

I. Introduction

The economies of California and Brazil are remarkably similar and that latter can learn much from the former in its own development. Both are ranked in the top ten largest economies in the world with Brazil being seventh and California eighth. Also, both will have been hosts to the World Cup and the Olympics. Brazil's economy is characterized by agriculture, mining, manufacturing, and the service sector which is similar to California's economy, minus mining. There are many opportunities for California businesses to be involved in the largest emerging market in South America. The two economies complement each other and Brazil can learn much from California's experience in hosting both the World Cup and Olympics.

II. Brazil's Economy at a Glance

Brazil is one of the most important emerging markets in the world today. By 2025, its economy will be the same size as Germany's. Since 2003, Brasilia has improved its "macroeconomic stability, (built) up foreign reserves, and (reduced) its debt profile by shifting its debt burden toward real denominated and domestically held instruments."¹ During the financial crisis Brazil experienced two quarters of recession as global demand for commodity exports decreased. In 2009, the economy contract -0.6% but in 2010 grew by 7.5% becoming one of the first of the emerging markets to recover.² Since 2009, industrial production has been either above potential and rising or above potential and moderating.³ By comparison the U.S., EU, and Japan continue to have diminishing capacity utilization.

¹ CIA World Factbook 2011

² IMF World Economic Outlook 2011

³ Ibid

Brazil continues to invest in its economic development and has made great gains since the 1990s. In fact, Brazil will experience one of the largest increases in share of the middle class as a percentage of total population in the world.⁴ However, 21.4% of the population lives below the poverty line.⁵ Infrastructure still requires much investment as 24% of the population does not have access to sanitation facilities.⁶ Ports, roads telecommunications, and energy industry will need to be developed as well in order meet and match Brazil's growth.

III. Infrastructure

The country's competitiveness remains in its ability to answer its infrastructure challenges. Investment in infrastructure will need to equal 5% of GDP in order to sustain economic growth.⁷ Unfortunately, Brazil is ranked low in terms of its ability to maintain its growth through proper infrastructure being 105 in terms of roads, 123 in terms of ports, and 95 in terms of airports of airports in comparison to 139 countries.⁸ Brazil plans to invest \$562bn from 2011-2014 in infrastructure in a plan known as the "Accelerated Growth Program" (PAC) with 30-40% expected to come from the private sector.⁹ Most is planned for investments the government wants completed in time for the World Cup and Olympics.

Brazil has outdated port facilities and inadequate road and rail links which are threatening to make it uncompetitive in the global economy. As trade and port operations grow companies in industrial distribution and logistics are welcoming opportunities to reduce costs. Currently, transportation costs for importing goods are 25-50% higher when compared to developed

⁴ Cardenas, Mauricio, Homi Kharas, Camila Henao. (2011, April 26) Latin America's Global Middle Class. Brookings Institute.

⁵ World Bank Data Catalog 2011

⁶ Ibid

⁷ Latin Business Chronicle. Brazil's Infrastructure Challenge. (2011, September 9)

⁸ Pratts, Jennifer. Infrastructure in Brazil: Enhancing Trade, Investment, and Competitiveness. (2011, May 6) Council of the Americas

⁹ Leahy, Joe. Growth puts strain on Brazil infrastructure (2011, March 27) Financial Times

nations.¹⁰ Ports are congested, with long wait times, and customs clearing is difficult. Los Angeles is experienced in dealing with such obstacles and can use its tacit knowledge to its benefit in partnering with Brazil to develop the necessary infrastructure.

Brazil has 34 ports, with the largest at Santos near Sao Paulo, and 95% of its trade passes through them.¹¹ More than 100 private terminals are run by exporters of Brazil's raw materials and are developing and implementing new technologies at the ports and railways.¹² The government's port infrastructure projects have laid the foundation for investments in efficiency and scale by private companies.¹³ For example, the government is pressed to increase capacity in order that the ports may handle the large super-containers following completion of the Panama Canal expansion project. Ultimately, the country's goals are to improve access, arrival, and departure of cargo.

Advances in port capacities will have to be matched by more rail and road investments. In terms of land area, Brazil is almost twice as large as the EU. Trade distribution and logistics falls on the country's poor highway system where only 12% of local and federal highways are paved.¹⁴ Unfortunately, Brazil has to rely on roads for 69% of its transport needs. Additionally, Brazil has no long term planning for road building to be inserted in an inter-modal system. The rising middle class is demanding more basic infrastructure needs to connect cities and the coast to the inland. Also, the agriculture industry, which is based in the interior, needs better roads to move food to the coast and ports. American firms will have to compete against European businesses, which have just as much experience in developing public transportation systems in rail and road.

¹⁰ Pratts, Jennifer. Infrastructure in Brazil: Enhancing Trade, Investment, and Competitiveness.

¹¹ Morris, Harvey. Ports: Traffic grows at double the rate of economy. (2010, May 6) Financial Times

¹² Ibid

¹³ Ibid

¹⁴ World Bank Country Data 2011

Brazil is pressed to have these infrastructure needs met by 2014 and 2016 in time for its sporting events. However, the country is behind schedule and underfinanced.¹⁵ In fact, the government has “not taken advantage of the private sector’s capacity and willingness to participate in the process”¹⁶ Almost all of the funds are coming from the public-sector as the government isn’t creating areas for the private sector to invest. Brasilia is not making the regulatory changes needed to attract private capital. The country’s leaders are being urged to bring in more private investors for its development. In order to accomplish this the government needs to streamline the licensing process. Also, the state development bank cannot hold a monopoly in the projects. The benchmark lending rate in Brazil is now 12.50%. The state development bank provides subsidized loans at low interest rates, thus, making it very difficult for private financial institutions to compete. Investors should know that when doing business in Brazil the tax and legal systems are complex. Businesses need to do their homework before entering this market. In fact, a joint-venture with a Brazilian company is probably the best mode of entry for most firms. Despite this difficulty, there are many advantages for investors in Brazil: low political risk, well-developed local capital market, and has a history of high private during the 1990s.¹⁷ Overall, opportunities abound for California businesses to apply their tactic knowledge and experience in infrastructure development if the right partner is chosen.

IV. Services

The energy sector will be one of the main drivers of infrastructure investment. The regulatory framework for this industry makes it attractive for investors. One of the most difficult

¹⁵ For example, only two of thirteen air terminals are on track to be completed by 2014 and Itaquerao stadium in Sao Paulo has not been built

¹⁶ Pratts, Jennifer. Infrastructure in Brazil: Enhancing Trade, Investment, and Competitiveness.

¹⁷ Latin Business Chronicle. Brazil’s Infrastructure Challenge.

energy infrastructure projects in Brazil is penetrating its deep water oil and gas fields.¹⁸ A major oil and gas reserve was found offshore and is trapped under 7,000 meters of sea water, rock, and salt. To tap into these resources something other than pipelines will be needed as the water pressure would be too much to bear. The technology exists to reach the oil and gas but no one has ever done this before. Petrobras will be the energy company extracting this and will need to do a joint venture in order to succeed. Other areas for investment and joint ventures in energy are in ethanol. Brazil has “the technical know-how of producing high-quality ethanol that is cheaper and cleaner than U.S. ethanol.”¹⁹ Chinese companies are rushing to Brazil to take advantage of its access to energy and tap into its knowledge. The U.S. can lose out on this if it does not act quickly enough.

Brazil is a great and expanding market for environmental services and California holds experience and advantages in this sector. Brazil is working to protect its rainforests and develop a sustainable forest management system in the Amazon region. Currently 29% of the Brazilian Amazon is designated as protected, 25% is privately owned, and 46% is untitled public land. The Amazon is a major source of tropical hardwood and “most timber extraction occurs in an unplanned and often illegal fashion, damaging the remaining trees, opening gaps in the canopy, and leaving large amounts of debris which make rain forests susceptible to burning.”²⁰ California businesses can provide ways to help with protecting and conserving natural resources and provide scientific research on forestry conservation.

Brazil has a growing need to develop its water and sewage system. Half of the population lives in an urban setting and many of these areas are experiencing an increase in slums which in

¹⁸ Wheatley, Jonathan. Oil & gas: Solutions to secret of difficult oil fields. Financial Times (2010, May 6)

¹⁹ Aramayo, Carlos and Carlos Pereira. Obama’s Visit to Latin America: Redefining U.S.-Brazil Relations. (2011, March 15). Brookings Institute

²⁰ World Bank Country Data 2011

turn is increasing pollution to water sources. Much of the country has “no appropriate infrastructure for water supply, sewerage, drainage and solid waste management.”²¹ Local governments need to develop the ability to manage water basins in an environmentally sustainable manner and expand its sanitary infrastructure.²² To help meet this long-term challenge the World Bank is lending \$485m to the state government of Rio de Janeiro for human development.²³ Of Brazil’s population, only 42% are linked to a sewage system and only 32.5% of the water is treated.²⁴ The country is close to reaching its goal of providing water to 87% of the population but is off target of providing sewage access to 77%.²⁵ However, its inability to meet waste treatment goals is increasing environmental concern over pollution in the coastal waters. Unfortunately, there remains a widespread lack of awareness by the public on the importance of sanitation.²⁶ California has learned a lot through its history and development on water conservation and sanitation and public sewage. This is another area where California’s experience would bring a big pay-off for investment in Brazil.

V. Conclusion

Unfortunately, most California businesses often overlook Brazil. Very often, due to geography, we spend our time and focus on Mexico and Asia and for very good reasons. However, Brazil provides California with an opportunity to apply its knowledge and experience and receive a great return. California can help Brazil achieve its development projects in order to be prepared for the World Cup, Olympics, and future status as a developed economy. Brazil

²¹ Ibid

²² Ibid

²³ Morris, Harvey. Brazil struggles to rise to sporting occasions. (2010, May 6). Financial Times

²⁴ Morris, Harvey. Water and sewage: Taps turn on but there’s trouble with the pipes. (2010, May 6). Financial Times

²⁵ Ibid

²⁶ Ibid

has a favorable environment for investors but due to the complexity of regulations and taxes it is best to enter this market in a joint venture with a domestic firm. California should not hesitate to act because other states and countries, especially China, are realizing the opportunities available in South America.