Brazil: More To It Than Natural Riches

The rise of the middle class during the last decade has propelled economic growth

Brazil is best known to the world for the Amazon rain forests and the Rio Carnival, appropriately so. They symbolize the immense natural wealth and rich cultural diversity of the largest economy in Latin America. They also showcase the resource base and vibrancy of a population that could make Brazil one of the largest economies in the world.

AN ETHNIC MELTING POT, RICHLY ENDOWED IN NATURAL WEALTH

Ever since Europeans arrived in Brazil in the 16th century, the country has been a veritable melting pot of different races and their cultures. As the indigenous population could not meet the rising labor demand, European colonists brought Africans as slaves to work in the sugarcane fields. By the time Brazil declared independence from Portugal in 1822, the country had an almost equal mix of American-Indians, Europeans and Africans. This predominantly Roman Catholic country now has the largest population of Africans outside the African continent.

Nature’s bounty has helped Brazil become a major supplier of minerals and farm produce to the world. The country is the largest exporter of orange juice, sugar, coffee, tobacco, beef, and iron ore. Brazil is also a major producer and exporter of soybeans, bananas, and cashew nuts.

A CULTURE MORE MULTI-HUED THAN AN AMAZON PARROT

The Rio Carnival, Brazil’s cultural showpiece, may owe its origins to the introduction of Christianity after the arrival of Europeans. Yet, Brazilians transformed it into an uninhibited and exuberant celebration of color, pageantry and camaraderie in a way no other people can even dream of. In Brazil, even the mundane becomes spectacular. No need for reasons to celebrate and nothing will be left out!

The shifting of the capital of the Portuguese empire to Rio de Janeiro in the early 19th century, and the transfer of the royal family to Brazil, accentuated the European influences. European customs and traditions were ingrained into local culture. Even when the country freed itself from Portugal as
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The cross-cultural influences are highly visible in what is now modern Brazilian culture, be it in music, literature, or performing arts. While at different times in Brazil’s cultural history any one of these external cultures were predominant, they all have now amalgamated into a rich medley of indigenous, European and African colors, smells, tastes and sounds. Every heritage became shared, something to be cherished and celebrated by all.

Though some of its celebrations and way of life may outwardly appear European or African, Brazil has also strived hard to preserve the rich indigenous cultures unique to the Amazon basin as they were. When the Europeans first arrived, the land was home to hundreds of tribes with distinct languages and culture. Some of these societies were lost, but the remaining are the links to the country’s vivid past dating back thousands of years. Around 200 distinct indigenous societies, who speak as many as 180 different languages, now live much like their forefathers did in exclusive preservations across Brazil. That is diversity at its very best.

USHERING IN ECONOMIC STABILITY

For a long time, the mention of Brazil evoked images of soccer prowess and the sensuous samba, but otherwise it was a rather poor and underdeveloped country. But with the onset of the new century, it appeared that there was more to Brazil than met the eye.

During the decade beginning 2003, the biggest economy in Latin America also emerged as an important constituent in the BRIC grouping of economies, driven mostly by commodities, credit, and consumption. The services sector, which includes banking and retail, contributes the most to the country’s GDP, while industrials are the second biggest contributor, followed by agriculture. Exports consist mainly of iron ore, food and agricultural products, as well as machinery and transport equipment.

Simple as it may sound, the transformation has been an arduous task for the country, which at one point in the mid-1990s witnessed hyperinflation hit a whopping 2100%. Financial crises resulting from overspending weighed heavily on the economy, which even had to change its currency several times to bring about a semblance of economic stability. Inflation still hovers above the government’s target, but is nowhere close to the levels seen in the dreaded 1990s when the salaried class used to run to the supermarkets with their pay checks to make their purchases before the value of their currency eroded any further. History, they say, is the best teacher. The hard economic lessons from its not-so-distant past made Brazil tread cautiously ever since. The firm establishment of democracy as the system of governance in the 80s after decades of autocratic rule also aided the economic transition.

COMMODITIES POWERHOUSE

Economic stability achieved, Brazil was lucky to have a visionary like Lula da Silva assume office as president in 2002. Meanwhile, China was beginning to spend huge sums on building its infrastructure, which required large quantities of raw materials like iron ore, the main ingredient used in steel-making. Brazil, blessed with minerals and natural resources, seized this opportunity to satisfy China’s
Bilateral trade between Brazil and China flourished so much that the Middle Kingdom soon replaced the United States as Brazil’s chief trading partner. To put things in perspective, commodities as a share of the country’s exports increased from 50% in 2000 to 70% for the year ended April 2013.

The surge in export revenues was a godsend for the struggling Brazilian economy, which clocked a growth rate of 7.5% in 2010. Lula, who came from the working class, realized that inflation hit the poor really hard. By launching schemes such as the Bolsa-Familia, which transferred money directly to the poor on the condition that they immunize their children and send them to school, the Brazilian government was able to lift millions out of poverty and elevate them to the status of the lower middle class, who comprise more than half of a total population of 200 million. Revenues from exports were also channelled to create more jobs and raise the minimum wage. Thanks to the rise in incomes and some shrewd social engineering, an average Brazilian household now brings home between $127-446 per person a month, and has access to the comforts of modern living such as refrigerators, ovens, and washing machines. The poorest sections of society, in particular, benefited greatly from the new opportunities and their incomes almost doubled over the past decade.

Though iron ore occupies a prominent place in Brazil’s export basket, Brazil is also a top exporter of edible agricultural commodities such as soy, sugar, orange juice, and coffee, not to mention its poultry and beef exports. Beginning in 1973, when Brazil was still a net importer of food, the country decided to expand domestic production with the aid of scientific research. Natural advantages such as the availability of land and water helped, but it was the exposure to global competition which pushed Brazilian farmers to give their very best. As a result, in the last four decades, Brazil has ensured its place as the first tropical agricultural giant, which is capable of giving the big food exporters such as the U.S., Australia, Canada, Argentina, and the European Union a run for their money.

Brazil, which was dependent on energy imports, was badly hit by the oil shock in the early 70s when the price of oil rose by nearly 70%. However, the innovative Brazilians found a way out by producing fuel-grade ethanol from sugarcane which the country had in abundance, giving Brazil a huge lead globally in the use of bio-fuels. However, it was the discovery of extensive oil fields offshore in 2007, described by the then president Lula as a “gift from God” which turned the spotlight on Brazil. Though the government-owned Petrobras is sometimes given preferential treatment in oil auctions and oil field allocations, Brazil is set to emerge as a major oil exporter in probably a decade’s time, according to a Financial Times report.

CREDIT-FUELED CONSUMPTION

Over the course of the last decade, Brazil’s sizeable middle class expanded further to more than half of the country’s population today, thanks to the fast economic growth, low unemployment, better education and above all, income redistribution in the form of social transfers. The combined purchasing power of these people made Brazil an attractive consumer market. As their standards of living improved with rising wages and money transfers from the government, Brazilians began to spend on non-essentials with money loaned from banks or credit card companies. The steady economic growth over the years instilled a sense of confidence in the average Brazilian about his job and future,
After the global financial crisis in 2009, Brazil entered a new era of credit-led growth. Changes were made to bankruptcy regulations, which made it easier for banks to lend. Availability of private credit in the Brazilian economy has almost doubled since 2007, while subsidized loans from the state development bank BNDES were also made available. The new middle class, already buoyed by a substantial rise in real wages, lapped up lending products such as payroll-deductible loans tailored to suit their requirements. Lower interest rates also encouraged lending. Co-branded credit cards issued by banks and prominent retailers were a big hit with consumers. Consumer-oriented sectors such as retail, automobile manufacturing, and financial services have benefited from the consumer spending boom. On the flip side, Brazilian consumers are overstretched as a major portion of their salaries goes into the repayment of loans, which they had taken out to buy televisions and cars.

KEY TAKEAWAY

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THE WAGES OF COMPLACENCY

Slowdowns are just temporary phases in the life cycle of an economy as any keen observer of global economic developments would tell you. Perhaps Brazilians, who have witnessed bigger crises in their lifetimes, should not have a problem with the current loss of growth momentum either. However, the mass protests which erupted in Brazil’s major cities in June 2013 and jolted the Dilma Roussef administration were without precedent. While the increase in bus fare was the immediate trigger, it had been long time coming as the public has been reeling under the shackles of rising inflation, corruption, high taxes, and poor public services.

Indeed, the rise of the middle class in Brazil has been one of its most inspiring success stories. But as this group has grown, their demands have also kept pace and this has posed a dilemma. For a really poor person, the biggest concern is his next meal. But, for a well-fed person who has access to material comforts, the needs are different: better roads, a corruption-free government and so on. Brazil spends just 2% of its GDP on infrastructure, compared to 5% by India and 13% by China, according to The Financial Times. It appears that the Brazilian government may be moving in the right direction by launching infrastructure projects totalling $407 billion in the run-up to the soccer World Cup and the 2016 Olympic Games to be hosted by the country.

Ironic as it may sound, Brazil spends more than it can afford in its quest to build a welfare state --- public spending has shot up from 22% of GDP to 36% of GDP in the last 25 years, which is no longer sustainable for a developing economy. Surprisingly, for a relatively young country, most of the money is spent on pensions and other welfare measures for the elderly. Moreover, the country’s Constitution guarantees free health care and a university education to its people.

Brazil has high taxes, which means that there is little room for further increases. The demand for decent public services can probably be met by reducing the huge pension benefits, simplifying the tax system, and reforming labor laws, not to mention cutting the red tape, as The Economist pointed out.

THE ‘BRAZIL COST’

Brazil’s taxes are equivalent to 36% of the country’s GDP, the highest in the developing world and comparable to the European welfare states of France and Norway. High personal and corporate tax is a concern for both the salaried class and potential investors. Moreover, the tax system is notoriously inefficient with mid-sized Brazilian firms having to spend about 2,600 hours a year on average to file
Astronomically high living costs and raging inflation affect Brazil’s competitiveness. Everything in Brazil, ranging from cheese pizzas to hotel rooms to domestic appliances and cars, is much more expensive than in many other countries. What’s more, huge labor costs stand in the way of hiring as does Brazil’s inefficient education system. High interest rates, rampant crime, and steep import duties all add to the cost of doing business in Brazil. Ruchir Sharma points out in his book *Breakout Nations* that Brazil’s productivity only marginally increased at an annual rate of about 0.2% compared to 4% in China between 1980 and 2008. In the long-term, boosting productivity will be crucial for Brazil to progress.

**BRAZIL, THE MASTERFUL INNOVATOR**

Brazil’s growth crawled to 2.7% in 2011 and a meager 0.9% in 2012 as big buyer China showed signs of a slowdown. It was then that Brazil realized that a growth model based on commodity exports alone would not be sustainable in the long run.

Still, Brazil has been able to leave its stamp on a gamut of industries ranging from aircraft manufacturing to agriculture to deep sea oil exploration. Embraer, the third-largest commercial jet maker in the world, is well noted for its business model as well as its innovative aircraft design. The agricultural research agency, Embrapa, went a step further, importing soybeans from Asia and cattle from India to suit the inhospitable climate in some of Brazil’s farthest regions. Similarly, oil major Petrobras has successfully made use of seismic technology for its underwater explorations, setting the stage for Brazil to emerge as a big oil exporter. Thanks to the rapid evolution of the retail sector, some of Brazil’s consumer brands are now quite well-known outside the country’s borders too. Not to be left behind, Brazil’s automotive sector has developed vehicles capable of running on both petrol and ethanol. Internet usage is on the rise, even as Brazil’s spending on technology and research is going up by about 7% a year.

**REFORMS ARE THE NEED OF THE HOUR**

Notwithstanding the socio-economic issues which need to be addressed, Brazil still has many things going for it. Huge reserves of commodities, a culture of technological innovation, and a huge middle class with an insatiable appetite for shopping are definitive positives for an emerging economy. However, the key to an economic rebound lies in implementing reforms in business to improve competitiveness and in the political system to root out corruption and eliminate structural hindrances to growth.
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