8-10-2012

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Recommended Citation
Brazil Plans to Expand Defense Industry
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Category/Department: Brazil
Published: 2012-08-10

After consolidating its economy and moving to a prominent position on the world stage during the eight-year administration of former President Luiz Inácio Lula da Silva (2002-2010), Brazil under the leadership of President Dilma Rousseff has begun to think and act like a major global player. It is now the world's sixth-largest economy, and both the International Monetary Fund (IMF) and the British Centre for Economics and Business Research (CEBR) predict that by 2015 it will overtake France to become the fifth-largest economy, topped only by China, the US, Japan, and Germany.

Against this backdrop, President Rousseff announced on July 14 that in the next three years the country would spend US$70 billion on a program to develop its defense industry. The government will subsidize the creation of large business partnerships dedicated to the production of arms and defense equipment—for foreign and domestic markets—with the only condition being that the decision-making power of those conglomerates remain in Brazilian hands. Incentives would come through granting tax breaks and "soft" credits, and providing special conditions for participating in state contract tenders.

In presenting the idea, Rousseff did not refer to the country's position as the sixth-largest economy but opted to speak of sovereignty. "Whether because of the size of our territory and length of our borders or because our country has been blessed with enormous wealth, we need to develop this industry, which is strategic to our sovereignty," she said.

Brazil's defense industry has experience with such joint ventures. There are already groups made up of businesses that maintain their original activities but partner with another company to develop a particular project. One such case is Odebrecht—a construction company with a presence throughout South America and in Dubai, Tokyo, Beijing, and the African countries of Angola, Ivory Coast, Mozambique, and Cape Verde, where the company builds everything from large railway networks to airports. It is associated with the state Nuclebrás (Empresas Nucleares Brasileiras), a Navy endeavor, using French technology to build a nuclear submarine budgeted at US$4.8 billion. Brazil also has long experience with companies such as Avibrás (drones and missiles), Helibrás (helicopters), and CBC (ammunition for military and civilian use).

The Rio de Janeiro daily O Globo says that the huge amounts of money involved will act as a powerful magnet for leading national construction companies to partner with multinationals that are already major global players.

The Andrade Gutierrez conglomerate joined the French group Thales Spectrum, and Engevix, an engineering firm that operates in energy and oil areas, joined German firm Thyssen Krupp. The daily said that other large companies, such as OAS, Camargo Correa, Synergy, Gueiroz Galvão, and even Embraer—the flagship of Brazil's aeronautics industry—are taking similar steps. The Associação Brasileira das Indústrias de Materiais de Defesa e Segurança (ABIMDE) said that the country has an export potential in defense products of US$7 billion starting in 2030.
Rousseff creates strategic defense companies

Conditions for accessing the incentives are spelled out in the text of law 12.958, passed in March, and the regulatory decree issued in late July, which establish strategic defense companies (empresa estratégica de defesa, EED). Companies that work in research or production of strategic and defense products will be designated EEDs if they are headquartered in Brazil and have bylaws guaranteeing that all decisions will be made by a majority of partners who are Brazilian nationals.

The Ministério da Defesa will verify compliance with the requirements and will also issue the "EED seal." Companies with this seal will be able to participate in federal government tenders for defense equipment and services contracts. The EEDs will receive incentives to obtain foreign technology transfer to develop their own research within Brazil. The EEDs special 5-year tax regimen suspends payment of three federal taxes, which together could range from 8% up to, in some cases, 54%.

The proposal to develop and expand the weapons industry brought criticism. The Federação das Indústrias do Estado de São Paulo (FIESP) says it is "perverse to promote partnership between local businesses and multinational weapons manufacturers." Despite the requirement that the Ministério da Defesa be in charge of supervision, "national companies will not decide what will be produced, this will be done by foreigners and, in that context, national sovereignty will become just a business opportunity," said FIESP.

The business organization explained that "most businesses in the sector are small, with fewer than 40 employees and limited financial ability to compete globally or to associate with large multinationals."

Gen. Aderico Visconte Pardi Mattioli said, however, that "law 12.598 and its regulatory decree open up the possibility of working in the military science and technology sector without the need to go through bidding, because foreigners will do it directly." The general, director of the defense products department at the Ministério da Defesa, touched a sensitive point. Corruption is endemic in Brazil, and the lack of bidding can lead to shady dealings.

As an example, the Web site Carta Maior recalled the problems with French company Thales, now associated with the Andrade Gutierrez construction company. The Argentine judiciary is still investigating a 1997 contract to privatize national radio broadcasting space, said the report. The case led to a request to Switzerland to lift its bank secrecy. The evidence sent by the Swiss had been sent to France in October 2007. During the second term of former President Carlos Menen (1989-1999), Thales—formerly Thomson CSF—"won" an unusual bidding process without competitors by which Argentina became the only country in the world to cede control of its air waves to a private company, and a foreign one at that (April 7, 2006). The contract was annulled in 2004 by President Néstor Kirchner (2003-2007).

Protecting oil reserves part of strategic defense

With a territory of 8.5 million sq km, Brazil is the fifth-largest country in the world. It shares a 14,691 km border with 10 other South American countries (Chile and Ecuador are the only South American countries that do not border Brazil) and has 7,491 km of coastline. It is home to 192 million people.

But President Rousseff did not cite these figures when she spoke of the need to guarantee security. When she said that the country had been "blessed with enormous riches," she was referring
to everything that Brazil has always had but she specifically spoke of the oil that, in 2007, was beginning to be discovered in the depths of the Atlantic off the coasts of Rio de Janeiro and São Paulo.

Days before the announcement of the special conditions for businesses in the military sector, the president said at a military event that Brazil was committed to increasing its naval power to protect its vast deepwater oil and gas reserves. "Investments in new patrol boats will enable an increased state presence in our territorial waters, where most of our oil and gas reserves are," said Rousseff, justifying the policy of modernizing the Navy as a "strategic demand."

Rousseff then expressed what could be understood as the philosophy of the business-partnerships plan. "We know that our role in preserving peace depends on our dissuasive ability. That is why our armed forces require quality equipment, ready to be used, and adequately trained personnel," precisely what the EEDs and their partners will provide.

Perhaps coincidentally, either because of business skill or the disloyalty of some high official in the Ministério da Defesa (as many lawmakers speculated), a day after the president made her ideas public, Boeing vice president Mike Gibbons sent a message from the company's Seattle headquarters, saying the US aerospace giant was "willing to offer Brazilian companies the opportunity to construct components for the Super Hornets and other future projects of Boeing."

Of course, Gibbons' generous offer came blatantly conditioned. For Boeing to make the offer a reality, Brazil would first have to be willing to buy Boeing's F-18 Super Hornets in a bidding process in which it is competing with French company Dassault's Rafale and Swedish firm Saab's Gripen (NotiSur, March 25, 2011, and May 25, 2012). In the short term, the contract would be for 36 planes, but by 2020 it would reach 120, at a cost of more than US$6 billion that Brazil would invest to protect, from the skies, the fabulous oil riches hidden under its Atlantic shelf.

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