Country report - Brazil

Brazil: an overview

Brazil, "officially the Federative Republic of Brazil" (Encyclopedia Britannica, 2010) is slightly smaller than the United States. Being the world's fifth largest country and largest population country in Latin America with about 193 million and is surrounded by lush vegetation especially in the northern regions, and vast wetland areas (BBC NEWS, 2009). Its main exports include manufactured goods, coffee, iron and other agricultural products (Branford, 2004). The majority of the population in Brazil is Roman Catholics (80%), and their ethnicities make up are 55% of white which includes Portuguese, Italian, German, Polish and Spanish, 38% of mixed white and black, 6% of black and a smattering of Japanese and Amerindians (1%) (Kwintessential Ltd, 2009). Nearly everyone speaks Portuguese, and there are no differences between provinces except for accents and vocabulary (ibid).

Among all South American countries, Brazil is the most influential, apart from being one of the world's biggest democracies.(BBC NEWS, 2009) Having long realized that domestic savings will not be sufficient to sustain long-term high growth rates, the policies of Brazil generally lean towards the encouragement of foreign investment. BBC NEWS (2009) mentions its President Luiz Inacio Lula da Silva has advocated the elimination of protectionist barriers to combat the effects of the global economic crisis. As such, it has been the greatest beneficiary from Latin America's foreign direct investment. Nevertheless, much still needs to be done to enhance its tax regulations for a more conducive environment for investments.

Opportunities versus risks

Brazil has a lot to offer to the interested corporations. Economically, it has an increasingly stabilized financial capacity to withstand financial market volatility. According to Political Risk Yearbook: Brazil Country Forecast by The PRS Group (2008), posits moreover, the sizeable offshore oil and gas fields just discovered may also instrumental in making and brightening the economy of Brazil be one of the best prepared in South America to withstand a consumer-led recession in the US. It also has great domestic market potential, acceptable business regulations and favorable labor overheads. Its manufactured products account for a hefty share in exports, and one may optimistically assume the preservation of the fundamental macroeconomic stability (ibid).

In addition, the main grocery players have already created strategic alliances, joint ventures and traditional cooperatives to create a favorable environment for the field (PR Newswire, 2007). Improved quality and cost have been adopted and standardized for the retailers' and suppliers' products and practices, which have led to further strategies for specific niches for small and medium competitors (ibid). Besides, another great opportunity is if the country were to stabilize and reduce its domestic debt, as it would open up doors for becoming the primary provider of commodities in Asia, and especially of China (The Council on Foreign Relations, 2002).

Public debt for Brazil has yet to wane, and the state is still not wholly impervious to sharp declines in prices of raw materials. The recent trends of slowing credit and its directly proportional relation to retail sales figures are also a cause of concern for foreign retail investors (The PRS Group, 2008). Nevertheless, in light of the government's stimulus packages, easing monetary policy, although the consequences of the global financial crisis on Brazil will result in GDP contraction at around 1.7% in 2009, the economic will be recovered moderately in 2010 to 2.7%. Cutting interest rate and reducing requirements of bank reserve to lower inflation rate, the economic potential of Brazil is anticipated to be strong and its economic outlook both in medium and long term is bright (Blaauw, 2009).

Furthermore, Brazil has recently been on the global spotlight following the announcement of the International Olympic Committee of the megalopolis Rio de Janeiro's winning the bid as venue of the 2016 Olympic Games (O'Connor, 2009). South America has never before been honored to host the prestigious sports competitions, and this latest development could only be seen as an impetus to spur further development in both the micro and macroeconomic levels (ibid).

Risk rankings

Coface North America, a trade risk management group, regularly ranks countries according to risk levels in year 2008. It takes into account vulnerabilities in growth, the banking sector, and governance, apart from external over internal indebtedness and currency liquidity. Brazil has been given a ranking of A4, which is midway between the most ideal level, A1 (indicating a steady political and economic environment with positive effects on an already good payment record of companies; with very weak default probabilities), and the least favorable stage, D (indicating the high risk profile of a country's economic and political environment which will further worsen a generally very bad payment record). A4 is described as, "An already patchy payment record could be further worsened by a deteriorating political and economic environment. Nevertheless, the probability of a default is still acceptable" (Coface North America, 2008). An identical rating was given for business viability, which translates to shortcomings in terms of debt collection, information dissemination and inter-company dealings (ibid).

Brazil as an offshore services location

A study regarding the viability of Brazil as an offshore services location was conducted last year with taking into account such factors as political and economic environments, and global and legal maturity. According to Dreyfuss and Karamouzis (2008), Brazil ranks "the best one-third" among 178 countries. Besides, international risk ratings are in the lowest record ever and investment grade rating was received in 2008 with growing direct foreign investments for more than US$30 billion and the country is included among the best top five destinations. Its cultural diversity, moreover, has made its business practices similar to that of Western Europe and the United States.

With regards to the risk assessment of Brazil, a slight current account deficit in 2009 is expected. This will be buoyed, however, by foreign direct investments and external debt ratios (Coface North America, 2008). Compared the country and business climate ratings of several nations such as China, India and Russia, it mirrors the fact that although the country has already seen steady growth under President da Silva, it has still a wide gap to cross if it has any plans of surpassing the other members of the Bric group: Brazil, Russia, India and China. Its average GDP growth is only 2.8%, although greater than all South American countries combined, still puts it at the lowest among the four nations (Coface North America, 2008).

Legal and regulatory risk

Likewise, the legal and regulatory systems are considered as risk by complexities and slow judicial process. Extensive regulation, although reduced in the past decade, has made Brazil 122nd out of 178 countries in the World Bank rankings for ease of starting business (Dreyfuss&Karamouzis, 2008). Despite of this, Brazil is a signatory of Intellectual Property (TRIPS) Agreement since 1994, which is a legal protection of knowledge and ideas comprise new goods, services and production processes (The PRS Group, 2008).

In this research of American supermarket retailer, its unique high quality customer service and distinctive check-out technology ideas can be protected under the Intellectual Property (TRIPS) Agreement. However, enforcement is not stringent and substantial works remains to be done (Dreyfuss, &Karamouzis, 2008). It is reasoned by Brazil has not ratified the World Intellectual Property Organization (WIPO) Treaties on Copyright and Performances and Phonograms. Hence, especially in enforcement, is a problem for intellectual property rights protection (The PRS Group, 2008). As a result, in 2006, the country was retained on the watch list of Special 301 priority, and moreover, the opportunity on political condition is fair (ibid).

Stable democracy but unstable political system

In political climate, being one of the largest emerging markets and democracies in the world, Brazil is enjoying a stable democracy since the end of military rule in year 1985 (The Economist Intelligence, 2008). Democracy has been well developed with transparent power divisions between the executive, legislative and judiciary (Blaauw, 2009). Besides, transitions were run smoothly between selected governments (The Economist Intelligence, 2008) Although corruption scandals in Brazilian politics affect all level of government and remain as a major problem, Brazil will play an active role in world recovery plan to withstand current rescission and enhance country position as focusing on regional trade integration and cooperation (Blaauw, 2009).

In spite of the strong power of institutions, the ineffective political system is considered as a risk and political reforms are required for party loyalty, transparency and effectiveness improvements (The Economist Intelligence, 2008). As the party system in Brazil is highly fragmented with more than 19 parties, the interconnection between state governments, legislative and executive bodies is difficult and therefore implementation for policies is often slow and complicated (Blaauw, 2009).

Social inequality

On the other hand, the social condition in Brazil is described as high inequality, numerous challenges in the form of educational, racial and ethnic divisions, income distribution and social security reforms have yet to be addressed. There are a deep division between the blacks and whites. Compared to the whites, blacks are lack of quality education, healthcare, political representation and income distribution is extremely uneven (The PRS Group, 2008). The lowest 10% of income earners only taking 0.8% of total income, however, the highest 10% earn nearly 46%. As a result, Brazil has a high GINI-coefficient at 58.0 with about 20% of Brazilian are living in poverty. (Blaauw, 2009).

Poor infrastructure3

In addition, infrastructure in Brazil such as ports, roads, and rail remains much to be desired. The Brazilian have the concept of time and try to be punctual, therefore the inefficiently run seaports can be a main serious impediments to trade (The PRS Group, 2008). However, most of products are imported by sea, with the high offloading cost, complex paperwork at ports and long turnaround time, it is considered as a risk (ibid). Notwithstanding there are none significant improvement yet by the Port reform legislation, government will take effective steps to enhance port facilities (ibid). For instance, partially privatize The Rio and Espírito Santo ports which can shorten turnaround time and lower costs (ibid). Secondly, with the lack of extensive rail network, inner state transportation is mainly transported by truck through the poor highway network system (The PRS Group, 2008). The high fuel costs add to the transportation cost significantly (ibid). However, river transport improvements have been limited regarding to the environment concerns and geographic constraints (ibid).

Increased demand for frozen food

It is considered that the vast multitudes of Brazilian spend a third of incomes on food, and are increasingly receptive to microwave meals, is an encouraging point for retailers. It is believed that nowadays are more receptive to the acquisition of kitchen appliances such as microwaves (Newswire Today, 2006).

Another corollary trend for the supermarket industry is the increasing demand for frozen food in a typical Brazilian meal due to high level of disposable income and busy life. Newswire Today (2006) reports the fast growing frozen food has created a leap of nearly 300% on the sales of frozen vegetables in the past three years as Brazilian per capita income is rising with the recovering economy. This favorable turn will lead to better living standards as consumers begin to dispense of their higher personal incomes (ibid).

Wander (2006) agrees with this observation. He states that the food industry is one of the chief driving forces of Brazil's economy. It accounted for 600,000 jobs and a quarter of Brazilian exports in 2005 (ibid). A possible risk on the trade may be the uncertainty of the supply chain (Farina &Viegas, 2003). All supermarkets have informal agreements with wholesalers, who also carry the added responsibilities of waste control and supply management (ibid). These wholesalers moreover prefer to supply small and open-air traders, which in turn contributes to their longevity in spite of the retail giants. Associations have been created, too, to ultimately guarantee competitive prices and reduce waste, creating a win-win situation for both retailer and wholesaler (ibid).

The gradual proliferation of multinational firms

Now is an auspicious time for multinationals to consider entering the robust Brazilian market due to economic stabilization, the spate of liberalization and the growth of the consumer market, as Farina &Viegas (2003) explains. Firstly, Brazil has become the de facto headquarters for the Southern Common Market, commonly known as the Mercosur. Brazil's GDP, in fact, was 62% of the Mercosur's GDP, and its imports accounted for 60% of Mercosur's. Mercosur, it must be noted, did not fully live up to its ideals (ibid). Regional specialization naturally led to oftentimes painful change in its member's economies (Farina 2001). As a result, protectionism became the common response. It is a step backward and contributes to the hindrance of integration and regionalism of the agricultural food trade (ibid).

Secondly, although by 2000, 8 of the 10 largest food companies in Brazil were already multinationals, the arena is so dynamic as it is far from becoming saturated with the 55 largest chains are responsible for half of total sales (Farina 2001). The U.S., furthermore, has long invested in Brazil's food industry. Since the liberalization of investments laws and the stabilization of the economy, investments were increased dramatically (Blaauw, 2009). American companies usually compete against their European counterparts like Unilever, which is next largest food company in Brazil with sales of $1 billion (Farina &Viegas, 2003). Thirdly, although Ken Maxwell opined that "Mercosur has failed for all sorts of reasons" (The Council on Foreign Relations, 2009), Brazil has the ability to trade more efficiently and become the regional leader that it is currently touted to be (ibid). Fourthly, the low-income elasticity of consumers makes this industry less sensitive to economic fluctuations (The PRS Group, 2008). Lastly, the capital goods and food industries have invested in cross-operational plants across the nation's members which "allows for scale and scope economies, and for tracking customer preferences and supplier trustworthiness" (Farina 2001).

The pattern for international production has three determinants: firstly, the competitive of companies in relation to the local industries; secondly, the nature of the location that enhances the value of these competitive advantages; and thirdly, the extent to which the market for these benefits are exemplified by the company itself (Newswire Today, 2006). Thus, one can now see the appeal of Brazil to foreign capital which is the considerable market size, a base point to other Mercosur countries, economic stability, manageable labor fees, tax incentives, and ready access to resources. In some aspects, the multinational by way of merger and acquisitions have advantages not available to a national firm (Blaauw, 2009). These include the easy release of products already distributed at the global level, and smooth transitions in local practices (Farina, 2001).

This developing trend of entries brings about favorable change in terms of competitive strategies, new technologies and heightened overall performance, all with the aim of strengthening their share of the store shelves (Farina, 2001).

Conclusion and Recommendation

A hint of caution must be given still when considering Brazil as an avenue for expansion. No matter how much improvement has been recorded, critics have been quick to point out to the often glaring disparities between the figures on paper from the actual situation. Indeed, inasmuch as Brazil is known for excellence in sports, it has also lagged historically in areas such as the economy and societal reform (Buarque, 2007). A common joke among Brazilians is that their country is one with enormous potential and will always be one with enormous potential. This is because despite numerous advantages, such as a sizeable economy and population, and vast natural resources, the nation has as yet failed to realize its potential. Case in point was that at the end of year 2001, public sector of Brazil's debt to GDP ration was 48 percent. In six months, the figure jumped 11 percent (The Council on Foreign Relations, 2002). It is corroborated this by stating that at the end of the year, it will become 60 percent due to its being indexed either to the dollar or to interest rates. Brazil has still has the daunting task of reducing its domestic debt to be able to perform optimally in the global economic arena (ibid). Indeed, the pressure is now on for the incumbent president to implement long-delayed reforms such as the reduction of corporate taxes, the decrease of public expenditures and the augmentation of private infrastructure (The PRS Group, 2008). The latter is especially necessary, as a ten percent decrease in freight costs can already improve imports by fifty percent. World class engineering and construction firms are something that Brazil has, however, and it gives this researcher confidence that it can surmount the odds of the latter.

All crucial things being considered, recommendation would be to seriously mull over Brazil as a reasonably viable location choice. This Latin American industrialized giant has a myriad of opportunities still waiting to be tapped by enterprising and willing multinationals. The country is expected to reach investment grade courtesy of international credit ratings agencies anytime soon, which will only enhance its reputation in international circles. Also, despite the above mentioned lack of essential reforms, Brazil is anticipated to advance its economic power with the continued influx of local and foreign companies. Already exports from Brazil to the United State have grown almost 19% from 2007 to 2008, and imports into Brazil from the United State have risen by more than 33% (Blaauw, 2009). Total operational costs are at par with the other countries being deliberated on. Among cities, Sao Paulo has the most expensive office space, whereas the inner suburbs offer more manageable rates. Orientation to Brazilian customs is also suggested for a smoother business transition; periodic monitoring is advised as implementers of Brazilian business practices and government policies may resort to informality rather than acquiescence to bureaucratic legal requirements considered complex (Dreyfuss, Kamarouzis 2008).

The American supermarket retailer of this research is affiliated with will still be able to exercise its key strength of high quality customer service as the Brazilian educated work force may be relied on for their good business acumen, client empathy, flexibility and a high literacy rate of 86.6% (Dreyfuss&Karamouzis, 2008). The innovative check-out technology would also give a practical and competitive edge to other players already plying the trade, as it frees up more time for store assistants to work in other areas of the store. It scores points on convenience too as the available system models allow consumers ease of transferring groceries, whether they are hauling bags or trolleys.

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