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Opportunities for Canadian  
investment in Brazil  
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# OPPORTUNITIES FOR CANADIAN INVESTMENT IN BRAZIL

## Background

Canadian firms have had a long history of investing in Brazil. Strong links were forged between Canada and Brazil when the first Canadian businessmen came to Brazil in 1889 to develop concessions granted for the development of electricity, electric street cars, a telephone system and gas and water utilities in Rio de Janeiro and São Paulo. Before World War I, Canada competed for the first position as top foreign investor with the United Kingdom and the United States. Although Canada's profile has diminished since 1979 with the sale of Brascan's utility operations, Canadian investment in Brazil has grown and expanded into various sectors of the economy including the mining and chemical sectors, and in 1994, Canadian direct investment amounted to 4% of total foreign investments in Brazil.

In 1994, Canada ranked **seventh** among the top ten foreign investors in Brazil with over US\$2.2 billion in accumulated investments (see table 1). Of this, 23% was in the chemical sector and 16% in the electric and electronic equipment sector. Other important sectors included mining and metallurgy and representatives of consortia (see table 3). Since 1990, Canadian investment has exceeded US\$2 billion reaching a high of US\$2.2 billion in 1994 (see table 2).

Furthermore, with recent changes in government policies concerning foreign investment and privatization, notably in mining and communications, Canadian investors have shown a renewed interest in doing business in Brazil. In the mining sector, many well known Canadian companies such as Barrick Gold Corporation, Cominco Ltd., Inco Ltd. and Alcan

have a foothold. Prime Minister Jean Chretien's visit to Brazil in early 1995, accompanied by a large delegation of Canadian business persons, reflects Canada's increased interest in intensifying relations with Brazil and Latin America in general. Since 1984, Canada has had a Double Taxation Agreement with Brazil. Canadian investment has been diverse, many well known and respected Canadian companies are represented and with the right investment climate, many more may expand their holdings in Brazil.

## Overall Investment Climate

The Real Plan has so far removed the problem of hyperinflation in the economy. Since its implementation in July 1994, it is now formally recognized abroad as a successful initiative. It has managed to bring down inflation rates from 50% a month to somewhere between 1 and 2% monthly. Forecasts for 1996 are that consumption should remain stable and that the presence of foreign products will offer competition to Brazilian goods, reduce prices and further help incorporate low income families into the consumer economy. Rising consumption should be met with goods supplied by an expanded private sector. Predicted growth rates for GDP are 2.5 to 3% for 1996.

New government policies are geared to increase medium and long-term foreign investment. This past year the Congress has approved several constitutional amendments (such as those which ended the discrimination between Brazilian and foreign companies, and began opening the telecommunication, energy, transportation and mining sectors to private investment). Over the past few years, the Central Bank improved

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regulations for foreign investment by issuing a series of directives with the purpose of disclosing the rules which regulate the registration of foreign investment in Brazil.

There is a great need for effective infrastructure as a prerequisite for globalized industrial production which Brazil hopes to achieve. As a consequence of the financial crisis in the 80's, deterioration in transportation, energy and telecommunications sectors is now evident. As the government continues to struggle with the public deficit, funding for the necessary development in infrastructure is not readily available, and thus the government is counting on private-sector involvement, as seen in the recent privatization plans for the telecommunications and energy sectors.

Furthermore, with recent trade agreements and the trend towards regional economic integration, Brazil can serve as a gateway into Latin America as a whole. Mercosul, a common market created in 1991 covering Brazil, Argentina, Paraguay and Uruguay, has enhanced the growth prospects of the region and should lead to considerably more predictability in trade policies of all four countries. In 1995, Mercosul also advanced negotiations for the establishment of free trade zones with Bolivia and Chile and further negotiations to include other Latin American countries such as Venezuela, Ecuador and Peru are scheduled for 1996. The creation of this single large market warrants a serious look by business interest, particularly in the area of direct investments. Brazil, due to its size and importance in Latin America (i.e.: Brazil accounts for 62% of Mercosul's GNP and 71% and 66% of its agricultural and industrial production, respectively) provides an opportunity to penetrate this market.

Direct foreign investments in Brazil for 1995 reached US\$3.2 billion, one billion more than

for 1994. Most are long-term investments which demonstrate renewed interest in Brazil by the international business community. Minister of Industry, Commerce and Tourism Dorothea Werneck stated that "investment intentions" announced to the end of 1995, were in the order of \$27 billion up to 1999 and included multinational corporation projects in five different areas: automotive, metallurgy, petrochemicals, pharmaceutical and foodstuffs processing. German corporations have indicated that they may invest \$6 billion in Brazil up to the year 2000, and French, Japanese and British investors are not far behind. Central Bank president, Gustavo Loyola has declared Brazil the "new frontier" for financial, commercial and technological investment.

Lehman Brothers recently reported that Brazil is considered the best option for investment in the Latin American shareholding market, as investments made within the context of the Real Plan should show solid gains in profits for 1996. Mergers and acquisitions also offer great opportunity for investment as the numbers for 1996 are expected to be high. In 1995, the total volume of mergers and acquisitions increased 300%, from US\$1.045 billion in 1994 to US\$4.183 billion. Most investment banks believe that the market should grow another 50% to 100% this year, especially among favorite sectors like food products, autoparts, consumer goods and electronic goods. Future expansion of Canadian investments in Brazil, including participation in joint ventures and privatization exercises, is not only possible but, in some cases, may be inevitable - if Canadian companies want to maintain their positions in certain segments of the Brazilian market. This is particularly true in key areas of major opportunity, such as telecommunications and energy.

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wire lines.  
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over \$2 billion in the medium term.  
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nearly twice that which was planned to be

1996, he forecast investments of \$8 billion.

eight years will amount to R\$275 billion. For

program for the Telebrasil System in the next

Communications announced that the investment

communications sector. The Minister of

major investment program in the

in 1995, the federal government launched a

significant business opportunities in Brazil. Late

The telecommunication sector offers the most

#### Telecommunications

#### Specific Opportunities

stabilization plan.  
already implemented in order to sustain the Real  
support for these measures and for those policies  
real possibility of issuing important political  
number of state companies. As well, it faces the  
and federal governments and privatizing a  
system, by balancing the finances of the state  
imbalance by reorienting the social welfare  
The government will need to overcome fiscal  
serious public debt problems are not yet in place.  
that the necessary fiscal reforms to the country's  
The risk of investing in Brazil at this time, is

of transmission lines by the year 2002 offers  
construction of an additional 600 kilometers  
only 4 percent. Brazil's plan for the  
current private sector participation is small at  
privatization in this sector in Brazil, although  
aptly. There appears to be little resistance to  
The demand for power and electricity is growing

#### Energy

\$200 million monthly.

with television, representing a potential of 1.2

2000. São Paulo alone has 6 million residences

have 30% of Brazilian homes cabled by the year

expand their operations. The industry goal is to

and TVA are investing US\$250 million to

Brasileira cable TV operators, NET, Multicanal,

markets in the world. The three largest

America and among the largest unexploited

TV is considered to be the largest in Latin

of around R\$110 million.

300,000 terminals. This will mean investments

contracted. Telemig will issue calls for a total of

over and above the 450,000 terminals already

Telesp will issue calls for 140,000 new terminals

450,000 new terminals and related systems.

they will issue calls for bids for a total of

company) have announced that, early in 1996,

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Both Telesp (state of São Paulo phone company)

planned telephone expansion unfolds.  
12% over the next three years, as Telesp's  
investment in telephone is expected to grow by  
in the world and eighth in Latin America.  
telephones per 100 inhabitants, Brazil ranks 39th  
in telephone, with a density of only nine

through Locasat). Globo Group, and  
Odebrecht have already announced their  
intention to invest.

intention to invest.



The risk of investing in Brazil at this time, is that the necessary fiscal reforms to the country's serious public debt problem are not yet in place. The government will need to overcome fiscal imbalance by restructuring the social welfare system, by balancing the finances of the state and federal governments and privatizing a number of state companies. As well, it faces the real possibility of losing important political support for these measures and for those policies already implemented in order to sustain the Real stabilization plan.

### Specific Opportunities

#### **Telecommunications**

The telecommunication sector offers the most significant business opportunities in Brazil. Late in 1995, the federal government launched a major investment program in the communications sector. The Minister of Communications announced that the investment program for the Telebrás System in the next eight years will amount to R\$75 billion. For 1996, he foresaw investments of \$8 billion, nearly twice that which was planned to be invested in 1995. He also announced an aggressive program to attract private sector involvement.

According to a study by the Brazilian Institute for the Development of the Telecommunications Sector, *cellular service* (Band B) should attract over \$5 billion in the medium term.

*Mobile telephone service* companies are becoming fierce competitors to the traditional data line providers. The key behind their success is that large numbers of phone lines can be set up faster than installing traditional copper wire lines.

In the *satellite* segment, Itamarati Group

(through LocaSat), Globo Group, and Odebrecht have already announced their intention to invest.

In *telephony*, with a density of only nine telephones per 100 inhabitants, Brazil ranks 39th in the world and eighth in Latin America. Investment in telephony is expected to grow by 12% over the next three years, as Telebrás's planned telephone expansion unfolds.

Both Telesp (state of São Paulo phone company) and Telemig (state of Minas Gerais phone company) have announced that, early in 1996, they will issue calls for bids for a total of 440,000 new terminals and related systems. Telesp will issue calls for 140,000 new terminals over and above the 440,000 terminals already contracted. Telemig will issue calls for a total of 300,000 terminals. This will mean investments of around R\$210 million.

Brazil's market potential for *cable TV* and *pay TV* is considered to be the largest in Latin America and among the largest unexploited markets in the world. The three largest Brazilian cable TV operators, NET, Multicanal, and TVA are investing US\$200 million to expand their operations. The industry goal is to have 30% of Brazilian homes cabled by the year 2000. São Paulo alone has 6 million residences with televisions, representing a potential of 1.2 million subscribers and country-wide revenue of \$200 million monthly.

#### **Energy**

The demand for power and electricity is growing rapidly. There appears to be little resistance to privatization in this sector in Brazil, although current private sector participation is small at only 4 percent. Brazil's plan for the construction of an additional 60 000 kilometres of transmission lines by the year 2002 offers

investors are needed to fund the Ferroviária railroad which will connect the North and Central West to the ports of Santos and Soledade. The first phase of the project is estimated at \$1.2 billion.

The first segment of the railway system, the West subsystem (Linha Oeste do Sul - São Paulo) was auctioned on March 2, 1986. The price was R\$23 million, in cash, but financed over a 30 year period.

Work was stopped during the previous administration. Japan's Eximbank is also expected to grant a loan for São Paulo's subway system. The National Development Bank (BNDES) plans to release more than R\$1 billion so that São Paulo state government can proceed with construction work on the São Paulo subway system.

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Transportation is probably the only way out of the crisis of the transportation sector. Neither the federal nor the state governments can pay for urgent repairs, let alone the expansion of highway networks. Something similar will no doubt happen with the railways, whose finances are in even worse shape than the highways and ports. Port managers were recently identified by a senior Brazilian economist as one of the main impediments to further increases in Brazilian export competitiveness.

These changes now allow companies continued with foreign capital to prospect for minerals and to mine in Brazil. The immediate impact has been a spate of visits from foreign companies. In the last six months, fifty large corporations have arrived to survey the market and 30 small

mining. Brazil is one of the five most important mineral producers in the world although it remains largely unexplored with less than 20% of the country mapped in detail. After the 1988 constitution, investments in the sector dropped from US\$160 million to US\$27 million per year. The government hopes to change this picture with the recent changes made to the Brazilian mining legislation.

The arrival of natural gas from Bolivia or Argentina or both will spur enormous investments in gas-fired co-generation projects. All indications point to southern Brazil being electricity-deficient in the coming 2 or 3 years.

The government will auction 60% of voting stock in Eletrobrás in the second quarter of 1986, the Rio de Janeiro state power utility, owned by Eletrobrás. The auction calls for selling for cash at least 21% of Eletrobrás. No minimum price was disclosed, but it is estimated at R\$1.2 billion for the 21% portion.

Total investment is estimated at R\$22 billion and 9 thermoelectric plants by 1992. The plants are capable of producing 23,700 megawatts. The government plans to sell 35 hydroelectric generation, transmission and distribution of electric energy. have constitutional impediments, including the participation in all public services which do not concessions of public services to the private excellent opportunities. The bill which regulates





excellent opportunities. The bill which regulates concessions of public services to the private sector has been approved, allowing their participation in all public services which do not have constitutional impediments, including the generation, transmission and distribution of electric energy.

The government plans to sell 35 *hydroelectric* and 9 *thermoelectric plants* by 1999. The plants are capable of producing 23,700 megawatts. Total investment is estimated at R\$22 billion.

The government will auction 60% of voting stock in Light in the second quarter of 1996, the Rio de Janeiro state power utility, owned by Eletrobrás. The auction calls for selling for cash at least 51% of Light. No minimum price was disclosed, but it is estimated at R\$1.2 billion for the 51% portion.

The arrival of *natural gas* from Bolivia or Argentina, or both, will spur enormous investments in gas-fired co-generation projects as all indications point to southern Brazil being electricity-deficient in the coming 2 or 3 years.

### **Mining**

Brazil is one of the five most important mineral producers in the world although it remains largely unexplored with less than 20% of the country mapped in detail. After the 1988 constitution, investments in the sector dropped from US\$160 million to US\$47 million per year. The government hopes to change this picture with the recent changes made to the Brazilian mining legislation.

These changes now allow companies constituted with foreign capital to prospect for minerals and to mine in Brazil. The immediate impact has been a spate of visits from foreign companies. In the last six months, fifty large corporations have arrived to survey the market and 30 small

companies are exploring mines in several areas of the country. Canadian companies are and have been some of the first to invest, with gold mining attracting companies such as TVX Gold, Barrick Gold (has been installed in Brazil since Dec 95), Echo Bay and Placer Dome. It is expected that overall foreign investment will total US\$ 1 billion by the end of 1996.

### **Transportation**

Privatization is probably the only way out of the crisis of the transportation sector. Neither the federal nor the state governments can pay for urgent repairs, let alone the expansion of highway networks. Something similar will no doubt happen with the railways, whose finances are in even worse shape than the highways and ports. Port charges were recently identified by a senior Brazilian economist as one of the main impediments to further increases in Brazilian export competitiveness.

The National Development Bank (BNDES) plans to release more than R\$1 billion so that São Paulo state government can proceed with construction work on the São Paulo subway system. Work was stopped during the previous state administration. Japan's Eximbank is also expected to grant a loan for São Paulo's subway.

The first segment of the railway system, the West subsystem (Mato Grosso do Sul - São Paulo) was auctioned on March 5, 1996. The price was R\$53 million, in cash, but financed over a 30 years.

Investors are needed to fund the Ferronorte railroad which will connect the North and Central West to the ports of Santos and Sepetiba. The first phase of the project is estimated at \$1.2 billion.





### **Automotive Parts**

This sector promises great opportunities for mergers and acquisitions in 1996. With changes to the industrial process of assembly factories and the increase in international competition, small specialized companies will merge with each other in order to provide a set of components to the assembly factories in place of individual parts.

### **Electronic Goods**

Subject to strong international competition, Brazilian companies will be looking for foreign partners in order to invest in technology and thus compete with the new wave of imports.

### **Food and Consumer Products**

The acquisition of food industry companies has increased over the last five years, particularly in 1995. With the increase in the purchasing power of the lower income population, companies within the food and consumer sectors must now invest to meet the new demand and to compete with imports.

### **Malls**

Brazil is considered the fifth-largest shopping mall market in the world, approaching a total size of US\$5.5 billion. Economic stabilization and the burgeoning consumer market is opening up major opportunities for firms interested in investing in factory outlet malls, strip malls, and

sector-specific retail chains. In the last two decades, the number of shopping centres has jumped from 12 to 104 and is expected to increase by 10 percent per year through the rest of the decade.

### **Plastics**

Since 1991, the Brazilian market for polyethylene terephthalate (PET) packages has been growing even though Brazilian prices are substantially higher than in the U.S., Asia or Europe. High prices are attributed to low production levels.

### **Insurance**

With changes in Brazil's social welfare system, the insurance market should re-arrange itself to accommodate foreign participation. It is expected that Japan and Germany will participate this year by buying into private retirement and life insurance.

### **Other**

Other areas of significant growth potential are forestry, private health care, retailing, agriculture. Sectors to be watched: auto parts production, construction, printing and packaging, infrastructure (ports, roads, rail) and banking.





## FOREIGN AND CANADIAN INVESTMENTS AND RE-INVESTMENTS IN BRAZIL

**Table 1**  
**TOP TEN FOREIGN INVESTMENTS AND RE-INVESTMENTS IN BRAZIL**

Country of Company	Current-cost basis (US\$ billions)	Current-cost basis (%)	Historic-cost basis (US\$ billions)	Historic-cost basis (US\$ billions) updated according to US consumer price index
United States	18.388	32.5	18.282	32.078
Germany	6.315	11.2	4.517	9.219
United Kingdom	5.107	9.0	5.342	8.540
Japan	4.161	7.4	3.447	7.188
Switzerland	3.331	5.9	2.292	5.674
France	2.388	4.2	2.288	4.356
<b>Canada</b>	<b>2.210</b>	<b>3.9</b>	<b>2.053</b>	<b>4.738</b>
Holland	1.701	3.0	1.487	2.502
Italy	1.603	2.8	1.588	2.626
Others	11.345	20.1	11.654	20.340
<b>TOTAL</b>	<b>56.549</b>	<b>100.00</b>	<b>52.950</b>	<b>97.261</b>

Obs.: Investments made from Canada only (does not include Canadian investments through third countries).

Source: Central Bank Dec 1994

Chemical	26.99
Electrical/Electronic Equipment	15.76
Construction, Repairs and Participation	14.70
Mining and Metallurgy	13.00
Other	10.50
Mechanical	6.40
Textiles	5.80
Transport	5.10
Automotive	2.10
Non-Ferrous Metal	1.50
Other	1.50
Food, Agriculture	1.00
Other	1.00
<b>TOTAL</b>	<b>100.00</b>



**Table 2**  
**CANADIAN INVESTMENTS AND RE-INVESTMENTS IN BRAZIL**

December of	Cumulative Investment in US\$ billions
1986	1.424
1987	1.456
1988	1.651
1989	1.863
1990	2.223
1991	2.131
1992	2.210
1993	2.177
1994	2.210

Source: Central Bank Dec 1994  
Current-cost basis

**Table 3**  
**CANADIAN INVESTMENTS BY SECTOR**

Sector	% of Cumulative Investment (1994)
Chemical	26.00
Electric/Electronic Equipment	15.70
Consortium Representatives and Participation	14.70
Mining and Metallurgy	13.00
Others	10.50
Mechanical	6.40
Portfolios	6.00
Tourism	3.10
Autoparts	2.00
Medical/Pharmaceutical	1.50
Textiles	.50
Other Activities	.40
Transportation	.15
Banking	.07
Agribusiness	.01
<b>TOTAL</b>	<b>100.00</b>

Source: Banco Central FIRCE/CONAP Dec 1994 (Current-cost basis)

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