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Investigations Could Damage Brazilian Government's Economic Efforts

by LADB Staff

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Brazilian President Fernando Henrique Cardoso says the economy is recovering, and he is trying to convince European investors to return to Brazil. Potentially explosive investigations into the judiciary and the Banco Central could hamper his efforts both in attracting foreign investment and in pushing Congress to pass additional reform legislation. Cardoso left for Europe April 13 to meet with government officials and private investors in Germany, Portugal, and Great Britain. He hopes to convince European Union (EU) member countries that Brazil is overcoming its economic difficulties.

Cardoso will tell Europeans that the worst of the crisis, which culminated with a devaluation of the Brazilian currency, the real, in January, has passed and that the economy is stronger than many think. "There were difficult moments...few countries withstand a blow like that," Cardoso said in an interview published April 7 in the *Jornal do Brasil* of Rio de Janeiro. "What bank went under? What company went under? What country was contaminated? None."

Banco Central is under investigation

Investment house Banco Marka did go bankrupt in January after betting that the government would not change its foreign-exchange policy. The Banco Central then sold it dollars at a subsidized rate to pay off its debts, allowing it to go under without scaring the market. Analysts estimate the cost to the government at US\$68 million. The Fonte Cindam, another investment bank, ceased operations March 23 and was sold to a French bank. The widely criticized Banco Marka bailout is part of a congressional investigation by the Comissao Parlamentar de Inquerito, CPI) into the financial system.

The unfolding currency-market scandal could overshadow Cardoso's efforts to project confidence and recovery to the Europeans. Besides investigating the Banco Central's dealings with the two failed banks, Congress will look into various foreign banks that took enormous amounts of money out of the country in the days following the Jan. 15 devaluation, despite restrictions.

The CPI will examine allegations that the Banco Central leaked confidential information about changes in foreign-exchange policy to some banks, allowing them to make big profits. The insider-trading allegations increased when weekly news magazine *Veja* quoted Salvatore Cacciola, former president of Banco Marka, as saying he paid a Banco Central informant US\$125,000 a month for apparently bad information.

On April 12, Justice Minister Renan Calheiros ordered federal police to investigate the bribery accusations. Both Banco Marka and Fonte Cindam deny allegations of wrongdoing. The CPI could involve top Banco Central officials and former officials, including Francisco Lopes, head of the Banco

Central when it allowed the real to float against the dollar (see NotiSur, 1999-01-15). And, Sen. Jader Barbalho said the commission will question Banco Central president Arminio Fraga, who took over in February.

Fraga said the bank will release its internal report into the allegations, including whether some banks were notified in advance of the change in foreign-exchange policy. It will also answer the accusations that it sold Banco Marka and Fonte Cindam dollar futures at below-market prices on Jan. 14. Former Banco Central director Claudio Mauch has said the deals took place, but denied they were illegal.

The scandals have only intensified public anger at the banks, especially at reported huge profits at some institutions so far this year. "What we're dealing with now is a society with violence and unemployment on the rise, while the government seems to go out of its way to help financial institutions," said Deputy Aloizio Mercadante of the Partido dos Trabalhadores (PT).

Judiciary is also under investigation

Meanwhile, on April 8, another CPI began examining allegations of corruption and nepotism in the Judiciary. On March 25, influential Senate president Antonio Carlos Magalhaes proposed the investigation, citing evidence of 800 cases of corruption, nepotism, and the irregular use of public resources by the judiciary. "Judicial power is not untouchable," Magalhaes said. "We have powers in the legislature to regulate it, including by launching a CPI." Both investigations will last about 180 days.

Despite Cardoso's desire that Congress begin voting on reforms to overhaul the tax system, simplify the political-party structure, and streamline the judiciary, lawmakers' attention has been focused on the probes. Political analysts say Cardoso has so far managed to distance himself from the scandal. "At this stage, it doesn't even come near him," said Haroldo de Britto, political analyst at Goes e Consultores.

Some warn, however, that the CPI's, which have broad investigative powers, could eventually cause problems. "This all comes at a very delicate time for Brazil; foreign investors are now beginning to regain confidence in Brazil as a serious country with a serious economic team," said David Fleischer at the University of Brasilia. "However, if this case explodes and drags in other hot information regarding the financial system in general, the CPI may go in uncharted directions."

Cardoso's support has plummeted

Opposition leader Luiz Inacio Lula da Silva of the PT has vigorously attacked the Cardoso administration and called for a series of demonstrations that will culminate on May Day. "Brazil continues on the edge of the abyss while the government insists on telling us that the crisis is passing," said Lula on March 25. Lula criticized government measures to respond to the crisis and the appointment of Fraga, who worked for international financier George Soros, to the Banco Central. "It's like putting a mouse to guard the cheese," said Lula. Cardoso's support has fallen drastically since his re-election in October 1998. In a recent poll by independent polling firm Vox Populi, only 16% of Brazilians interviewed think Cardoso has done a good job. Another 39% percent say Cardoso's performance has been average, while 43% say he has done a bad job.

In addition, many respondents said they felt "deceived" by Cardoso, who was re-elected in part on the perception that he would insulate Brazil from the global financial crisis. While 36% of respondents said they felt Cardoso had deceived them, 18% described their attitude toward the president as one of "distrust," and 15% said "confidence." Prospects for a turnaround in support for Cardoso do not look good. Unemployment is hitting new highs and the government estimates the GDP will drop between 3.5% and 4% to negative numbers in 1999.

On March 30, Cardoso admitted that the austerity measures, implemented to get International Monetary Fund (IMF) bailout funds, had slashed social programs for schools, retirement homes, and projects to eradicate slave labor and protect the environment. The austerity drive has meant budget cuts for all ministries, including health and education. The government halved its budget for food rations for 8 million of the poorest Brazilians. Cardoso said the government sometimes made mistakes when deciding how to allocate scarce funds and unintentionally hurt crucial areas. [Sources: Associated Press, 04/07/99; Spanish news service EFE, 03/25/99, 03/28/99, 03/29/99, 04/08/99; Notimex, The Washington Post, 04/10/99; Clarin (Argentina), Notimex, 04/12/99; Reuters, 03/30/99, 04/07/99, 04/08/99, 04/12/99, 04/13/99; The Miami Herald, The New York Times, 04/13/99

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