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Special for *O Papel* Magazine

Roberto Haddad: "If on one hand we have a number of challenges to overcome, on the other, investors want to enter or increase the stake they already retain in Brazil"

Brazil ranks last in cost competitiveness

Despite the significant increasing interest on the part of many companies in servicing Brazil's large and growing domestic market, costs in our country are higher than those observed in other high growth nations, such as China, India, Mexico and Russia. This was the conclusion of the *Competitive Alternatives 2012* research performed by KPMG.

This investigation provides an independent comparison of international business sites in more than 110 cities of 14 countries, worldwide. The study contemplates a large variety of issues on its analysis of business competitiveness, focusing the undertakers costs and, also, population characteristics, demographic data, education, qualified labor, innovation, infrastructure, economic conditions, regulatory environment, cost and life quality.

The 2012 edition is the first *Competitive Alternatives* study to examine high growth countries and compare their competitiveness costs. "The reason for such inclusion is due to the fact that they are relevant countries in today's global economic scenario; countries now deserving great investment attention. Therefore, evaluation of particular costs is fundamental in this sort of study. It is of essential importance for investors to be aware of costs, challenges and opportunities related to each of the said countries", says Roberto Haddad, partner in KPMG Brazil's International Tax area.

Based on this objective, the study has concluded that China and India are leaders among the analyzed high growth countries, with overall business costs 25.8% and 25.3%, respectively, lower than the North American reference base. Mexico, in turn, presents costs 21% lower than the North Americans, while Russia has a 19.7% difference also in relation to the United States. Coming to Brazil, cost advantage amounts to only 7% in relation to the US economy, which figure ranks the country in the last place.

Low labor costs provide support to China and India's competitive advantage, with the first one offering the lowest costs in the manufacturing sector and, for the second, in the services segment. In turn, factors that hurt Brazil most are referred to salaries and taxes. "Salary levels in Brazil, including the minimum wage, are significantly higher than those of the high growth studied countries, and the tax load also negatively impacts Brazil's total cost performance", says Haddad.

However, the KPMG's International Tax partner states as impossible to blame a single factor and label it as being the main reason for the country's last-place ranking. In this month's Interview, Haddad grants a detailed analysis of the Brazilian current scenario, brings up negative factors and discloses the impacts they may cause to the interest of foreign investors towards Brazil.

O Papel – What reasons cause Brazil to exhibit the highest costs in comparison to the four other high-growth countries? Does the country's tax burden stand out as the main responsible factor?

Roberto Haddad – I wouldn't attribute all the blame to the tax burden. The study we prepared is quite complete, since, in order to have a ranking of countries based on costs and competitiveness, it turns out essential to analyze a variety of factors. The points analyzed not only include measurable costs - as the case of labor costs, tax costs, infrastructure costs and energy costs (that is, all the costs that involve an economic business) -, but also issues that indirectly impact the undertaking. In other words, those factors not that easily measurable, such as characteristics of a country's population, status of education and number of professionals prepared for the existing labor market. Therefore, this means that any position presented in the ranking is the consequence of a combination of factors. It is not possible to blame a specific item for the ranking of a country, be it Brazil or any other analyzed nation. I believe that Brazil's bottleneck is in large evidence perhaps because the country was not prepared for such a high growth, followed by a sudden repositioning. Of course, this progress is a country's merit, since it did its economic homework properly, but, at the same time, is also related to the decline of other countries. I see the global scenario with fewer competitors, which fact generates more opportunities. Brazil, however, is not yet prepared to compete at its best.

O Papel – What competitive disadvantages can this high cost factor cause to the country? Could the interest of other countries to invest in Brazil be endangered?

Haddad – Before saying what can negatively affect the country, it is important to understand that Brazil is in the spotlight. If on one hand we have a number of challenges to overcome, on the other, investors want to enter or increase the stake they already retain in Brazil. This has to do with several matters. The first: in view of an environment of systemic crisis of considerable uncertainty and insecurity, Brazil stands out with a strong fiscal and financial profile. The second: even those countries not in the center of the crisis have lost a bit of the investment focus. They are, in general, more mature markets that hold higher competitiveness, but, in exchange, do not have a significant entry of new consumers in the market. Brazil stands out as a nation that has increased about 30 to 40 million people in its consumer market. It's an enormous amount of people that was not on the sight just a few years ago and, at present, has much more credit and purchasing power. Additionally, there are certain issues that put Brazil on the international radar, such as the discovery of a large amount of oil and a gigantic market surrounding it. It is also important to remind the upcoming sporting events, which also attracts considerable investment. As a result, this is a very favorable moment for Brazil. It makes many investors look at the country with special attention.

O Papel – But what would be the appropriate ways to reduce costs that make Brazil ranking the last and, with so, improve its condition of competitiveness?

Haddad – In Brazil, there still are gaps in education at all levels. If we compare to China, we will see there a population that can only have one child per family and invests a lot in education of their children. As a result, China is developing well-qualified professionals for the future. We will, certainly, also have good professionals here, but, quantitatively speaking, I can't say whether we are at a same level. In terms of infrastructure, improvements are to be made in a variety of areas. Our airports, for example, do not possess adequate structure to service a large number of users, a scenario that hinders the access to the country. The lack of hotels is another point that draws attention when looking at infrastructure. This scarcity causes all available rooms to double in price. This whole situation shows a series of faults: there isn't an appropriate education, non-existence of large capacity airports, not enough hotels. In terms of quantifiable costs, the study has shown that salaries are higher in Brazil. But I believe that salaries in Brazil are higher than in some other countries because needed to cover expenses that should be taken over by the government, like healthcare. I do not believe the solution would be to cut salaries in Brazil and match them to those paid in China, where different sorts of slave labor still exist. The Brazilian issue that has to be solved is the way taxes are distributed, which strongly involves labor costs. In addition to compensation, there are very high labor charges that end up costing around 60% more than the salary itself. And, lastly, there is the matter of taxes, but it would be a mistake to consider the income tax as the main item responsible for impacting the ranking. Even though the income tax rate is in Brazil

34%, it is a figure attuned to that of other countries. The global average is 30%. Perhaps, the biggest impact should be attributed to the excessive number of taxes in Brazil, such as IOF, IPI, ICMS and many others.

O Papel – Are there any actions performed by the other four developing countries that could be adopted in Brazil, in order to minimize the today existing costs?

Haddad – We must always learn from good examples, but they are of a quite different line from the ones practiced in Brazil, and we cannot ignore the cultural traditions of each country. In fact, in such an aspect I even see advantages in our favor: Brazil is the most westernized among the four other analyzed countries. The fact that we have ways of speaking and acting similar to those of the Western countries establishes a stronger connection and generates more easiness. If, however, we were to shadow anything, I believe that unconditional dedication to education would be a good option. We need to invest more in education, because with prepared people we can settle everything else.

O Papel – What are your expectations in relation to solving the bottlenecks pointed out?

Haddad – In the short term, I do not see any major improvements , since we rank a very distant position in comparison to the top positions. However, and without a doubt, we are seeing many initiatives in changing. The concern towards reducing labor charges is an example that has already become reality, as well as the need for investing in infrastructure. I would say that, with the upcoming sport events, I do not see how not progress in terms of basic infrastructure. We were lucky and have shown competence in winning the dispute to host these events. Perhaps, if not having these events on the calendar, such changes would not be feasible so soon. The trend, in my opinion, is towards improvements. ■

Ranking and cost index of countries presented on the KPMG's *Competitive Alternatives 2012* study

Overall ranking in 2012	Position within the segment	Country	2012 cost index	Cost advantage in relation to the USA
High-growth market				
1	1	China	74,2	25.8%
2	2	India	74,7	25.3%
3	3	Mexico	79,0	21.0%
4	4	Russia	80,3	19.7%
5	5	Brazil	93,0	7.0%
Developed market				
6	1	United Kingdom	94,5	5.5%
7	2	Holland	94,7	5.3%
8	3	Canada	95,0	5.0%
9	4	France	96,1	3.9%
10	5	Italy	97,9	2.1%
11	6	United States	100,0	0.0%
12	7	Germany	100,1	-0.1%
13	9	Japan	109,4	-9.4%