Brazil Focus –
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Weekly Report
May 27-June 2
2017

Looking Ahead ➔ What to watch for?

- 5th June -- Central Bank ➔ FX flow in May
- 6th June -- Anfavea vehicles produced in May, - % MoM & - % YoY
- 6th 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.% 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.% MoM but - % YoY
- 18th June -- Caged data ➔ jobs lost in April
- 18th June -- Central Bank to release IBC-Br for April ➔
1 - POLITICS

1.1 – Maria Silvia resigned BNDES

Late Friday afternoon, 25th May, Maria Silvia Bastos Marques delivered her resignation at President of the BNDES in person to President Michel Temer. She was at the helm of the National Development Bank for a little over one year. He tried to convince her to stay on but she was resolute in her decision. She alleged “personal reasons” for her resignation. However, the real reasons apparently were that she was discontent with the pressures from the private sector for the BNDES to “liberate” its low-interest loans more rapidly. Also, she was upset with the aggressive investigation of BNDES loans and criteria for same recently conducted by the Federal Police. Several BNDES directors were taken to the Federal Police HQ in Rio for “coercive testimony”. One of her “accomplishments” was to put an end to the ‘PT scheme” of granting low interest loans from the development bank. Immediately, she suspended the disbursement of US$ 4.7 billion to firms under investigation by Lava Jato.

Pres. Temer quickly named Paulo Rabello de Castro to replace Bastos Marques. He had been the head of IBGE. On 31st May, Roberto Olinto, the current Director for Research at IBGE was confirmed as the new President of IBGE. He began at IBGE in 2005. He was sworn in on 1st June to replace Paulo Rabello de Castro.

Quickly, Rabello de Castro affirmed that he had nothing to do with his son-in-law, Bruno Luz, who together with his father, Jorge Luz, was arrested in Operation Blackout – the 28th phase of the Lava Jato investigation.

1.2 – Temer replaced Justice Minister

On Sunday, 28th May, Pres. Temer appointed his Minister for Transparency, Fiscalization and CGU, Torquato Jardim, to replace Osmar Serraglio as Justice Minister who had he returned to his seat as federal deputy he would have dislodged Rodrigo Rocha Loures and returned him the first alternate on the PMDB-PR list. Thus, Rocha Loures would have lost his status as foro privilegiado at the Supreme Court where he would have been tried for the recent PGR accusations regarding the recent plea bargaining testimony by the Batista brothers (JBS). However, Pres. Temer saved Rocha Loures
from this fate by appointing Serraglio to replace Torquato Jardim at the Transparency post. However, Serraglio decided not to accept the Transparency/CGU post and returned to the Chamber of Deputies, thus dislodging Rocha Loures who lost his “cover” from the foro previlegiado. Torquato Jardim was sworn in as Justice Minister of 31st May.

Torquato Lorena Jardim was born in Rio de Janeiro in December 1949, and had been a professor of Constitutional Law at the University de Brasilia for 20 years. He served as Minister on the TSE between 1988 and 1996 and is considered a specialist in the area of election law. He concluded graduate studies at the University of Michigan and Georgetown University (1977), and studied at the Inst. of International Human Rights in Strasburg, France (1982). Reportedly, Torquato is against using the “closed list” in the 2018 election.

Torquato criticized the Lava Jato investigations that two OAS directors had been convicted without and adequate evidence. The President of the Assoc. of Federal Police delegados – Carlos Eduardo Santos - voiced “concern” for a loss of autonomy of the Federal Police under Torquato Jardim

1.3 – Situation of Pres. Michel Temer

So far, the Temer support coalition in Chamber has lost four parties that decided to join the Opposition ➔ PSB, PPS, Podemos (ex-PTN) and PHS, a total of 66 deputies. Thus, the government support base was reduced from 413 to 347. However, not all the deputies linked to these four parties will adopt an “opposition posture” vis-à-vis the Temer government. PPS President Roberto Freire resigned his post as Minister of Culture, but Raul Jungmann remained at his post as Minister of Defense. At least half of the PSB deputies will vote in favor of the social security reform and Mines & Energy Minister Fernando Bezerra Filho (PSB-PE) refused to step down. Some PSB deputies want to expel him from their party.

The STF (Judge Edson Fachin) determined that the Federal Police have up to ten days to conduct an “interview” (written Q&A) with Pres. Temer (take his testimony) regarding his participation on the clandestine tape recorder by Joesley Batista. Temer’s lawyer, Antonio Cláudio Mariz de Oliveira, requested that this (Q&A) be suspended until after the Federal Police technicians conclude their evaluation of the audio tape (and recorders) used by Joesley Batista to record his “conversation” with Pres. Temer. If not, Mariz requested that this Q&A not include anything extracted from this tape. Of course, any Q&A based on the videos of the plea bargaining by the Batista brothers and other JBS and J&F employees would be viable.
On 31st May, J&F concluded a leniency agreement with federal prosecutors for R$ 10.3 billion to be paid over 25 years.

1.4 – Lava Jato

1.4.1 – Operation Dry Well

On 26th May, the Federal Police carried out Operation Dry Well that investigated the acquisition of an offshore petroleum exploration field in Benin for US$ 34.5 million. Allegedly, some US$ 10 million in bribes (side payments) had been extracted. Joao Augusto Rezende Henriques had been the PMDB operator involved in this operation. He was arrested in the Lava Jato investigation in September 2015 and sentenced to 7 years in jail.

1.4.2 - Judge Moro absolved Claudia Cruz

On Friday, 26th May, Judge Sergio Moro absolved the wife of former Chamber President Eduardo Cunha, Claudia Cruz of the accusations of money laundering regarding the US$ 1 million in her Swiss bank account “Kopec”. Federal Prosecutor Carlos Fernando dos Santos Lima said that this decision by Judge Moro was “not justified” and that federal prosecutors would appeal this decision. Santos Lima added that Moro had a “generous heart”. However, Moro ordered the confiscation of the remaining funds in in Claudia Cruz’s Swiss bank account ➔ R$ 640 million.

Recently, the Federal Police Operation Dry Well concluded that Cunha had received US$ 5.5 million in bribes related to the Petrobras petroleum exploration contact with SARL-CBH in Benin.

1.4.3 – Antonio Palocci

On 31st May, STF Judge Luis Roberto Barroso denied a habeas corpus request by the lawyers for Antonio Palocci and his ex-staffer Branislav Kontic who are held prisoners in Curitiba for 8 months. Reportedly, Palocci has replaced his lawyers with ones who have experience in conducting plea bargaining negotiations.

1.4.4 – CVM opened inquest against JBS

On 30th May, the CVM (SP Stock market watchdog) opened an investigation regarding FX manipulations by JBS just before the plea bargaining by the Batista brothers became public. Reportedly, they bought some US$ 1 billion before this “insider information” became public and had a strong impact on the FX market in Brazil.

Want more? BNDES-PAR claims that it has now “recovered” R$ 5 billion of the R$ 8.1 billion that it invested in JBS.

1.4.5 – Joesley Batista – R$ 800 million blocked in SP

In response to a suit filed by lawyer Hugo Flizer Chaves Neto requesting that the federal courts block R$ 10 billion from the bank accounts of the Batista brothers and their families, on 1st June
1.4.6 – PGR renewed prison request for Rocha Loures

Soon after the release of the tape and plea bargaining by the Batista brothers that implicated then federal deputy Rocha Loures, the PGR requested that the STF issue an arrest warrant for the deputy. STF Judge Edson Fachin refused this request by suspended his mandate as federal deputy. However, when Dep. Osmar Serraglio (PMDB-PR) was replaced as Justice Minister by Pres. Temer, he returned to the Chamber of Deputies and dislodged Rocha Loures who was serving as his alternate (*suplente*). Now, Rocha Loures is no longer a deputy there is no impediment for his arrest and thus the PGR renewed this request. If Judge Edson Fachin issues this arrest warrant, the chances that Rocha Loures will attempt plea bargaining increase. His wife is pregnant and is pressuring him in this regard. However, his father is against this idea. If he does enter a plea bargain, this might be very bad news for Pres. Temer. Rocha Loures has hired the same lawyer who is negotiating the plea bargaining by Lúcio Funaro.

1.5 - Mensalão

On 31st May, STF Judge Luís Roberto Barroso authorized Henrique Pizzolato to complete the remainder of his sentence under “house arrest”. Pizzolato was convicted of corruption and receiving illicit funds he embezzled from the Banco do Brasil when he authorized the transfer of R$ 73.8 million to DNA the advertising firm of Marcos Valério in 2003 and 2004. He was convicted and sentenced to 12 years and 7 months in prison and a fine of R$1.3 million, but fled to Italy (where he holds citizenship) using a passport in his brother’s name (who had died 35 years ago). He was finally extradited back to Brazil in 2015 and has been serving his sentence in the Papuda prison in Brasilia.

1.6 – Foro Previlegiado

On 31st May, the Senate approved a PEC (Constitutional Amendment) that would “limit” the guarantees (shield) allocated to members of Congress and cabinet ministers via the *Foro Previlegiado* – that stipulates that the latter can only be prosecuted (tried and convicted) by the STF. This PEC would allow these authorities (including governors and mayors) to be prosecuted by first level federal and state courts. **BUT** – different from other Brazilian citizens (mere mortals), if a deputy or senator were convicted in a second level court, he/she would not automatically go to jail. The Supreme Court would be spared having to prosecute members of Congress, but the latter would have their **privileges** transferred to the lower courts. This PEC will now go to the Chamber for two rounds of voting.

The STF began deliberating the end of the *Foro Previlegiado* 31st May. After four votes in favor of restrictions on the *Foro Previlegiado*, the “new” STF judge Alexandre de Moraes **pediu vistas** (asked to study the case further) and this postponed this deliberation until Moraes returns the case and casts his vote – who knows when?

1.7 – Rui Falcão ➔ 2018 elections
Just prior to the opening of the National PT Congress, on 1st June, national PT president, Rui Falcão analyzed the party’s perspectives for 201.

He affirmed that the PT has suffered “reverses” and is trying to “recover” after the election and impeachment of Pres. Dilma Rousseff and the debacle suffered in the municipal elections in October 2016. Falcão denied that the proposal for direct elections for Temer’s successor id proposed as a “rapid fire” attempt to elect Lula before he is declared ineligible by the Lava Jato investigation. He even suggested that the PT might join an alliance with the PDT in support of the candidacy of Ciro Gomes in 2018.


2 – FOREIGN RELATIONS & TRADE

2.1 – Judge Sergio Moro ➝ Portugal

On 30th May, Lava Jato Judge Sergio Moro participated in a large international conference in Estoril, Portugal on “The struggle against crime in a Democracy: The role and limits of the Criminal and Justice System”. Among the participants – Antonio di Pietro (Italy), Baltazar Garzon (Spain), and Jorge Quiroga (Bolivia) plus Brazilian politicians – Chamber of Deputies President Rodrigo Maia (DEM-RJ) and former deputy and law professor (UFGo) Vilmar Rocha.

http://www.estorilconferences.com

2.2 – China - US$ 20 billion partnership with Brazil

In spite of the recent political crisis in Brazil, China decided to maintain plans to launch a US$ 20 billion partnership – US$ 15 billion in Chinese funds and US$ 5 billion from the Brazilian STN. The main areas of Chinese interests are in the agriculture and infrastructure sectors. In order to guarantee mineral and grain (soy) exports, these investments will concentrate on the port in Itaqui, MA.

This agreement was signed during the two-day event in São Paulo – Brazil Investment Forum 2017 on 30th May organized by APEX and the Inter-American Development Bank – in the presence of the Chinese Ambassador to Brazil Li Jinzhang.

See ➝ http://www.valor.com.br/brasil/4986150/bndes-sera-um-dos-operadores-de-novo-fundo-de-cooperacao-brasil-china

Pres. Michel Temer participated in the opening ceremony of this event the morning of 30th May.

See ➝ http://www.brasilinvestmentforum.com/

2.3 – May Trade Surplus ➝ US$ 7.7 billion
On 1st June, MDIC released the trade data for the month of May ➔ a trade surplus of US$ 7.661 billion, the largest surplus since this data series began in 1989. The five-month accumulation in 2017 now stands at US$ 29.032 billion. In May, exports totaled US$ 19.792 billion and imports were US$ 12.131 billion. So far in 2017, total exports were US$ 87.93 billion (+7.5% YoY) and imports were US$ 58.9 billion (+4.0% YoY). In 2016, Brazil posted a trade surplus of US$ 47.692 billion. For 2017, the analysts surveyed by the Central Bank project a surplus of US$ 56.2 billion.

2.4 – Brazil ➔ OECD

Finally, after many invitations to join the OECD were refused by Brazil, now Brazil has requested negotiations aimed at becoming a member of this important organization. However, this means that Brazil would have to accept and comply with the very stringent rules of the OECD – especially in the area of “public management”. Brazilian negotiators affirm that these negotiations might be completed so that Brazil could formally join (be accepted) the OECD in 2019.

3 – REFORMS

Nothing this week.

4 – PRIVATIZATION & REGULATION

4.1 - CEMIG

On 2nd June, the MG state-owned electric company (generation, transmission and distribution) announced that it will sell (disinvest) R$ 6.6 billion in assets in 2018 and 2019 ➔ including its shares in the Belo Monte and Santo Antonio hydro electric installations plus 19% of its 31.5% share in the Taesa transmission line, the Transmineira transmission line, its share in the generation controlled by Light, Gasmig, Cemig Telecom and find a “strategic partner” for its renewable generation Renova Energia. These funds will be used to reduce the large outstanding Cemig debt.

5 - ECONOMICS

5.1 – Positive GDP 1st Q/2017

On Thursday, 1st June, IBGE released the GDP data for 1st Q/2017 ➔ +1.0% QonQ, but -0.4% YoY (compared with 1st Q/2016). The 12-month accumulation was negative ➔ -2.3%. This was the first positive GDP in eight quarters (two years). This result was due in large part to the growth on the agriculture sector ➔ +13.4%. The industrial sector had +0.9% and services posted 0.0% growth.

Because unemployment continues high, the rate of family consuming had a slight decline (-0.1%) and government consumption was down by -0.6%. Investments declined by -1.6%.
The end of recession? The answer from the IBGE technicians and economists in general is “Not yet”. Sustained (a two-quarter) sequence of positive growth and a greater “balance” among the three sectors. It is possible that Brazil’s GDP might turn negative again in 2nd Q/2017, but the specialists believe that positive growth should again appear in 3rd and 4th Q/2017.

Fiesp reported that in April the level of industrial activity was up by +0.3%.

5.1.1 – Investments decline

Amid all the “euphoria” regarding the positive GDP in 1st Q/2017, a very negative note appeared ➔ investments declined to 15.6% of GDP – the lowest level since 2006 (-1.6% QoQ and -3.7% YoY).

See ➔ http://economia.estadao.com.br/noticias/geral,real-indicador-de-geracao-de-empregos-investimento-e-o-menor-desde-2006,70001822905

5.2 – Moody’s signaled possible down grade for Brazil

After S&P recently issued an alert that a new down grade for Brazil was being considered, on Friday, 26th May, Moody’s followed suit and also signaled a possible down grade for Brazil because of recent “negative factors” – the political crisis of the Temer government, the plea bargaining testimony by the Batista brothers (JBS) and the stalled reform process in Congress

5.3 - Copom

Copom met on 30-31 May and decided to reduce the Selic rate by one p.p. – from 11.25% to 10.25%. However, in its communiqué Copom signaled “caution” and that the next Copom meeting in June might reduce the basic Selic rate by a moderate (smaller) increment. Copom affirmed that Brazil’s economy (economic recovery out of recession) might be threatened by “uncertainties” regarding the pace of the current reforms. Before the plea bargaining by the Batista brothers (JBS) and the clandestine audio tape of the conversations be Joesley Batista with Pres. Temer became public, the Central Bank had signaled that the 30-31 May Copom meeting might reduce the Selic by more that 1 p.p.

5.4 – Unemployment declined, slightly

On 31st May, IBGE released its PNAD for the period of February-April 2017. Compared with the last PNAD (January-March) Brazil’s unemployment rate declined slightly 13.7%➔13.6%. The 12-month accumulation was 2.6 million more unemployed. The PNAD for February-March-April 2016 revealed 11.2 million unemployed versus 13.6% in February-March-April 2017. In part, an increase in the number of “self-employed” helped reduce the level of unemployment.

5.5 – Brazil, [much] less competitive
On 31st May, IMD released its World Competitiveness Rankings for 2017. Over the past years, Brazil has steadily declined on this evaluation for 63 nations. In 2013, Brazil was ranked 42nd and in 2016 had declined to 57th but in the 2017 report Brazil was ranked 61st and surpassed Venezuela and Mongolia. Ever since this ranking began in 1969, Hong Kong has been at the top of this list followed by Switzerland. In 2017, Singapore advanced to 3rd rank and the US declined from 3rd rank to 4th rank.


https://www.youtube.com/watch?v=egAY0vgZSCY

In the four components of this survey, Brazil was ranked very badly in 2017 compared to 2013:

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<thead>
<tr>
<th>Component</th>
<th>2013 Rank</th>
<th>2017 Rank</th>
</tr>
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<tr>
<td>General Performance</td>
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<td>61st</td>
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<tr>
<td>Economic Performance</td>
<td>42nd</td>
<td>59th</td>
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<tr>
<td>Public Sector Efficiency</td>
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<td>62nd</td>
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<tr>
<td>Private Sector Efficiency</td>
<td>37th</td>
<td>49th</td>
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Some analysts attribute this sharp decline in Brazil’s competitiveness ranking to the massive corruption in the past 5 or 6 years that involved major firms in the private sector. This survey listed Brazil as the most corrupt country surveyed – surpassed only by Venezuela.

5.6 – May auto sales

Fenabrave released data for auto sales in May on 1st June ➔ +24.63% MoM and +16.77% YoY. In May, 195,586 units were sold. However, Fenabrave maintained its projection of increased sales of +3.11% YoY for 2017.

5.7 – Industrial Production

On 2nd June, IBGE released data for industrial production in the month of April ➔ +0.6% MoM but -4.5% YoY. This was the first positive result in 2017 and the best April result since 2013. The 12-month accumulation is now -3.6% and this accumulation has been steadily declining month by month since October 2016 posted -8.4%. This April data plus the 1st Q/2017 GDP data showed industrial sector growth at +0.9% are clear signs that the economy is improving in 2017. In April 2017, the positive IP result was led by the production of capital goods (+1.5%) and intermediary goods (+2.1%). ➔ See Item 5.1
