



## FINANCIAL TIMES

'Without fear and without favour'

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# Brazil's fall from grace is of its own making

The important question now is whether its institutions continue to hold

Brazil is in crisis. Earlier this month, more than 1m protesters took to the streets to voice their discontent. Much of the country suffers water rationing following a long drought. Petrobras is engulfed in an epic corruption scandal that saw up to \$10bn embezzled from the oil company. The economy is likely to shrink this year and perhaps next year as well, which would be its worst performance since 1931. Approval ratings for Dilma Rousseff, the president, have slid to 13 per cent, the lowest on record. It seems only yesterday that the country was feted as the new best thing. So its fall from grace has been spectacular. Sadly, the situation is likely to get worse still. The central question is whether Brazil's institutions hold as it does.

A large part of the blame lies with Brazil itself. For much of the 2000s, it enjoyed an unprecedented commodity boom. This bolstered its terms of trade, swelled government revenues, boosted domestic wages and propelled a domestic credit boom. When investors clamoured to buy into Petrobras's 2010 \$70bn equity offering – the world's largest – Brazil really did seem to be *o melhor país do mundo*, the best country in the world. In reality, it was riding the steroid fix of a credit boom in which Brazil reaped the benefits of globalisation without any of its disciplines. Now the process is going into reverse.

The collapse in the currency, down almost a third against the dollar in just six months, is a dramatic repricing of the economy. But the trade-weighted real exchange rate, which adjusts for inflation, is still higher than its 20-year average. Unit labour costs are also higher, in dollar terms, than in 2010. So the currency is likely to weaken more.

Interest rates have been increased. That is partly to quell inflation, a side-effect of the weaker currency. But interest rates have also had to rise to

compensate foreign investors for higher country risk – and Brazil needs foreign capital to fund its current account and fiscal deficits. On the domestic side, though, higher rates will hurt indebted Brazilians, adding to the squeeze from finance minister Joaquim Levy's austerity plan.

The discipline of globalisation is being felt in other ways too. US market probes into Petrobras added impetus to a local corruption investigation that has led to 103 indictments and a Supreme Court investigation into more than 30 sitting politicians. Ms Rousseff, chairwoman of Petrobras before she became president, has so far been spared. But calls for her impeachment, while ultimately unlikely, are rising.

The government, in power for 12 years, has blamed external factors. But the mess is largely of Brazil's own making. For a counterfactual, one only has to look at the more market-orientated Pacific Rim countries of Chile, Colombia and Peru. They enjoyed similar commodity and credit booms but without the same hangovers. Their economies are still growing fast.

All is not entirely bad for Brazil, though. The country is a long way from falling back into its hyperinflationary ways of old. Better still its institutions are holding, especially the judiciary. Last year, prosecution of the *mensalão* vote-buying scandal saw several high-level politicians convicted. Now others are in the dock over the Petrobras scandal too. Separately, Eike Batista, a former billionaire accused of insider trading, may go to jail. This would have been unthinkable a few years ago, when impunity reigned.

So Brazil's crisis is bad and will probably get worse before it gets better. Yet it could have been worse still. That is progress, of sorts, for "the country of the future", as the cliché goes. Most of all, it means that Brazil still has one.

# Warm feelings are no help to the climate

Curbing greenhouse gases requires policy action, not gestures

It takes some variety of wilful ignorance to dismiss the need for action to avert the threat of climate change.

From imaginings of vast conspiracies to complacency that global warming can only be benign, the arguments against taking the danger seriously are rooted in a refusal to face reality. The climate is a complex system, of course, and forecasting it fraught with uncertainty. But the evidence is strong enough to make it clear that the risk of catastrophe cannot be dismissed.

Yet advocates of action on climate change often display their own varieties of irrationality. The campaign for universities, charities, local governments and others to sell their holdings in fossil fuel companies, which has been gathering momentum in recent years, is a case in point.

The campaigners' zeal is understandable. The potential consequences of unrestrained fossil fuel development are alarming, and if you are looking for someone to blame, the oil, gas and coal industries are an obvious target.

By focusing on divestment, however, the campaigners are channelling their efforts into an issue that is largely irrelevant to the ultimate objective of minimising the threat of climate change.

The financial impact of divestment is likely to be negligible. If charities sell their holdings in fossil fuel companies, other investors will buy them. If enough funds sell, the shares may fall, raising the companies' cost of capital, but evidence from the divestment campaign over South Africa suggests the effect is unlikely to be large.

Divestment campaigners often say their objective is not so much financial as symbolic: they want to send a signal that fossil fuels are morally unacceptable. It is hard to see, however, how the world can be persuaded to shun voluntarily the source of more than 80 per cent of its energy. Fossil fuels offer

enormous benefits as well as great risks, and their role in sustaining standards of living worldwide is for the time being irreplaceable.

Nor is it reasonable to expect fossil fuel companies to be the pioneers of the transition to other sources of energy; they have tried that many times in the past, always with disappointing results. The real advances recently in low-carbon energy, such as the plunging cost of solar power systems and progress in battery technology, have all come from outside the fossil fuel industries.

It is true that as the world shifts away from high-carbon energy, the oil, gas and coal companies will become less attractive investments, but shareholders can take their own views about the timing and consequences of that transition. Divestment should be seen as an outcome, not an instrument.

If global greenhouse gas emissions are to be brought under control, governments will have to play a central role. That does not mean the state takeover of the economy sometimes imagined by climate sceptics, but there will have to be a framework, including taxes and other incentives, that changes the behaviour of both businesses and consumers.

A genuine solution to the threat of climate change will require a price on greenhouse gas emissions, greater investment in energy innovation, switching from coal to gas to power generation, cost-effective means of storing carbon dioxide, and a global framework that encourages all the countries of the world to participate. Divestment helps with none of those.

At best, the divestment campaign will encourage a wider debate about those practical measures that are needed. At worst it will fool people, including the campaigners themselves, into believing that something significant is being achieved.

# Letters

## Sound of bubbles popping could be deafening

Sir, John Plender sees European Central Bank QE as distorting markets ("Draghi's quantitative easing stokes risk of bond market bubble", Insight, March 18). "Risk"? When investors have to pay the German government for the privilege of lending it money for the next seven years, and most European peripheral bonds in a depreciating currency yield significantly less than the US, is there much room for doubt?

One point of QE is to distort asset markets (known in polite circles as the portfolio balance effect). Excessive price action in government bonds, credit, equities and the euro needs to happen, or it won't work. Needless to say, this all distorts the allocation of resources and important investment and savings decisions.

The question is what happens when the buying stops. Will governments have used the benefit of low rates and

better growth to sweeten the pills of structural reform and improved debt sustainability?

If not, depending on global inflation and the growth backdrop, the sound of bubbles popping could be deafening.

**Paul Mortimer-Lee**  
Global Head of Market Economics  
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## Calm down – the parallels with 1937 are not as close as has been suggested

Sir, In "Fed rate rise risks 1937-style market slump, says fund chief" (March 18), you gave prominence to the warning from Ray Dalio, hedge fund owner, that the US Federal Reserve risks a disaster when it decides to raise interest rates. It is nevertheless appropriate to remind people to calm down and set the record straight since the parallels with 1937 are not as close as suggested.

Economists still debate the causes of what was then the third worst recession in US history, in which gross domestic product fell 11 per cent, industrial production 32 per cent and the unemployment rate rose to 20 per cent. The one thing that was not to blame was a rise in interest rates because these had been at zero for some time and the brief blip up of a few basis points in 1937 was inconsequential. A more likely monetary villain was the decision by the Fed to double bank reserve requirements in the summer of 1937, following three years in which reserves had increased sixfold.

Probing a little deeper, we know now that this monetary measure was introduced after a sharp slowdown in the money stock, which was in turn due to the Treasury's decision to sterilise all gold inflows with effect from the end of the previous year. Gold comprised more than four-fifths of the monetary base. This decision was taken because, after the US returned to the gold standard in 1934, strong inflows of gold to the US fuelled vigorous monetary expansion, which instigated economic recovery and fears of rising inflation. By early 1937, the economy stalled, coinciding with the administration's decision to distance itself further from the New Deal by balancing the budget. The Fed's reserve requirement changes were not helpful but, by the time they came into force, the damage was done.

Many people nowadays opine about Fed policy and there is no question that leaving the post-financial crisis monetary regime, now under consideration in the UK as well as in the US, will involve taking policy risks. It is not appropriate, though, to draw on the lessons of a totally different monetary and fiscal experience. The important point is that as central banks gradually adjust policy rates away from crisis-type levels, which they should, they must try to ensure that market expectations about future interest rates remain well informed and contained.

**George Magnus**  
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## Google Earth fails . . .

Sir, With reference to Lucy Kellaway's column "Google CFO's 'I quit' note is a classic in a suspect genre" (March 16): Patrick Pichette deserves poor marks in geography, too – Serengeti National Park is some 300km from Mount Kilimanjaro, which therefore can hardly be "towering" over it.

Ditto, of course, for Toto.

**Kresimir Penavic**  
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## COMMENT ON FT.COM

**Cleaning up the lobbying business**  
Nick Butler says it's wrong to think UK, US and European public life is free of corruption  
[blogs.ft.com/nick-butler](http://blogs.ft.com/nick-butler)

## Wrestle no longer with the Greenspan conundrum

Sir, Martin Wolf is correct that "ultra-low interest rates are not a plot by central bankers", but rather the result of "real" economy forces that overmatch monetary policy ("Strong currents that keep interest rates down", March 18). He also rightly points out that if central banks had been causing rates to drop below equilibrium for a very long time, it would have pushed up resource utilisation to a point where scarcity caused prices to rise.

It is possible to apply Mr Wolf's insight to predict the effects of the keenly anticipated increase in the Fed funds rate. The forecast issuing from Mr Wolf's position is that it will not much matter. This may surprise people. After all, the Fed's interest rate policy is the most closely monitored and discussed economic variable of our time. Is it really possible this emperor has no clothes?

Indeed it is. The Fed funds rate affects the cost at which banks can borrow reserves overnight, and US banks are awash in excess reserves to an extent that has no historical precedent. US banks don't need to borrow reserves, so it won't matter a bit that the Fed has increased the price of borrowing reserves. If the Fed's interest rate is a non-event to banks, there is no channel by which it can be transmitted to the rest of the spectrum of rates, other than if it acts as a "sunspot" to co-ordinate expectations.

Another fact in support of Mr Wolf's position is that the last time the Fed fund rate was increased, in 2004-05, long-term rates barely budged. Fed chairman Alan Greenspan could not understand why, so he called it a "conundrum". Mr Wolf has explained why it is not a conundrum at all.

**Daniel J Aronoff**  
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## But what's behind the glut and dearth?

Sir, Martin Wolf ("Strong currents that keep rates down", March 18) effectively dismisses loose monetary policy as the cause of today's ultra-low interest rates. He wonderfully describes central bankers as "apes on a treadmill", finding no better options to deal with the current global depression. The alternative explanation Mr Wolf offers is "a glut of savings and a dearth of good investment projects". It's curious that he stops here and does not discuss the causes of this glut and dearth.

What impresses me in the seventh decade of my life is the degree of uncertainty in today's world, which seems directly linked to political



## Sophisticates would have preferred 'share of sip'

Sir, I could not agree more with Jonathan Kahn's assessment regarding the vulgarity of the term "share of throat" (Letters, March 19). Alas this term was generated by the much larger and less delicate sector of the beverage industry: carbonated beverages. Even "market share" implies a heinous commonality between, God forbid, beer as well as sodas. Had we in the tea industry chosen a term to define our market presence I think we would have preferred to go with "share of sip".

Yours in sophisticated superiority,  
**Jim McDowall**  
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instability in every region of the world and to the global threats of climate change and infectious disease. The pace of technological change could be another major factor. The economic depression surely contributes to political instability but not necessarily more than other factors. And there is no credible link between the depression and global warming or outbreaks of Ebola and other pathogens.

I see little chance of "normal" interest rates before people around the world feel less worried about what's coming next and how it will affect them.

**Lex Rieffel**  
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## The more diversity, the better for boards

Sir, Of course the finance industry needs more women ("Boardroom tokenism skirts the need for female skills", John Kay, March 18). But Professor Kay gets the case maddeningly wrong in three ways.

First, there is strong evidence that companies with more diverse boards, no matter how diversity is defined, are more likely to perform better compared to similar companies with less diverse boards. This is perfectly intuitive given the reasons behind regulations requiring independent, outside board directors. Well-functioning boards include individuals ready to raise challenging questions, work through conflict, and inspire respect and collaboration. The more diversity, the more likely boards work in this way. Boards and C-suites of financial services companies should definitely strive for greater diversity.

Second, despite the claim that risk-taking is a function of biology, important research on women in the workplace has found that they

embrace risk and that their decision-making around risk follows patterns identical to men's. The idea that women are more risk-averse than men reinforces stereotypes that stymie career progression for men and women, and limit organisational potential.

Third, it is probably true that we need unique guidelines for corporate governance in the financial sector because, to an unusual extent, banks and other financial institutions both serve and pose risks to the public. But rather than focus on gender, these unique guidelines should focus, as the 2009 de Larosière report on EU financial supervision noted, on aligning the interests of multiple stakeholders, including the taxpayers ultimately responsible for bailouts.

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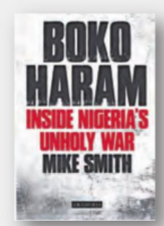
## Such opposing beliefs cannot be marginal

Sir, Gideon Rachman certainly has unique insight into how the US and China are posturing in Asia: "China's strongest card is its growing economic power. America's strongest card . . . is its military might" ("China's money magnet pulls in America's allies", March 17). I would have thought he might have briefly juxtaposed the world's largest communist power and the world's most powerful democracy, along with their respective differences and how each nation "influences" in Asia. The differences are vast, grounded in government and ideology. Can it be that such opposing beliefs are marginal, and all that matters today is economic power and military might?

**Neal Horowitz**  
President,  
Henry Hale Maguire,  
Singapore

# Complex roots of Nigeria's deadly insurgency

Book review  
Michael Peel



**Boko Haram: Inside Nigeria's Unholy War**  
by Mike Smith  
IB Tauris (€18.99/£9.29)

Boko Haram's pledge of allegiance to Islamic State of Iraq and the Levant has seized attention for an insurgency that has killed thousands and threatens the security of Nigeria's northeastern neighbours. But, as *Boko Haram: Inside Nigeria's Unholy War* makes clear, the Islamist group's caliphate also mirrors the existential troubles gripping Africa's most populous country as it stands on the brink of its most open elections for almost two generations.

The March 28 presidential and parliamentary polls were postponed from February 14 to give a new multinational military force time to drive Boko Haram from areas where 1.5m people have fled their homes. The election pits President Goodluck Jonathan, a Christian from the oil-rich south, against Muhammadu Buhari, a Muslim northerner and former military dictator. The contest reflects divisions long associated with deadly conflict in Nigeria, a country confectioned by the British a century ago – and yet the rise of Boko Haram has more complex roots than that.

Mike Smith, the Agence France-Presse news agency's Lagos bureau chief between 2010 and 2013, traces the history behind today's northern killings and the #bringbackourgirls meme that swept the media last year after more than 200 female students were kidnapped from the town of Chibok. Corruption and mismanagement have denied the majority of Nigeria's estimated 170m people a fair share of the oil wealth,

but the north has mostly missed out on even the limited development that underpins southern-based industries, such as telecoms, and the emergence of Lagos as an ambitious quasi city-state. Smith highlights the modern resonance of the 19th-century northern caliphate centred on the city of Sokoto. One academic calls it a "truly remarkable" example of state-building, almost free of "rebellions or schisms, famines or epidemics, and . . . economically successful as well". The contrast with today's poverty, illiteracy and ill-health is stark.

These are the arid fields in which a militant Islamist movement emerged more than a decade ago, prompting the first of many counterproductive official crackdowns. Smith quotes a Nigerian security official telling him last year that up to 3,000 suspected Boko Haram detainees might be quietly radicalising further as they suffered abuses in the "ratholes" where they were held. The author recounts how Abubakar Shekau, the "bloodthirsty" architect of Boko Haram's suicide bombings and kidnaps of the past few years, took power only after his predecessor was shot in police custody in 2009. The book examines possible reasons why the security forces and their civilian masters have failed to quell the threat since, including an ill-equipped military, graft and lack of political will.

Smith is sceptical of Mr Jonathan's strategy of branding Boko Haram as "al-Qaeda in west and central Africa",

in an effort to win more global support. While some experts suspect links between individuals associated with Boko Haram and al-Qaeda in the Islamic Maghreb, the Nigerian group seems so far to have remained focused on its heartland and the porous border region around it. The author's take is that the debate over Boko Haram's cross-frontier connections and jihadi goals is in any case "almost beside the point"; the underlying problem is the way Nigeria is being "robbed daily" of its riches and dignity.

The best bits of *Inside Nigeria's Unholy War* are focused reportage such as the moving tale of Wellington Asiyai, an assistant police superintendent shot in a 2012 attack in the northern city of Kano. The writing, however, could have done with a tougher edit.

Smith's achievement is in diligently marshalling the available information rather than in offering striking new facts or insights. What shines through is his measured anger, shared by many Nigerians, about a country battered by empire builders, the curse of oil, the military and a devastating 1967-70 civil war. Since becoming nationals of a country they neither desired nor designed, Nigerians have had to be resourceful and durable. The Boko Haram war, and the election it looms over, are as stern a test as they have faced in a long time.

The writer is the FT's Bangkok regional correspondent and a former west Africa correspondent