



CNI proposals for the 2014 elections

Strategic Map
OF INDUSTRY 2013-2022
AN AGENDA FOR COMPETITIVENESS

 CNI PROPOSALS FOR THE
2014 Elections

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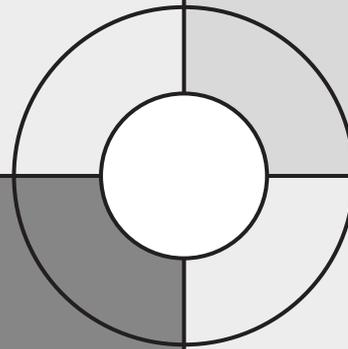
Haroldo Pinto Pereira

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CNI. THE STRENGTH OF THE BRAZILIAN INDUSTRY



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OF INDUSTRY **2013-2022**
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BRAZIL, 2014

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CNI

Confederação Nacional da Indústria

Setor Bancário Norte

Quadra 1 – Bloco C

Edifício Roberto Simonsen

70040-903 – Brasília – DF

Phone: (61) 3317-9000

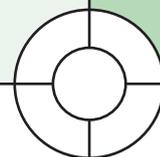
Fax: (61) 3317-9994

<http://www.cni.org.br>

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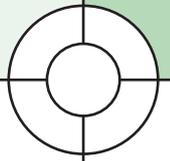
Phones: + 55 61 3317-9989 / 3317-9992

sac@cni.org.br



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INTRODUCTION

Brazil is faced with opportunities and challenges. It is a country with diversified industries, a considerable base of scientific and technological institutions, an abundance of natural resources, high biodiversity and high energy potential, from the pre-salt layer to renewable sources. Its domestic market is one of the largest in the world and continues to expand. However, if the country is to take full advantage of these opportunities, there are also challenges that must be faced.

Countries develop by improving their institutions on an ongoing basis. The National Congress, the Executive Branch, the Judiciary and society need to create conditions for the country to transform itself. Systemic costs have turned Brazil into one of the most expensive countries in the world, besides reducing its growth potential. The institutional environment for entrepreneurs is marked by complexity and insecurity. None of the branches can bring about these changes by itself. It is a job for society as a whole.

Industry has an important role to play in Brazil's growth agenda. It is the source of solutions to the challenges of creating quality jobs, increasing productivity, innovation and generating foreign exchange. GDP growth is dependent on the development of industry. Since 1970, Brazilian GDP has only grown by more than 4% a year on 22 occasions. Industry was the engine driving this growth, as it was the sector that grew most in 13 of those 22 years.

Countries are giving renewed support to industry. Throughout the world, the role of industry is being given renewed support. From the USA to the European Union, there is growing recognition that the metrics used to measure industry's share of GDP are not sufficient for capturing the effects of industry on innovation, the formation of activity networks, and its influence on service sector dynamics. The existence of an industrial ecosystem, made up of networks of companies, think tanks, providers of technological services and universities, is seen as crucial for stepping up productivity and fostering innovation. A strong industry is vital for growth.

The challenges for 2015-2018 should be seen through lenses adjusted to the transformation processes experienced by Brazilian and international economies and, especially, to the technological changes and to the systems through which global value chains are being integrated. Brazil has to develop an active strategy for integrating into the global economy. Our market is large, but not sufficiently explored. The Mercosur is important, but it cannot provide all the trade, investment and technological environment that Brazilian industry needs. The challenges of the global economy, of promoting institutional modernization, and of reducing the so-called Brazil Cost cannot be overcome through small improvements. Results need to be substantial.

Industry has a key role to play for Brazil to grow more and better. Brazilian industry has been virtually stagnant since 2010. As it has become less competitive, Brazilian industry has lost market share both domestically and abroad. The share of imported products in the domestic market for manufactured products has soared, in real terms, from 12%, in 2005, to 22%, in 2013. The volume exported by industry remains below the pre-2009 crisis volume.

Manufacturing industry production
Seasonally adjusted data
(Base: 2012=100)



Source: IBGE.

Brazilian industry will only resume growth by becoming more competitiveness.

Stepping up productivity and reducing the Brazil Cost are the challenges to be faced.

Increasing productivity is a priority. This will enable salaries and profits to rise whilst prices simultaneously fall. Greater competitiveness means increased production, more jobs, and higher earnings. Unlike in the past, we cannot expect an increase in the labor force to be the determining factor for growth in the Brazilian economy.

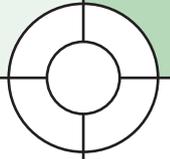
Productivity growth enables increased salaries to be sustainable. Increased salaries are important for the population and for strengthening domestic demand. Real earnings for industrial workers in Brazil have increased by 21% in real terms over the last 10 years, but these workers are, on average, only 1.8% more productive. The result is that the real unit cost for industry has grown by 19% more than in many other countries.

The appreciation of the real has intensified the low productivity problem. There are other equally important variables, but this effect cannot be underestimated. In spite of depreciating by 30% over the last two years, Brazilian currency still accumulated an appreciation of 30% between 2003 and 2013. The result is that unit labor costs have increased by 190% in US dollar terms, much more than observed among our main competitors. With such a high increase, it is not surprising that Brazilian industry's share in both the domestic and the international market has fallen.

Brazil is an expensive country. Other important costs for industry have grown more in Brazil than in competitor countries. Brazil is near the top of the ranking for higher energy, transportation, red tape, tax and interest rate costs, among others.

Determinants of Competitiveness			
	Brazil	USA	Mexico
Strengthening of local currency against dollar (2004-2014)a	20%	-	-11%
Increase in salaries (2004-2014)a	100%	27%	67%
Increase in electricity costs (2004-2014)a	90%	30%	55%
Increase in gas costs (2004-2014)a	60%	-25%	-37%
Increase in labor productivity (2004-2014)a	3%	19%	53%
Bureaucracy (Doing Business 2014 ranking)b	116	4	53
Nominal interest rate (3 months) 2014c	10.90	0.23	3.80
Tax burden (2011)d	35.3	24.0	19.7

Sources: (a) Boston Consulting Group. (b) Doing Business Country Ranking (1-189). World Bank. (c) The Economist, published on May 31, 2014. (d) OECD.



KEY POINTS TO BE ADDRESSED BY 2018

In 2018, industry hopes that Brazil's competitiveness indices will have improved substantially. Four years from, we want to be able to say that:

- **The tax system has been freed of the main inefficiencies that characterized it in 2014** (cumulativeness, taxation on exports and investment). Its complexities have been reduced significantly, making it compatible with international standards;
- **The labor relations system has evolved in the direction of recognizing bargaining supported by modern, flexible legislation and legal safety;**
- **Investments in infrastructure have grown in relation to GDP** through an increasing in private capital and public funds through better management. The progress made in this area has transformed into the main source of growth in the country's competitiveness;

- **Fiscal policy has evolved in such a way as to increase the rate of investment in GDP**, bringing interest rates down to levels closer to international ones and leading to a more stable, competitive exchange rate; and
- **The quality of education has improved significantly**, as shown by such student assessment tests as the *Prova Brasil* (Brazil Test) and the OECD Program for International Student Assessment (PISA).

The roads to competitiveness

The business environment needs a radical overhaul. Companies' capability to absorb the costs and accessory obligations arising from a wide range of laws, especially those governing taxation and labor relations, has been exhausted. Besides burdening enterprises, this environment also creates uncertainties for investors.

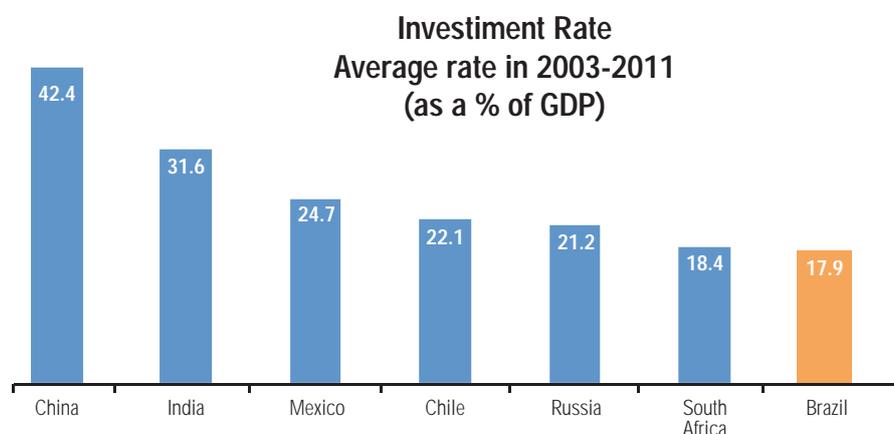
Brazil has one of the highest tax loads in the world and, unlike the majority of countries, also taxes investments and exports. Eliminating cumulative taxes and reducing the complexity of the tax system are key measures for reducing the costs of enterprises and legal uncertainty.

Labor legislation that is out of touch with the modern world, with excessive red tape and legal uncertainty, is a burden on companies and workers. Enterprises and workers suffer from both an excess and a shortage of rules. Red tape must be reduced, but it is also necessary to create clear, stable rules, especially with respect to outsourcing. In a world where outsourcing is the dominant form of organizing production, banning outsourcing is condemning Brazilian industry to inefficiency.

Growth also depends on a stable, predictable macroeconomic environment. Low inflation, balanced public accounts in the long term, and a credible monetary policy are key conditions for expanding horizons and keeping confidence high. This environment is vital for enabling internal and external economic agents to take their strategic decisions to increase the rate of investment in the economy.

Low savings penalize industry via exchange rates and interest. It is necessary to increase the volume of funds for investment in order to increase the rate of investment (as a proportion of GDP). The current rate, the lowest one among all emerging countries, reflects low domestic savings rates, especially due to the lack of contribution from the public sector.

Mechanisms must be imposed to limit public sector current spending in a way that allows for public savings to be generated without resorting to tax increases.



Source: IMF.

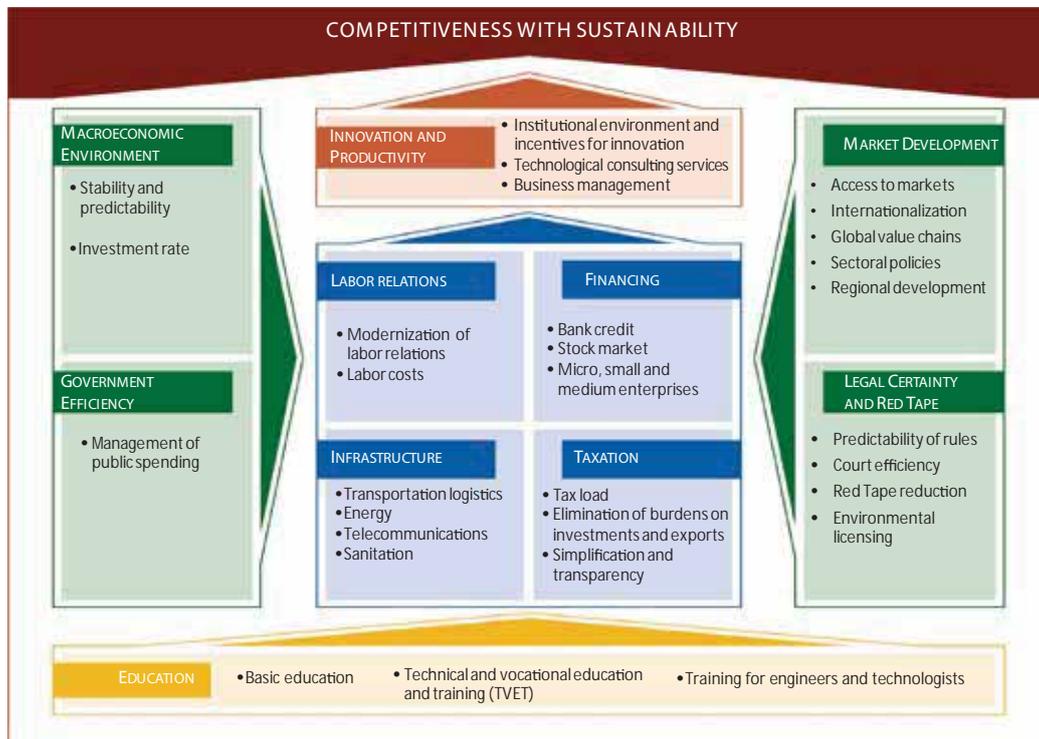
The shortage of qualified labor makes it difficult to increase efficiency and improve product quality. The marked increase in employment since 2005 has left the country suffering from a lack of qualified professionals. In industry, this is a problem that affects 65% of companies in all areas, especially on the shop floor.

Infrastructure: an example of challenges and opportunities. Brazil's inadequate transportation infrastructure and the high cost of energy supply are two of the main causes for the low competitiveness of Brazilian industry. Increased investments in infrastructure will produce significant gains. Significant progress has been observed in the regulatory framework in recent years; however, excess bureaucracy and the low efficiency of public administration have held investments back.

Focus, sound management, and a commitment to address competitiveness problems are necessary. The Brazil Cost issue has been on the agenda since at least 1994. It is vital for a president-led system of governance to be developed to manage the competitiveness agenda based on clearly defined goals and targets, full commitment, and periodic assessments with international competitors as a benchmark in order to ensure that this agenda is really put into practice.

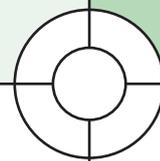
The Strategic Map of Industry 2013-2022 defines the key factors for increasing competitiveness. The agenda presented in this document aims to create a favorable business environment for the country's sustainable growth and to boost industrial productivity.

STRATEGIC MAP OF INDUSTRY 2013-2022



Brazil needs to make up for ground lost over the years in relation to its competitors.

This document sets out 42 executive summaries of CNI's proposals for voters and candidates in the 2014 elections. The studies and recommendations were drawn up based on the guidelines developed in the *Strategic Map of Industry* and they are intended to boost industrial competitiveness. The recommendations outlined herein are essential for the development of Brazil.



42 PROPOSALS FOR INCREASING COMPETITIVENESS

CNI offers agendas with proposals for comprehensive and specific reforms in ten key factors for competitiveness¹:

Taxation

- **Tax strategy: ways of moving reform forward** outlines paths towards reforming the Brazilian tax system, defining priority areas where changes are required for increasing the competitiveness of Brazilian products.
- **Cumulativeness: elimination to increase competitiveness and simplification** assesses taxes on consumption of goods and services (value-added taxes) and presents recommendations for redesigning this type of taxation in a way that respects the principle of non-cumulativeness of the tax system.

¹These agendas are available only in Portuguese at www.cni.org.br/eleicoes2014

- **Tax cost on investment: Brazil's handicaps and actions for change** measures tax cost on investments, compares it to other countries, and presents proposals for eliminating them.
- **The "SIMPLES Nacional" tax regime: changes to make growth possible** describes distortions that make it difficult for micro and small companies to grow as a result of high tax increases and proposes corrective measures.
- **Reducing tax and customs bureaucracy: proposals for simplification** identifies measures that impact on companies' operations, which would be easy to implement and do not depend on complex negotiations in the National Congress.

Labor Relations

- **Labor costs and productivity: international comparisons and recommendations** identifies, based on international comparisons, the importance of labor costs for competitiveness and discusses how the Brazilian legal framework contributes to increasing this cost either directly or by discouraging higher labor productivity.
- **Modernization and red tape reduction in labor relation: proposals for moving forward** presents feasible solutions that will have positive impacts on the competitiveness of Brazilian enterprises.
- **Outsourcing: essential changes** shows how production and organizational changes in enterprises can lead to the quest for specialization and how this phenomenon has changed international relations through global value chains. This document defends a draft law to regulate outsourcing and eliminate current legal uncertainty problems.
- **Collective Bargaining: giving value and modernizing** reveals that most of the solutions for labor relations involve giving value to and effectively recognizing collective bargaining as a tool that enables adjustments to be made according to different productive and labor scenarios and caters to the interests of both workers and enterprises.

Macroeconomic environment

- **Fiscal Rules: improvements for consolidating fiscal balance** analyzes the fiscal rules in force based on international best practices and proposes improvements to the Brazilian system.
- **Social Security: changing to guarantee sustainability** shows the importance of reform for the country's fiscal management and suggests paths for this reform.

Education

- **Education for the world of work: route to productivity** shows the connection between education and productivity along with what needs to be done for Brazil to improve its education.
- **Human resources for innovation: engineers and graduates from industrial technology programs** presents proposals for restructuring engineering courses as a tool for preparing professionals better adapted to facing the challenges posed by productivity and innovation.

Infrastructure

- **Infrastructure: the costs of backwardness and necessary reforms** examines the reasons behind delays in six infrastructure projects in Brazil and suggests reforms that can lead to more effective management of large infrastructure projects.
- **Logistical axes: industry's priority projects** summarizes CNI's studies that identify and select the lowest cost logistical systems, focusing on the domestic and external markets. These projects can be considered a portfolio for improving Brazilian infrastructure, with a view to integrating Brazil's regions physically and economically and allowing for the Brazilian logical infrastructure to be better planned.

- **Oil and gas concessions and transportation concessions: progress and proposals for improvements** assesses different processes for granting concessions in the oil and gas industry and in transportation, describing the progress made in this area and where change is necessary.
- **Ports: what has been done and what still needs to be done** gives a balance of changes in the regulatory framework, highlights the progress made, and suggests new areas for improvements.
- **Global energy environment: the implications for Brazil** presents recommendations for diversifying the energy matrix based on recent transformations in worldwide energy supply resulting from technological and regulatory trends.
- **Electric power: an agenda to ensure energy supply and reduce energy costs** details recent developments in the sector, identifies problems, and provides recommendations for Brazil to ensure a more secure electricity supply at competitive prices.
- **Natural gas: an alternative for a more competitive industry** shows the impact that shale gas exploration will have on the world and its effects on industry's competitiveness. It presents an agenda for necessary regulatory changes for Brazil to be successful in this new environment and develop a source of this essential supply for industry.
- **Sanitation: opportunities and actions for ensuring universal access to sanitation** details necessary efforts to ensure universal access to these services and opportunities for the industry that supplies equipment and goods in this area.

Legal Certainty and Red Tape

- **Paths toward strengthening legal certainty** identifies sources of uncertainty and provides recommendations for reducing legal uncertainty in Brazil.
- **Environmental licensing: proposals for improvements** details problems at both federal and state level and suggests a set of proposals to resolve this matter, which is one of the main reasons for delays in substantial investments in Brazil.
- **Regulatory quality: how Brazil can do better** explores the best international regulatory standards and points out the need for Brazil to carry out reforms that can improve regulatory quality by providing companies with better guidance and safety.

- **Relationship between the Internal Revenue Service and taxpayers: proposals for reducing tax complexity** shows, based on international experience, that Brazil can improve revenue service/taxpayer relations greatly by honing the process of establishing rules and consulting taxpayers.
- **Modernization of inspection mechanisms: international lessons for Brazil** seeks to identify the best inspection practices in the world and proposes improvements for Brazil.
- **Red tape reduction** is presented in three sets of proposals in the areas of **tax payment, foreign trade** and **labor relations**. Problems caused by excess red tape are identified and solutions are presented through proposals for new wording for relevant normative instructions.

Government Efficiency

- **Governance for competitiveness of Brazilian industry** shows that the Federal Government's ability to manage horizontal agendas, which are scattered amongst several ministries and agencies, is essential for getting results.
- **Regulatory agencies: initiatives for their improvement and strengthening** shows the importance of independent, transparent, stable agencies for ensuring the necessary security for attracting private investments in infrastructure.

Market Development

- **Foreign trade: proposals for institutional reforms** identifies institutional coordination problems in strategic planning and actual operation and the need to reinforce areas and institutions, besides suggesting innovative solutions such as nominating an industrial attaché in important countries for expanding exports of manufactured goods.
- **Reducing foreign trade bureaucracy: proposals for improvements** presents the consolidation of Brazilian foreign trade legislation and a set of initiatives for reducing red tape and sources of legal uncertainty.

- **Trade agreements: an agenda for Brazilian industry** presents industry's priorities for trade agreements and identifies key topics for negotiations.
- **Bilateral trade and investment agendas: China, United States and European Union** suggests strategies and actions for developing markets for Brazilian products in China, the United States and the European Union.
- **Brazilian investments abroad: their importance and actions to remove obstacles** identifies problems and necessary actions to stimulate the internationalization of Brazilian enterprises and reduce competitive disadvantages.
- **Services and industry: the missing link for competitiveness** points out the growing importance of services for industry's competitiveness and how the tax regime reduces the capacity of high value-added industrial companies to grow.
- **The Sectoral agenda for industrial policy** addresses the urgent need to overcome competitiveness problems and suggests measures that can facilitate the structural transformation of industry with a view to diversification and technological development.
- **Bio-economy: opportunities, obstacles and agenda** identifies the enormous opportunities available for Brazil to develop new industries in the pharmaceutical, food, energy, cosmetics and green chemistry areas, pointing out obstacles and what needs to be done.
- **Regional development: agenda and priorities** describes actions designed to reduce regional inequalities and strengthen the domestic market.

Innovation and Productivity

- **Innovation: priorities for modernizing the legal framework** highlights the progress made in innovation support tools, lingering problems, and what needs to be done.
- **R&D centers in Brazil: an agenda for attracting investments** points out the importance of Brazil taking systematic action to attract R&D centers and the need to improve coordination mechanisms between ministries and agencies around an innovation agenda.

- **Financing innovation: the need for changes** assesses investments under way and suggests the need to reshape these mechanisms in the light of new demands and changes in industry.
- **Intellectual property: changes in industry and a new agenda** describes changes taking place in the industrial and innovation environment that require a new vision on the role of intellectual property as a tool to promote innovation in Brazil.

Financing

- **Financing innovation: the need for changes**, as pointed out above, features proposals for improving tools currently available.
- **Private securities market: a source of corporate financing** supports the notion that the debentures market can be an ancillary instrument for company financing. A lot can be done in this area and the agenda does not depend on significant legal changes.

CNI

POLICY AND STRATEGY DIRECTORATE – DIRPE

José Augusto Coelho Fernandes

Director

Renato da Fonseca

Mônica Giágio

Fátima Cunha

Executive Management Unit for Publicity and Advertising – GEXPP

Carla Cristine Gonçalves de Souza

Executive Manager

Walner Pessoa

Editorial Production

Documentation and Information Unit – GEDIN

Mara Lucia Gomes

Documentation and Information Manager

Alberto Nemoto Yamaguti

Normalization

Grifo Design

Editorar Multimidia

Graphic design and editing

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