Brazil's competitiveness challenge

YES, PRESIDENT ROUSSEFF is a member of the Workers Party, but lately her administration's efforts to keep some workers in their jobs in, for example, the auto industry may be threatening jobs in other Brazilian industries. Take the electricity industry. In September the administration announced Provisional Measure 579, which among other things reduced electricity rates. The result? Immediately recognizing that power company revenues would plunge, investors pulled away. Since August, major power companies listed on the Bovespa stock exchange have lost US$34.6 billion in market value. Is this any way to grow the economy? Growth depends on investment. A policy that clearly reduces return on investment can only discourage investors.

> Protectionism and red tape are pushing Brazil off a competitiveness cliff.

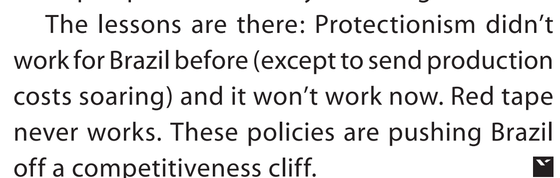
Agriculture and manufacturing are both desperate to get their goods to market more cheaply so they can compete with countries that have decent roads and ports. But instead of investing in infrastructure, the administration has been giving tax incentives for consumption—which may help the auto industry, at the cost of crippling the rest of the economy. Local content rules prevent companies like Petrobras from buying the best equipment and expertise from abroad. Not exactly a recipe for competitiveness. Or, for that matter, a model of sound management.

The government's social policy of transfers and subsidies to low-income households limits the amount of money the government has available to invest in infrastructure, and unquestionably its minimum wage and pension decisions have been decidedly generous—some might say profligate. It's great that 35 million more Brazilians are now considered middle class—but the new middle class would probably appreciate an economic policy that helped them stay there rather than sliding back again.

Brazil desperately needs higher productivity. That depends on a facilitative business environment, skilled labor, and innovation. Instead, according to the World Bank Doing Business indicators, Brazil has regressed two points, to 130th out of 150 countries. In other words, it's getting harder, not easier, to do business in Brazil.

Innovation, which in turn often depends on skilled labor, can be a powerful way to increase productivity and cut costs. Take General Motors in the U.S. as an example: In the 1990s GE outsourced is production of appliances to China in the 1990s. In the last 10 years, it's been bringing production back to the U.S. Today, GE does US$5 billion; 55% comes from its U.S. factories and by the end of 2014 that will be 75%. How can US workers possibly compete with the low-cost Chinese? The answer is innovation. GE put together teams of design and manufacturing engineers, line workers, and sales and marketing staff to redesign both products and assembly lines. The result was spectacular: made in China, its Geo Spring Water Heater costs US$1,599; made in the US, it costs US$1,299.

Meanwhile, Mexico is making it easy for companies like Embraer to invest there. There's a reason it will soon take over from Brazil as the most prosperous economy in the region.



The lessons are there: Protectionism didn't work for Brazil before (except to send production costs soaring) and it won't work now. Red tape never works. These policies are pushing Brazil off a competitiveness cliff.