightarrow +US\$ 6.742 \) billion. Remittances were \(-US\$ 3.227 \) billion and services had a deficit of \(-US\$ 2.515 \) billion.

**FDI** – In April, Foreign Direct Investment posted \(+US\$5.577 \) billion and accumulated \(+US\$29.530 \) billion.

**Foreign Investments** \( \Rightarrow \) April had a surplus of \(+US\$ 383 \) million in financial market investments and an accumulation of \(+US\$ 1.040 \) billion in 2017.

**Government Bonds** \( \Rightarrow \) In April, \(+US\$ 4.351 \) billion was posted, and accumulated \(+US\$ 3.235 \) billion in 2017.

### 5.2 – May Inflation

On 23rd May, IBGE released the data for the IPCA-15 that tracked inflation between 14th April and 15th May \( \Rightarrow +0.24\% \). The 12-month accumulation now stands at \(+3.77\% \), down from the \(+4.41\% \) posted in April. This is the lowest 12-month accumulation since \(+3.71\% \) in July 2007. This 12-month accumulation through 15th May is below the Central Bank “target” of \(+4.0\% \) and approaching the lower limit of this “target” \(+3.0\% \).

### 5.3 – Glencore to acquire Bunge?

On 24th May it was reported that the agriculture division of the Swiss Glencore is attempting to acquire the large American grain dealer – Bunge. Bunge was founded in 1818 and is one of the world’s largest grain dealers and is the “B” of the ABCD competition \( \Rightarrow \) ADM-Archer Daniels Midland, Bunge, Cargill and Louis Dreyfus. Bunge had gross earnings of US$ 42.7 billion in 2016.

### 5.4 – Petrobras to exercise option on 3 pre-salt areas

On 25th May, it was revealed that Petrobras had decided to exercise its participation option (30%) for three pre-salt exploration areas – Sapinhoá, Peroba and Alto do Cabo Frio Central – in the next round of concession auctions to be held by ANP at the end of October. As he announced this decision, Petrobras CEO, Pedro Parente, affirmed that this decision was based on technical aspects and on financial restrictions and would probably amount to some R$ 810 million. He maintained the goal of US$ 21 billion through 2018. Ticket sales began on 23rd May.