Brazil Focus –
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Weekly Report
Jan. 6-12 2018
Looking Ahead ➔ What to watch for?

- 15th Jan. -- IBGE-PNAD unemployment reached % in August-October 2017 period
- 15th Jan. -- Martin Luther King Day observed [National Holiday in US]
- 15th Jan. -- IBGE: November retail sales ➔ % MoM & % YoY
- 17th Jan. -- FGV to announce IGP-10 for January ➔ +0.%, +0.% in December 2017
- 18th Jan. -- BigMac index, Brazil ranked ➔ US$
- 20th Jan. -- City Holiday in Rio de Janeiro [St. Sebastian]
- 22nd Jan. -- Caged ➔ jobs lost in 2017
- 22nd Jan. -- IBGE to release its IPCA-15 ➔ +0.%, & +0.% in December, 2017
- 23-26 Jan. -- World Economic Forum to meet in Davos-Klosters, Switzerland
- 24th Jan. -- TRF-4 to deliberate Lula’s conviction by Judge Sérgio Moro
- 25th Jan. -- EIU 2017 “Democracy Index” ➔ Brazil ranked
- 25th Jan. -- 464th Anniversary of São Paulo (city holiday)
- 25th Jan. -- Transparency International to release Corruption rankings
- 28th Jan. -- SRF - Tax collections: R$ trillion in 2017 ( % YoY)
• 30\textsuperscript{e} Jan. -- ABAS ⇒ Growth of supermarket sales in 2017 ⇒ +% YoY
• 30\textsuperscript{e} Jan. -- FGV: January IGP-M ⇒ %
• 30\textsuperscript{e} Jan. -- Central Bank to announce 2017 fiscal deficit ⇒ billion
• 30\textsuperscript{e} Jan. -- Public Account data for December 2017
• 31\textsuperscript{e} Jan. -- Social Security (INSS) deficit in 2017 ⇒
• 31\textsuperscript{e} Jan. -- IBGE ⇒ PNAD unemployment 4\textsuperscript{th} Q/2017 ⇒ % (million unemployed)

1 - POLITICS

1.1 – Cristiane Brasil barred from Labor Ministry

Traditionally, in Brazil, the President appoints a cabinet minister and one or two days later the new minister is sworn in by the President.

No so, in the case of Dep. Cristiane Brasil (PTB-RJ) who was indicated by the national PTB president Roberto Jefferson (her father) and accepted by Pres. Temer.

Quickly, the press exposed her “problem” with Brazil’s labor laws – she had not signed the labor work card for two of her drivers who had sued for their “labor rights” and back pay. The first level labor court in Rio convicted her to pay R$ 60,000.00 to one driver and R$ 14,000.00 to the second driver and the TRT-RJ (Regional Labor Court in Rio) upheld this conviction.

It seemed “strange” to appoint a person with labor law violations to the Labor Ministry. This would be equivalent to appointing a person who owed some R$ 10 million in back taxes to the Finance Ministry, or a person accused of rural slave labor to the Ministry of Agriculture.

Several labor lawyers agreed with these comparisons and filed suits to impede her swearing in as Labor Minister. A first level federal judge in Niterói agreed and the AGU filed an appeal. This appeal was rejected on 9\textsuperscript{th} January by the TRF-2 (Federal Regional Court in Rio) Vice-President Guilherme Couto de Castro via an injunction because the full TRF-2 is still inactive during the judicial recess period.

Thus, Pres. Temer postponed the swearing in of Cristiane Brasil (that had been planned for 9\textsuperscript{th} January) until a final decision is rendered by the STF – during the judicial recess, by the STF President Cármen Lúcia. This appointment had already been published in the Daily Record on 4\textsuperscript{th} January. However, before going to the STF, the AGU filed an appeal at the TRF-2, in hopes that another judge might overturn the initial injunction.

On 9\textsuperscript{th} January, after a meeting with Pres. Temer in Brasília, Roberto Jefferson told the press that the PTB has no “Plan B” and will insist on Cristiane Brasil as its indication for the Labor Ministry. Jefferson was accompanied by Jefferson was accompanied by Cristiane Brasil and the PTB floor leader in the Chamber Dep. Jovair Arantes (PTB-GO).
The Temer government is pessimistic regarding a STF decision favorable to Cristiane Brasil, but wants to “show” the PTB that the government is appealing in her favor. If the STF decides against Cristiane Brasil’s appointment, apparently the “Plan B” would be the appointment of Arantes to the Labor Ministry.

This is yet another example of judicialization in Brazil, where the Judiciary does not “respect” the check and balances of the three-power arrangement and intervenes regarding Executive Branch decisions. The press questioned the injunction issued by the federal judge in Niterói that was confirmed by the TRF-2, but forgot that in early 2016 the STF (Judge Gilmar Mendes) intervened to prohibit the appointment of Lula (by then President Dilma Rousseff) to the Casa Civil.

On Wednesday afternoon, the TRF-2 denied both appeals – by the AGU and by Cristiane Brasil herself. This put Pres. Temer in an awkward position, because his relationship with the STF President is not very positive. Judge Carmen Lúcia annulled part of Temer’s Christmas Holiday pardon, and his advisors have informally ascertained that she probably would maintain the federal court veto of Cristiane Brasil. For this reason, Temer is holding the appointment of a new MDIC minister until the case of the PTB-Labor Ministry is resolved.

Want more? The press discovered that Cristiane Brasil and several friends spent the New Years holiday at the Fernando de Noronha reserve. They flew on a regular commercial flight, but stayed at the FAB hotel (for military and civil “authorities”) at R$ 250,00 daily rate, while the holiday rate at the private hotels was around R$ 3,500,00. FAB said that this was on a “space available basis”.

Even more? The press has now discovered another (older) Labor Law violation by Cristiane Brasil – regarding her domestic servant (maid, house cleaner) Sebastiana Benjamin in 2003. She claimed that Cristiane never paid her contributions to INSS (Brazil’s social security system). This case was settled by the labor courts for R$ 500,00 to be paid to Sebastiana.

Still More? The press discovered yet another driver (woman) – Aline Lúcia Pinho – who worked for Cristiane Brasil for some 10 years. She alleged that she was employed at the special Secretariat for Healthy Aging, the city of Rio, when Cristiane was Secretary – but she never worked at this Secretariat. Aline alleged that Cristiane fired her while she was on an INSS health leave.

1.2 – Police Strike ends in Rio Grande do Norte

A “work stoppage” by Civil Police, Polícia Militar and fire fighters began in Rio Grande do Norte on 20th December over non-payment of November salaries and the 13th month end-of-year salary plus the December salary. The Defense Minister authorized a contingent of the armed forces to help provide some safety/security in the state capital and some larger cities. Finally, the state government negotiated payment of November and December and the promise to pay the 13th wage in mid-January and the work stoppage ended on 10th January. Part of the negotiations involved the promise by the government to pay the 20-day work stoppage and no other punitive actions against the police.

1.3 – Attempts to “flexibilize” the “Golden Rule”
In Brazil, the “golden rule” was inserted into the 1988 Constitution via a PEC and stipulates that the government can not “over spend” its budget allocation (a budget “cap”) and that the annual budget can only be expanded by the IPCA inflation rate from the previous year.

In the first days of January, the Temer government “floated” the idea that this Golden Rule should be “flexibilized” by another PEC. However, the complaints regarding this change were very loud that the government “forgot” this initiative for the time being.

Another “flexible” initiative by Temer was to transfer R$ 15 billion from the FGTS fund to the CEF to help this federal bank resolve its cash flow problems and avoid violation of Central Bank (and Basileia 3) norms for financial institutions. This was not a “loan” by a direct “injection in the CEF vein”. However, the TCU is questioning this dubious operation.

2 – FOREIGN RELATIONS & TRADE

2.1 – Venezuela paid (part of) debt with Brazil

On 5th January, Venezuela paid part of its debt with Brazil ➔ US$ 262.5 million – due in 2nd Q/2017. Another part of this debt fell due in January 2018 ➔ US$ 274.6 million.

2.2 – STJ to judge 123 year old case

Apparently, the STJ will finally decide the oldest judicial case in Brazil. In 1895, the Brazilian royal family that had been ousted in 1889 by a Republican coup, Princess Isabel sued the new government to return her property – the current Palácio da Guanabara that had been deeded to her by the State as part of her dowry when she married the French Conde d’Eu in 1964. In 1889, this property was confiscated by the Republican government. This case was dormant between 1897 and 1964.

In 1950, the grandsons of Princess Isabel filed another suit regarding the Guanabara Palace. Lower courts denied both requests and they arrived at the STJ in 2009. The royal family does not necessarily want the property returned to the descendants, but instead are interested in receiving a financial compensation.

3 – REFORMS

Nothing this week.

4 – PRIVATIZATION & REGULATION

4.1 – Viracopos
Three groups are studying possible proposals to assume the concession of the Campinas airport Viracopos. A group led by a Turkish investor, a group from Singapore and IG-4 Capital. At stake is a 51% share of this concession currently held by UTC and TPI-Triunfo. The other 49% is held by Infraero.

The first (Turkey-based) group is a pool of firms including an airport operator in Europe, a logistics firm and an investment firm.

The second Singapore-based group is also interested.

The third group is led by led by IG4 Capital, an investment management firm, has held informal conversations with the creditors of this concession – BNDES, Banco do Brasil, Bradesco and Itau. The American firm Cerberus is also participating. This group also includes Schiphol, one of the best international airport operators.

Both UTC and TPI are under court supervised bankruptcy procedures. Viracopos is considered a well administered airport and its air freight potential is large.

⇒ Stay tuned!!

4.2 – Rodanel Norte

The northern section of the highway that circumvents the city of São Paulo had its concession auction on 10th January. Ecorodovias had the highest bid ⇒ R$ 883 million (90.97% over the basic price). Structural investments will be some R$ 581.5 million. When this highway complex is complete it will alleviate much heavy truck and bus traffic through the city of SP – this “through traffic” from one highway to another.

5 - ECONOMICS

5.1 – S&P downgraded Brazil

Early Thursday evening, 11th January, Standard & Poor’s announced that it had downgraded Brazil’s credit rating from “BB” to “BB-” – as doubts increased about the results of the October 2018 Presidential election and the possibility of Congress trimming the costly social security pension system. This decision underscores the concerns that the apparently “business friendly” but very unpopular Michel Temer government might “stall out” (become a “lame duck”) in 2018 prior to the October presidential elections and a shortened legislative period.

This downgrade by S&P puts Brazil three notches below the investment grade level. Brazilian government officials just “shrugged” – saying “This downgrade was already expected”. This means that the Brazilian government agencies and private sector firms will be forced to pay higher interest rates and stiffer loan provisions in 2018. Brazil is now at the same level as Honduras.

https://www.ft.com/content/b45cdd6a-cda7-3d5f-b312-7ea716eb9ba9
5.2 – December IPCA

In December, IBGE posted the IPCA at +0.44%. The IPCA followed an increasing trend in the 4th Q/2017 ⇒ October (+0.42%), November (+0.28%) and December (+0.44%). This December rate was the highest in 2017.

Thus, the IPCA in 2017 posted +2.95% -- below the lower limit (+3.00%) of the IPCA target set by the Central Bank. This was the lowest annual rate since 1998 (+1.65%). In 2017, food prices were down by -1.87%, but bottled cooking gas was up by +16.0% and gasoline was up by +10.32%.

In spite of this low IPCA inflation rate, for 2018, the minimum wage was readjusted even lower ⇒ +1.81%. – a loss of -0.25%. (R$ 28,80). The new minimum wage in January 2017 also had a “loss” ⇒ -0.1%. In 2016, the “gain” was +0.36% and +2.46 % in 2015. The largest gain was in 2012 ⇒ +7.59%.

However – the IPCA in Brasília posted +3.76%, the highest among the 27 state capital cities.

IGPs in 2017 – The three general price indexes compiled by the FGV were negative in 2017. The last negative result for the IGPs was in 2009:

<table>
<thead>
<tr>
<th>Index</th>
<th>2009</th>
<th>2016</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>IGP-DI</td>
<td>-1.43%</td>
<td>+7.18%</td>
<td>-0.42%</td>
</tr>
<tr>
<td>IGP-M</td>
<td>-1.72%</td>
<td>+7.17%</td>
<td>-0.52%</td>
</tr>
<tr>
<td>IGP-10</td>
<td>-1.68%</td>
<td>+6.95%</td>
<td>-0.42%</td>
</tr>
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FGV economist André Braz observed that the IGPs should be positive in 2018 (no deflation) – the economy on a positive track, prices increases (such as fuels), higher food prices, and less favorable climate conditions.

5.3 – November retail sales

After a retraction in October (-0.7%), Black Friday retail sales helped increase retail sales in November (+0.7% MoM & +5.9% YoY). Apparently, in October, consumers postponed their acquisitions awaiting cheaper prices on Black Friday in November. The sectors with the largest increases were ⇒ construction materials (+8.3%), furniture & appliances (+7.5%) and textiles, clothes & shoes (+4.9%).

5.4 – Federal revenues increase
The SRF should release the final federal tax collections data at the end of January, but the expectations for December – some +4.5% above estimates. The government expected tax revenues of R$ 72 billion in December. With this increase, the primary deficit should be around R$ 130 billion. The 2017 “target was set at R$ 159 billion. Market analysts predict that this deficit should be R$ 153.9 in 2018. 🔄 Stay tuned!!

5.4.1 – “Bracket Creep”

Ever since 1996, the SRF-Federal Tax Service has not readjusted its income brackets for its tax levies. According to Sindfisco-Union of SRF Fiscal Auditors, this “bracket creep” has accumulated 88.4% since then. Thus, in 2018, the lowest bracket for federal taxes is R$ 1.903,98 but when “bracket creep” is removed the minimum to begin paying federal income tax should be R$ 3.556,56. Obviously, if this readjustment were made, federal tax collections would be reduced. In 2016 and 2017, these brackets were not readjusted for inflation.

5.5 – Capital flight??

Some analysts are predicting “capital flight” from Brazil to the US in 2018 because of the recent tax reform package approved by the US Congress last month. The US corporate tax was reduced 35%→21%, while Brazil’s rate remains at 34%. Because other production conditions are better in Brazil than in the US -- labor costs, input costs (energy, materials, etc.), property taxes, etc – perhaps the capital flight of direct investments by multi-nationals might not occur.

5.6 – Sigma to invest in lithium production

The Canadian mining firm – Sigma Lithium Resources – plans to invest R$ 230 million in mineral operations in the Jequitinhonha region in Northeastern Minas Gerais. To this end, Sigma plans an IPO in early 2018. This lithium production should come on line in 1st semester 2019. Sigma expects a large increase in the demand for lithium with the increase in the production of electric autos and trucks.

5.7 – Services sector in November

On 12th January, IBGE released data for the services sector in November. Surprisingly, this sector had a considerable increase ➔ +1.0% MoM & +0.7% YoY. According to IBGE, the “leaders” ion this sector in November were services provided to families and information/communication services.