Doing business in Brazil

Although still dealing with the fallout of the Covid-19 pandemic, longer-term positives could be in store for Brazil, where the economy is currently undergoing structural changes that will affect important aspects of the business environment and open up new opportunities for companies.

Trade and economic overview

Brazil has been one of the countries most affected by Covid-19, which clouded the economic outlook and led to a 4.1% drop in GDP last year, according to the World Bank[1].

Recovery momentum is expected to propel Brazil's growth to 3% in 2021, although this is subject to large uncertainty, particularly in terms of the impact of the new wave of the pandemic and the pace of vaccination.

It has been widely reported that Brazil has struggled with the rollout of its Covid-19 vaccine campaign. But the country has a history of successful immunisation programmes, and is now in a position to ramp up production and distribution. "It's taken a while for Brazil to catch up, but it's getting traction now, which is good," says Andre Carvalho, Head of Trade LatAm, Treasury and Trade Solutions at Citi.

Trade is expected to make a positive contribution to Brazil's economic growth this year.

According to Brazil's Ministry of Economy[2], the country's trade surplus widened to US$10.35bn in April 2021, from US$6bn in the same month the previous year, and compared with market expectations of US$11.4bn. Imports in April grew 41.1% to US$16.13bn.

Exports in April surged 50.5% over the previous year to US$26.48bn amid higher sales of manufactured products (43.9%), mining goods (73.2%), and agricultural products (44.4%). Among Brazil's chief trading partners, exports increased to China (55.1%), the EU (37%), and the US (33.7%).

With the Brazilian real having slumped 30% last year, and commodity prices continuing their recovery, export growth looks set to continue.

"The real has been underperforming, which for exports is a positive factor; it's almost a perfect scenario for Brazilian exporters," says Carvalho. "We are also seeing some good momentum thanks to agricultural demand from China, where the economy is recovering fast, which is helping the trade surplus."

Brazil's Economy Minister Paulo Guedes noted in late 2020 that the country's exports to China are forecast to reach US$100bn a year within a decade.

China has been playing an increasingly critical role as a trading partner to Brazil, and Latin America as a whole. Chinese investments in the region are also at record highs.

"China is continuing to consolidate its position in the Latin America region, which from a geopolitical perspective is extremely important to China, given the historical US dominance in the area," says Carvalho.

Nevertheless, Chinese demand alone will not be enough to boost the Brazilian economy. A reactivation of the services sector – the largest component of GDP – will be crucial to sustaining wider economic growth.

A market-friendly agenda

Brazil's long-term economic reform, initiated in the early 1990s, has led to more open trade and investment regimes – and efforts are continuing.

Via its participation in the Mercosur trading bloc, Brazil is negotiating several free trade agreements, including with the EU, which speaks to the aim of integrating the country into global supply chains.

"As a result of the pandemic and the need for supply chain resilience, we're going to see more nearshoring and reshoring of supply chains, and trade agreements are going to become an area of focus again," says Carvalho.

"We've seen a number of our clients in a wide range of sectors, from beer producers to auto part manufacturers, put in place large supply chain finance programmes in Brazil to enable domestic production and consumption, as well as exports to the wider region," he adds.

The Brazilian government has undertaken several measures to reduce bureaucracy and lower import duties – most recently on a number of products needed to combat the pandemic.

"There are many things that have been done to make Brazil more business friendly. There is still a way to go, but that's the trend. These efforts are trying to drive foreign direct investment and infrastructure," says Adriano Milani, Trade Head of Brazil, Treasury and Trade Solutions at Citi.

High on the government's agenda are labour and tax laws – both historical areas of concern for companies doing business in Brazil.

Recent changes to the country's labour legislation aim to simplify labour procedures, and include modifications to a series of rules and regulations to protect both companies and their staff during the ongoing pandemic.

The government has plans to this year approve an overhaul of Brazil's tax code; the proposed reform seeks to unite the country's abundance of taxes, making them more simplified and manageable.

Elsewhere, a significant reform of the country's foreign exchange system is on the cards. The bill of law proposes that foreign capital be granted the same legal treatment afforded to local capital under equivalent conditions.

Snapshot

Currency in Brazil	Economic growth	Top trading partner
R$	3.7%	
Brazilian real	IMF forecast for 2021	**China**

2021 structural reform priorities

- **Social protection:** Increase the effectiveness of social benefits
- **Education and skills:** Enhance equity and outcomes in education and professional training
- **Competition and regulation:** Reduce barriers to competition and trade
- **Tax system:** Reduce distortions in the tax system
- **Environmental policy:** Preserve natural assets and halt deforestation

Brazil Economic Snapshot, OECD, April 2021

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This would, for example, allow a Brazilian individual or entity to open a bank account in a foreign currency in Brazil, which is not possible under the current rules.

"If this reform goes ahead, it will be a game changer for companies in Brazil that import and export because they will be able to hold US dollars – or other currencies – in the country," says Milani.

Other amendments include last year's liberalisation of Brazil's agribusiness laws, aiming to improve foreign lenders' collateral options for commodity and trade finance facilities, by providing greater legal security to foreign banks financing trade in commodities such as soy and corn.

Changes to Brazil's insolvency legislation at the start of this year give foreign lenders greater certainty over how credits and collateral will be treated in the event of a principal or interest default by local borrowers, or in the event that a local borrower files for judicial reorganisation protection.

Trade and investment prospects

With a population of 212 million people, a significant need for infrastructure, and a relatively modest price tag given the depreciation of the real, Brazil offers a number of attractive business opportunities.

"There is a great desire from key economies around the world to see Brazil booming again," says Carvalho. "Many multinational companies are in 'wait-and-see' mode as we approach the end of the recent political and economic crises – and hopefully soon the winding down of the pandemic. There's a feeling that we might be close to another positive cycle for Brazil. Those who witnessed the economic boom from 2012 to 2016 will not want to miss the same opportunity."

Infrastructure bottlenecks have been identified as a key challenge affecting productivity and market efficiency, and hindering domestic integration and export performance. The Brazilian government is working to attract foreign investors to its multitude of infrastructure projects.

"Considering Brazil's infrastructure gap, there are significant opportunities across the sector, from energy to railroads, ports, healthcare, logistics and technology – especially in term of the rollout of 5G," says Milani.

In terms of the country's burgeoning agribusiness sector, higher commodity prices will continue to be tailwinds for the resource-rich nation.

"The mining, steel and agricultural companies in Brazil are very well positioned. These exports are firmly established, and will naturally continue to be a good opportunity because of the positive momentum," Milani adds.

Harnessing opportunities

Companies looking to enter the Brazilian market would do well to seek assistance from trusted legal and tax advisors, and a banking partner, to help navigate the complexities of the local regulatory and tax systems.

"At Citi, we work with a number of multinationals with operations in Brazil who rely on us to point them in the right direction. We're very aware of the difficulties they face when setting up," says Milani.

Citi's legacy in Brazil – and the wider Latin America region – dates back to the early 1900s.

"No other bank in Latin America has the footprint that Citi has today. In terms of trade and supply chain financing, we're in a very privileged position, given our virtually unlimited access to dollar liquidity as a US financial institution, and the bank's dominance in these fields around the world," says Carvalho.

"We're also the largest FX settlement bank in the country, with a market share of 15%, which really shows how deeply embedded we are in the trade flows."

References
1. https://www.worldbank.org/en/country/brazil/overview
2. https://www.gov.br/produtividade-e-comercio-exterior/pt-br/assuntos/comercio-exterior/estatisticas

Citi's "Doing business in…" series, exclusive to **GTR**, takes a look at the practicalities of doing business in, and engaging in cross-border trade with, high growth, complex markets. This third instalment focuses on Brazil, and showcases the views of Andre Carvalho, Head of Trade LatAm, and Adriano Milani, Trade Head of Brazil, Treasury and Trade Solutions at Citi.