Since the late 1970s Brazilian industry has not had such a favorable situation for investment as today. The moment, however, comes with warning lights. The big question: Will the current course at last bring about structural changes that will give Brazil sustainable growth and a bigger and better position in world trade?

The share of industry in gross domestic product (GDP) peaked at the end of the “economic miracle” in the 1980s, when the policy of import substitution raised the sector’s share to 37% of GDP. By 2009 it had fallen to 25%, according to the Brazilian Institute of Geography and Statistics (IBGE). With industry now maturing, it is time for more difficult choices. Both corporations and government need to focus on technological and institutional development to bring about the desired quality leap.

There are several complications. Apart from changes in world trade, especially with China affecting both demand and supply, some domestic factors could slow progress. There is a duality: although the profile of GDP in Brazil is closer to that of the developed countries — services already account for 68% of GDP — the profile for exported goods is more like that of developing economies, with emphasis on primary products and with manufacturing declining.

Unparalleled fall

The share of manufactured goods in total Brazilian exports has declined since 2007, a phenomenon that was accelerated last year with the plunge in global demand. “Even after taking into account the effects of the crisis, our exports with higher added value are likely to continue decreasing because we are losing competitiveness in this area,” says Miguel Jorge, Minister of Development, Industry and Foreign Trade. “Another significant factor is the intensification of global competition,” he adds. “Many players have adopted more aggressive actions to promote their exports in the last 10 years.”
And the recovery of the US and European economies is still sluggish.

The chances are remote that much can be done about the appreciated exchange rate, one of the main factors that make Brazilian goods less competitive globally. The cost of money also remains high, though that does not prevent the extension of credit for consumption, says Renato Baumann, director of the Brazil office of the United Nations Economic Commission for Latin America and the Caribbean. He says, “The combination of these elements generates both positive and negative effects. On the one hand, it helps to sustain domestic demand, but on the other it is a model based on consumption rather than investment, especially in the public sector.” A radical change in policy is ruled out by the major candidates to succeed President Luiz Inacio Lula da Silva in the October elections.

For industry the biggest challenge is external competitiveness; the domestic market is doing very well. The problem of falling exports is heightened by the need to improve the quality of manufacturing to ensure productivity in market niches. This requires clear regulations and technological innovation, among other advances. “Animal spirits abound in businesses, but typical problems persist, like the ‘Brazil cost’ reflected in the excessive tax burden and inadequate infrastructure,” said Jose Augusto Coelho Fernandes, executive director of the National Confederation of Industry (CNI).

**Search for identity**

With what identity will the country expand its presence in world trade? “India has established itself in the international market as a software producer and exporter of talent. But what differentiates Brazil?” asks Lia Valls Pereira, coordinator of the Center for the External Sector of the Brazilian Institute of Economics (IBRE). Although Brazil is at the forefront of clean energy...
Brazil’s manufacturing share in world exports has been virtually stagnant: it was 0.7% in 1980 and 0.8% in 2008.

For a number of years, Mexico has attracted large amounts of foreign funds for production processes known as “maquillas” — assembly lines of manufacturing predominantly for export, with all the components imported. “Mexico’s participation in world exports of manufactures grew, but the share of industry in GDP has not, because industry’s value-added declined,” Valls Pereira says. To avoid this in Brazil, past governments established minimum levels of national inputs for various industries.

What about Brazil’s role as a world breadbasket? There is no doubt that selling commodities is important because it brings foreign exchange, but data from the World Trade Organization already show a decline in the share of agriculture in the world market, says Valls. Meanwhile, the share of processed foods has increased worldwide. Lately Brazil has been doing better in processed foods.

Like other diversified economies, Brazil has some advanced technology sectors but others are far behind. “In 60 years of industrialization, the country has succeeded in creating a production system with many virtues, but … we depend too much on commodities, although producers have evolved in recent years,” says Glauco Arbix, coordinator of the Innovation Observatory of the Institute of Advanced Studies, University of São Paulo.
Paulo. “In the past,” he says, “cattle went overseas standing up on ships. Currently, Brazil as the largest exporter of beef and pork has sophisticated systems for slaughtering and distribution. But commodities are still limiting our economy.”

**Differences**

Ricardo Sennes, partner at Foresight Consulting International, has questions about the decline of manufacturing exports. “When we look at sectors individually, significant differences can be detected. There is a direct correlation between a corporation’s external competitiveness and a high standard of innovation in processes and products. This trend is growing and those who stay out of it suffer badly,” he explains. The 10 Brazilian companies that registered more patents in Brazil and abroad in recent years have an international presence. “Some niches are doing well,” Sennes says.

The decline in Brazil’s manufacturing exports is different depending on the export market. Brazil’s exports to South America are predominantly those with medium and high technological density, such as automobiles and textiles, while exports to the US and European countries have less technology content. Brazilian manufacturing exports to Europe are about 30% of total exports. Technological content and value-added plunge in what Brazil sends to Asia. The share of manufacturing in exports to China is close to zero — 68% are iron ore and soybeans, and the rest is orange juice and meats.

This phenomenon affects not only Brazilian products; China crowds out other countries in various markets, says Minister Jorge. In absolute numbers, Brazil’s sales to the US grew steadily in the last 10 years, except 2009. But, he explains, “In 2010 we started to regain ground: in the first half, exports to the US rose 24% over the same period last year. But the relative share declined because exporters and government made a huge and successful effort to diversify the countries of destination of our foreign sales.”

**International integration**

The share of manufactures in Brazilian exports increased from 45% in 1980 to 59% in 2000, then began to decline steadily. In 2009 it was 44% and from January to June 2010 it was 40%. The share of Brazil’s manufacturing in world exports has long been stagnant: it was 0.7% in 1980 and 0.8% in 2008, according to the Foundation Center for Study of Foreign Trade.

For Baumann the question is not whether the increasing share of commodities in exports is good or bad for Brazil, but rather how to have
more efficient international integration. “There’s nothing wrong with being rich in natural resources. Nordic countries generated wealth by selling natural resources and Latin America can find a good way to take advantage of its natural resources, too,” he said.  

David Kupfer, professor of economics at the Federal University of Rio de Janeiro, expands on Baumann’s comments: “One of the major transformations of Brazil in the next decade will be integration into the global economy. Progress can occur not only with integrating global production chains, but also South American integration of regional production chains.”

The internationalization of Brazilian companies should continue since so far it has occurred almost exclusively in just a few sectors: “It’s one thing for the Vale Corporation to have a presence around the world. It’s another for all export industries to achieve global presence.”

According to the CNI, the increasing share of commodities in exports must be examined carefully. If Brazil finds markets for products at exceptional prices, it is natural that the export profile changes. “This is a spontaneous movement, and healthy,” says Robson Braga, CNI president. “The concern is when we are faced with a decline in manufacturing exports because of internal dysfunctions or a highly appreciated exchange rate. That’s why industry calls attention to the low level of savings, the excessive expansion of current government spending, high interest rates, and lack of investment in infrastructure.”

**China’s factor**

The problem is not just that the share of Brazil’s manufactures in world exports has not increased. A real issue is the loss in manufacturing sales to a single competitor, China. China produces more than half of world production of crude steel and is moving into rolled and other sophisticated

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**BRAZILIAN EXPORTS BY TYPE**

<table>
<thead>
<tr>
<th>US$ billion FOB</th>
<th>Share of total exports (%)</th>
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<tbody>
<tr>
<td></td>
<td>Commodity</td>
</tr>
<tr>
<td>1964</td>
<td>1.4</td>
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<tr>
<td>1970</td>
<td>2.7</td>
</tr>
<tr>
<td>1980</td>
<td>20.1</td>
</tr>
<tr>
<td>1990</td>
<td>31.4</td>
</tr>
<tr>
<td>2000</td>
<td>55.0</td>
</tr>
<tr>
<td>2001</td>
<td>58.2</td>
</tr>
<tr>
<td>2002</td>
<td>60.4</td>
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<tr>
<td>2003</td>
<td>73.0</td>
</tr>
<tr>
<td>2004</td>
<td>96.5</td>
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<tr>
<td>2005</td>
<td>118.3</td>
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<tr>
<td>2006</td>
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<tr>
<td>2008</td>
<td>197.9</td>
</tr>
<tr>
<td>2009</td>
<td>153.0</td>
</tr>
<tr>
<td>Jan.–Jul. 2010</td>
<td>89.2</td>
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</table>

Source: Ministry of Development, Industry and Foreign Trade.
steel products. “China is a fact that cannot be ignored,” says Valls Pereira.

Brazil’s share in total imports to the US has had a slight recovery, but the Chinese share has advanced much more, says Braga. “Only in two sectors of manufactured goods with greater technological content are Brazilian exports higher than Chinese: aircraft and other aerial devices, and weapons and ammunition. But in the case of aircraft Brazilian participation has been declining, while China’s has increased slightly,” he says.

**Identity crisis**

Just what is Brazil lacking? “We are the largest exporter of orange juice, but American consumers do not know that when they buy our juice. There is a need to create a Brazil brand. For soybeans it may be dispensable, but for machines and shoes it is essential,” stresses Valls Pereira. Another step is to facilitate the access of small industries to foreign markets, and that will require official incentives. There are countless federal and state programs to encourage exports, but the results are questionable. She comments that, “Unfortunately, there are many ideas or programs, but these initiatives have not been assessed seriously.” Excessive bureaucracy still prevents companies from enjoying the benefits of such programs.

Manufactured exports had a huge boost in Brazil in the 1970s and 1980s, when the government subsidized them under the Second National Development Plan, and the policy of import substitution was observed. Valls Pereira makes it clear that it is necessary not to repeat the past but to learn from it to implement effective programs to promote exports.

**Initiatives**

A long-term industrial policy could help. Some programs have been reactive rather than strategic. The acting president of the CNI, Robson Braga, praises the Productive Development Policy, announced in 2008, for being focused on annual actions to simplify and reduce the term of administrative procedures. Braga says, “The central problem is that the most important issues for the sector require an extraordinary effort of coordination between government agencies and government branches.

Deindustrialization has occurred elsewhere in the world and usually goes together with increased exports of services. ... Brazil has established itself as an exporter of services and should bet on service exports to offset the decline of manufacturing exports.

Taxation, labor relations, and legal and regulatory frameworks must be adequate to provide vital business competitiveness.”

Minister Jorge highlights the resumption of the national debate on the need for an industrial policy with the launch of the PDP, after more than two decades without explicit policies for industrial development.
He said it is “a deep extension” of the 2004 Industrial, Technological and Foreign Trade Act, but there are still basic steps, qualification of a skilled workforce and tax reform, that “should be the focus of the next federal government, state governments, and Congress.” In his opinion, “The world standard is no export tax of any kind, direct or indirect.”

Braga says that CNI seeks to demonstrate that “having industry at the center of economic strategy is a way to grow more and better because it is the main source of technical progress, innovation, and productivity. But this does not require protection and encouragement of inefficiency. What we want is a level playing field: adequate infrastructure, good quality education, and mobilization of policy tools used by our competitors.”

What’s next?
Can Brazil become the fifth-largest global economic power in 2016 with industry’s share of GDP at around 25% and exporting low-value-added commodities? “Why not?” asks Wagner Iglecias, professor of the University of São Paulo. “Do we necessarily have to tread the same path as developed countries 50 years ago? Is it not possible for a country to consolidate an economy that is at the same time rural and post-industrial, based on services and other assets?”

Brazil is competitive in a number of agricultural products that are responsible for the trade balance surplus, and its presence in world markets is also affected by subsidies and import barriers imposed by rich nations, Iglecias notes. In his view, the main issue is whether in the medium and long term there will be demand and prices for these products. “The situation in Brazil, compared to some neighbors, is privileged. Mexico exports agricultural goods, manufactured goods, and services, but it has only one customer, the United States. Venezuela has several business partners around the world but offers only one product, oil,” he says. But Brazil has a diversified range of both export products and trading partners.

To Minister Jorge, the share of manufactures in exports is falling at a pace that should not affect the growth of the domestic economy. Moreover, Brazil is fully capable of making its industry more competitive and thus raising foreign sales of products with higher added value.

Sennes points out that deindustrialization has occurred elsewhere in the world and usually goes together with increased exports of services. “The higher a country’s GDP per capita, the greater the share of the service sector in its economy,” he adds. Brazil has established itself as an exporter of services — legal, engineering, infrastructure, design, information technology, and medical, among others — and should bet on service exports to offset the decline of manufacturing exports. “Of course industry still has an essential role in the strategic development of Brazil, but we need to think more broadly. Besides promoting the manufacturing industry, we should promote the Brazilian service industry,” he recommends.