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FEATURED Q&A

Are Brazil-U.S. Military Relations Experiencing Turbulence?

Q Brazil's Foreign Affairs ministry said March 1 that the U.S. Air Force's cancellation of a \$355 million contract for defense aircraft manufactured by Embraer was a surprise and does not help bilateral military relations between the two countries. The cancellation, which Air Force officials said was due to faulty documentation surrounding the contract, followed reports that Brazil is likely to choose France's Dassault instead of U.S.-based Boeing for a multi-billion-dollar contract for military aircraft. Have these developments affected military and business relations between the two countries? Will Brazilian President Dilma Rousseff's visit to Washington next month help improve bilateral relations? What will be the most important agenda items during her visit?

A Craig Kelly, member of the Advisor board and vice president of the Cohen Group in Washington: "Some press reports have suggested that the U.S. Air Force announcement could not have come at a worse time—with Deputy Secretary of State Bill Burns traveling in Brazil and President Rousseff about to visit Washington. Actually, those visits underscore the wide range of important issues that the United States and Brazil deal with cooperatively and pragmatically every day. Whether it's the global economy, trade, investment, agriculture, educational exchange, cooperation on science and tech-

nology, biofuels, combined efforts to combat racial discrimination, cultural programs or sports diplomacy—our countries enjoy an exhaustive record of coordination. That list includes important military-to-military ties, in the context of the U.S.-Brazil Defense Cooperation Agreement, which covers research and development, defense technology, peacekeeping operations, military education and training and defense-related commercial matters. As for the U.S. Air Force announcement, Brazil has made clear that it was surprised and

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Venezuela's Chávez to Return Home This Week After Surgery

President Hugo Chávez said in a television appearance Sunday that he plans to return to Venezuela this week. He has been in Cuba since undergoing surgery to remove a cancerous growth on Feb. 26. See story on page 2.

Photo: Venezolana de Televisión.

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NEWS BRIEFS

Authorities Find 167 Bodies in Mexican Cave

Mexican authorities said Saturday that they found the bodies of 167 people in a cave in the state of Chiapas, the Associated Press reported. Experts believe the remains are at least 50 years old and, in a statement, said that there were no visible signs of violence. Authorities said they will "not discard any line of investigation."

Telefônica Axes 1,500 Employees After Vivo Merger

Telefônica Brasil will dismiss 1,500 employees in the states of Rio de Janeiro and São Paulo, Bloomberg News reported Saturday. Telefônica Brasil, which had about 19,000 workers, merged with **Vivo Participações** at the end of last year. According to the Sindicato dos Trabalhadores em Telecomunicacoes no Estado de São Paulo union, the company had wanted to fire more staff.

Brazil's Government Extends 'IOF' Tax to Longer-Term Loans

The government of Brazilian President Dilma Rousseff has extended the country's IOF financial operations tax to foreign loans of as long as five years, Dow Jones reported Friday, citing a government decree. Previously, the 6 percent tax was assessed only on loans of three years or less. The expansion of the tax is part of Brazil's efforts to stem gains in the country's rallying currency. Brazil's government has had growing concerns that increasing amounts of cash will flow into the country's economy due to the country's high interest rates. Finance Minister Guido Mantega has said Brazil is poised to take additional actions to curb the appreciation of the country's currency.

Political News

Chávez Planning Return to Venezuela This Week Following Cancer Surgery

Venezuelan President Hugo Chávez, who is recovering from having cancer surgery on Feb. 26 in Cuba, said Sunday in a televised appearance that he plans to return home this week, the Associated Press reported. Chávez, wearing a track suit bearing the yellow, blue and red of Venezuela's flag, also said he would undergo radiation treatment in coming weeks. Chávez said that after his latest surgery, to remove a 2-centimeter growth from his pelvic region, he now has "completely normal vital parameters, a good

“We have one single plan ...
Hugo Chávez is our candidate!”

— *Justice Minister Tareck El Aissami*

general state of health, without any complication of any kind." The growth was removed from the same place in his pelvic region where surgeons removed a larger tumor last June. Chávez, who has never publicly identified the type of cancer he is fighting, paraphrased philosopher Friedrich Nietzsche, saying his struggle against cancer is "my longest and steepest hike." Chávez's television appearance, which was similar to his regular weekend television program, seemed designed to project an image of the president at work as usual. He talked about government projects, ranging from public housing to subway expansion initiatives and also briefly sang. A day earlier, thousands of Chávez supporters gathered in demonstrations across Venezuela to show support for the president. In Caracas and other cities, demonstrators waved flags and pictures of Chávez, beat drums and danced in the streets. Other leaders of Chávez's socialist party spoke to the crowds, expressing optimism about Chávez's health as he seeks re-election in

the country's October presidential election. "We have one single plan ... Hugo Chávez is our candidate!" Justice Minister Tareck El Aissami said at a rally in Trujillo state.

Economic News

Brazil Seeking Quota to Restrict Mexican Auto Imports

Brazil's government wants Mexico to cut the number of autos it exports to Brazil by more than a third to approximately \$1.4 billion annually, Reuters reported Friday. The proposal for a new export quota comes as Brazil is trying to protect its auto industry amid a strong Brazilian real. In a March 8 letter, Brazil's government said the quota was equal to the average annual value of Mexico's auto exports to Brazil over the past three years. Putting the restriction in place would amount to a 40 percent reduction in the number of autos Mexico exported to Brazil last year. An official of the Mexican government told Reuters that if a quota is to be put in place, it should be based on the latest export figures, not an average over three years. "What we say is that it needs to start on the basis of trade flows today, and that we can establish mechanisms to avoid a sudden increase in exports," said the official, who asked not to be named. Last year, auto exports from Mexico to Brazil reached \$2.4 billion, said the official. That was an increase of approximately 70 percent from 2010, when exports totaled just less than \$1.4 billion. In its letter to Mexican Foreign Minister Patricia Espinosa and Economy Minister Bruno Ferrari, Brazil's government also said Mexico should move toward more liberal trade in heavy vehicles, a move which could benefit Brazil's vehicle exports to Mexico. Brazil had a \$1.7 billion trade deficit in automotive trade with Mexico last year, more than twice the previous year's deficit, according to Brazilian figures.



Espinosa

File Photo: Mexican Government.

Company News

YPF Must Reinvest in Production, Halt Dividend: Argentine Official

Argentina's YPF must use its profits to reinvest in production and suspend payment of dividends until the oil producer is able to reverse declining output, Roberto Baratta, the government's representative on YPF's board told Reuters Friday. "I think we are looking at a long period in which the profits will be reinvested in the country," said Baratta. Argentine authorities have been putting pressure on YPF, a unit of Spain's Repsol, to increase production as energy demand surges amid the country's growing economy. The cost of imported fuel has also been rising, crimping government finances. Argentina's government currently has an antitrust investigation against YPF to probe allegations that it limits fuel supplies in order to drive up prices. The government has also accused the company of overcharging for diesel fuel. Last year, YPF reported a net profit of 5.30 billion pesos (\$1.23 billion). It also has among the industry's highest

“I think we are looking at a long period in which the profits will be reinvested in the country.”

— Roberto Baratta

dividend as it distributed 80 to 90 percent of its profits to shareholders. "There are studies that show companies in the energy sector generally distribute 20 to 30 percent of their profits as dividends, while the rest go toward reinvestment," Baratta told Reuters. The company's production declined last year by 8.5 percent, to 495,000 barrels of oil equivalent per day. Officials at YPF declined to respond to Baratta's comments to Reuters. [Editor's note: See related Q&A in the Feb. 27-March 2 [issue](#) of the Dialogue's weekly *Energy Advisor*.]

Featured Q&A

Continued from page 1

concerned. Since that time, the Air Force has underscored that the decision reflected an internal issue that is under investigation, and U.S. officials have signaled continued interest in the Brazilian bid. Moreover, Pentagon and State Department officials emphasized publicly and privately that this issue is completely separate from the Brazilian fighter competition. When President Rousseff visits Washington next month, we should expect an agenda rich in variety and depth, as befits a conversation between two of the world's largest economies. In a relationship this big and complex, there will always be differences—but one of the reasons for having these visits is to discuss those issues privately, in the context of the far more numerous issues that bring the two nations together."

A Rubens Barbosa, former ambassador of Brazil to the United States: "The U.S. Air Force's chief of staff, Gen. Norton Schwartz, said the cancellation was a shame, disappointing and could affect the institution's reputation. This is the second time that a contract awarded to Embraer in a U.S. public tender has been canceled due to political reasons. The timing of the announcement shows lack of coordination among different agencies. U.S. Deputy Secretary of State William Burns was in Brazil to discuss Dilma's visit to the United States, a Brazilian delegation was in Washington for a discussion with U.S. authorities in an effort to strengthen the bilateral relationship in the area of military cooperation and there is a pending Brazilian decision on the tender for the fighters (Boeing is well-placed). The cancellation is another example of the distance between rhetoric (interest in improving the defense relationship) and practice (cancellation of tenders, a U.S. veto of Embraer's deal to sell military aircraft to Venezuela in 2006 and barriers to transfer of technology). The reaction of the Brazilian government was moderate and

cautious ('doesn't help the deepening of defense cooperation'), as it should have been. No doors have been closed. The April presidential visit will foster the bilateral relationship leaving behind ideological prejudices of the Lula era. The most important items on the agenda seem to be energy (oil and renewable) and innovation cooperation. How the two countries' private sectors may take advantage of political support from Washington and Brasilia in these two areas is an open question."

A Peter Hakim, member of the Advisor board and president emeritus of the Inter-American Dialogue: "The U.S. Air Force's sudden and still largely unexplained cancellation of the Embraer contract on the eve of Dilma's first visit to the White House illustrates why Brazil remains distrustful of Washington and reluctant to pursue a closer relationship with the United States. No two countries talk more about the need for and potential benefits of a 'strategic partnership' and do less to establish the basis for one. Frequently, the United States treats Brazil as if it did not quite earn or measure up to the status it has achieved in world affairs. To be sure, Washington sees Brazil as the 'primus inter pares' when it comes to Latin America, but does not assign it anywhere near the global importance it does to China and India. It often seems that the United States considers Brazil an interloper when it comes to international politics. And Brazil often responds in kind. It seems intent on demonstrating its growing stature and influence by consistently flaunting its independence of the United States and, on many issues, showing off its opposition—even where bedrock U.S. interests are at stake. The growing mistrust between the two countries should not be surprising. Nor should the occasional tensions. Dilma's visit to Washington is unlikely to alter much, any more than Obama's visit to

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Brazil did a year ago. Both nations would benefit from a change in approach."

A **David Fleischer, emeritus professor at the University of Brasilia and editor of Brazil**

Focus: "The abrupt cancellation of the U.S. Air Force's \$355 million contract with Embraer and Sierra Nevada to supply 20 Super Tucano light-attack aircraft only reinforced suspicions by Brazilians that in this area of military contracts the United States 'can not be trusted.' These planes were to be constructed at Embraer's facilities in Florida and would have generated 1,200 U.S. jobs. Unfortunately, this procurement became the focus of a vociferous lobby launched by Kansas-based Hawker Beechcraft, which lost the contract to the Brazilian firm and filed a suit in federal court against the Air Force. These developments forced the Air Force to cancel the contract as a means of quashing this lawsuit and mobilizing a new procurement effort. Recently, high level U.S. government representatives (William Burns, Rose Gottemoeller and Thomas Countryman) took great pains to explain to their Brazilian counterparts that

Embraer is still a strong contender in the new procurement (which would be finalized in 2013, after the U.S. presidential election). Many in Brazil feel that the Air Force's action has weakened the chances of the Boeing F-18 Super Hornet being selected by Brazil in the multi-billion dollar procurement for 36 fighter planes (F-X2), and has strengthened the chances of the Rafale from France's Dassault of being selected. Boeing became so concerned that it sent a group of high-level executives to Brazil to reinforce its F-18 proposal. Brazil suspects that if the Boeing plane were selected, the United States would embargo (partially or totally) the transfer of technology for Brazil to manufacture this plane. Non-military business relations should not be affected by this episode. Surely, this controversy and Brazil's F-X2 procurement will be on the agenda during the Rousseff-Obama encounter on April 9. Other items, such as Iran's nuclear program, should also be included."

The Advisor welcomes reactions to the Q&A above. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.

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