The new and emerging economies, with their ever-growing number of middle-income consumers are an enticing proposition. In some cases, where products have been commoditized or margins squeezed, new sectors or product niches present opportunities for the transfer of existing skills. But decisions made now can have enduring consequences. Lack of market understanding or insufficient forward planning can blight a venture in years to come. Commercial and operational issues, taxation, intellectual property, employee remuneration and regulation all bring challenges in new markets and jurisdictions. Meanwhile pricing, innovation, supply chains and routes to market in one industry or sector may turn out to be quite different in another.

KPMG can help fill the gaps in knowledge and assist with strategy development activities as well as anticipating and preparing for the opportunities and risks of entering a new market.

Brazil comes of age

The eyes of the world are on the so-called BRICs (Brazil, Russia, India, China). In many ways, Brazil’s economy is one of the most promising markets across the globe. The Real, Brazil’s currency, recently hit a nine-year-high against the dollar, inflation is under control and millions of Brazilians are being propelled into a growing middle class. Brazil’s largest stock exchange, Bovespa, located in São Paulo, was one of the best performing exchanges in the world last year and recently, Brazil has been awarded “investment grade” status by Standard & Poor’s.

Unlike many other regions in the world, Brazil’s economy resumed growth only experiencing negative growth in just one quarter of 2009. 2010 GDP and personal disposable income are expected to resume growth as unemployment is projected to decline further. A growing population and increasing consumer demand, coupled with stable input cost prices, may indicate that Brazil could be an attractive market to enter.

Market attractiveness

Brazil’s gross domestic product (GDP) declined by just 0.3% during the global economic crisis in 2009, and it is expected to rise by 5.8% in 2010. Its balance of payments deficit is less than 2% of GDP and its budget deficit, which stands at less than 4% of GDP, is very relatively low. Inflation also stands at a moderate level of 4.6% per annum, and short-term interest rates at 8.5% per annum are high enough to continue to keep inflation under control.
Developing a Market Entry Strategy for Brazil - 3

Given Brazil’s prominence on the international stage and strong underlying fundamentals, it is no surprise that many companies are considering expanding into the Brazilian market. Although the country presents many reasons that justify its position as a strong market, this entry does require research and planning. Whether you are considering acquisitions, making a greenfield investment or restructuring, you need to understand the strategic and financial impact of these decisions and the implementation risks. Understanding where the opportunities and risks lie, the size of each opportunity and what competitors are doing will arm you with the confidence to make a sound investment decision.

As many experienced investors in Brazil would say, the prospects are very attractive, but this diverse and dynamic market masks a minefield of complexity.

After a slightly decreased growth rate in 2009, Brazil’s GDP\(^{(a)}\) is forecast to resume steady growth and reach over R$1.18 trillion in 2012 at a 10-'12 CAGR of 4.6%.

The country’s population is expected to reach 197 million in 2010 with a steady annual growth rate of about 1.2% through 2014.

In line with this growth, personal disposable income is expected to grow at a rate of 1.5% and unemployment is expected to decline at a rate of 3%.

Private Consumption is expected to average 7.8% annually, outpacing expected inflation which is estimated to be 4% through 2014.

Market Entry

Given Brazil’s prominence on the international stage and strong underlying fundamentals, it is no surprise that many companies are considering expanding into the Brazilian market. Although the country presents many reasons that justify its position as a strong market, this entry does require research and planning. Whether you are considering acquisitions, making a greenfield investment or restructuring, you need to understand the strategic and financial impact of these decisions and the implementation risks. Understanding where the opportunities and risks lie, the size of each opportunity and what competitors are doing will arm you with the confidence to make a sound investment decision.
The Brazil commercial arena is changing rapidly due to the country’s increasingly competitive markets, as well as government initiatives. However, a number of potential target companies may lack reliable financial, tax, commercial and operational information as well as historical and forecast management reports, competitive intelligence, operational and market data may be untimely, inconsistent, inaccurate or simply nonexistent.

**Our approach to market entry**

KPMG in Brazil Market Entry service offerings focus on assisting international and domestic investors in developing an understanding of what it takes to succeed in a market. We study, in detail, the market size and growth potential, regulatory and competitive environment, key demand drivers and possible future developments, tax, legal and labor aspects which could be critical in the evaluation of an industry. We assess the attractiveness of the industry and evaluate whether the opportunity is realistic, as the client builds a strategy to enter or expand in the market using a structured, quantitative approach.

When well executed, new market entry is often the most controllable way for managers to drive corporate growth.

In considering the first steps into a new market, organizations have many issues to consider. Our team helps you identify which steps are the most critical, where the most significant risks could be and how to implement a plan both to take advantage of market opportunities while mitigating risks:

1. Identify the market - which markets, which segments, how to manage and implement marketing efforts, how to enter – through intermediaries, or directly, using what information?
2. Develop sourcing opportunities - whether to obtain products, make them or buy them?
3. Decide on the form of investment and control – joint venture, local partner, acquisition?
4. Determining how to operate in Brazil from a tax perspective – what are the most efficient structures, the key potential taxes, risks, opportunities involved, existing benefits and incentives?
5. Building or validating a business plan – how the business is likely to perform in the upcoming years? How the key commercial and operational drivers, external and internal factors will impact the business?
6. Evaluating where to establish the business (location assessment, site identification) - What locations (regions, cities) are more attractive? Within the selected locations, what are the sites (properties, land, buildings) that best fit the business needs?
To answer these questions, our team leverages a high level of local expertise, resources and networking capabilities in Brazil along with a broad range of external information resources to develop a comprehensive market entry plan.

Our talent pool of highly qualified professionals has always been our greatest strength. As a multi-disciplinary advisory firm, instead of just being specialists in one discipline, we encourage our people to cross into other functions to bring a more rounded and commercial approach to every assignment. This means, for instance, that our Market Entry teams don’t just think about strategy and deal resolution but about the post-integration of systems and cultures, tax, legal and labor aspects; they consider how internal audit will operate across a wider group; how risk can be effectively managed and reputations maintained and enhanced.

They have the know-how and experience to consider the big picture and, where appropriate, to call in more specialist expertise. Nothing is considered in isolation but in terms of how it will promote overall corporate well-being. For clients, this means that KPMG staff talk the whole story, not the abridged version. They take time to really understand your business and are plugged into the issues that make it tick.
Integration with other advisory teams
Multidisciplinary by essence, in the context of a market entry exercise, KPMG can provide accounting advisory services, tax structuring, due diligence assistance, integration and separations advice, business modeling, valuation services, negotiation support and deal management, assistance in restructuring processes, turnaround as well as debt advisory and fund raising.

Clients using our full range of advisory services benefit from improved efficiency of data gathering and communication as well as cross-fertilization between the teams, which allows us to offer you a better deal in relation to cost.

An example of a successful market entry exercise
Our client is a major diversified products manufacturer that was looking for opportunities to enter the Brazilian construction materials market. In order for it to formulate its market entry decision, the client was interested in gaining an understanding in three key areas for which KPMG’s assistance was requested: 1) market potential, 2) current customer perceptions and 3) competitive landscape and target identification.
Developing a Market Entry Strategy for Brazil - 7

Brazil Factsheet

Country Profile

Geography

Brazil is the fifth largest country in the world with a total area of 8.5 million square kilometers, covering approximately half of South America. Distances are continental: 4,420 kilometers from north to south, 4,328 kilometers from east to west, an Atlantic coastline of 7,367 kilometers and a total border of 23,102 kilometers. It neighbors every country in South America except Chile and Ecuador.

The country is divided into five regions:

- North - comprised mostly of the Amazon Basin; also consists of the states of Acre, Amazonas, Roraima, Rondônia, Pará, Amapá and Tocantins.
- Northeast – comprised of the states of Maranhão, Piauí, Ceará, Rio Grande do Norte, Paraíba, Pernambuco, Alagoas, Sergipe and Bahia.
- Central West – comprised of the states of Mato Grosso, Mato Grosso do Sul, Goiás and the Federal District.
- Southeast – comprised of the states of Minas Gerais, Espírito Santo, Rio de Janeiro and São Paulo.
- South – comprised of the states of Paraná, Santa Catarina and Rio Grande do Sul.

More than half of Brazil is 200 meters or more above sea level but only a small part rises above 1,000 meters, with the highest peaks reaching an altitude of around 3,000 meters. Brazil’s river system is extensive. The Amazon and its tributaries, which are great rivers in themselves, drain over half of Brazil. Other large rivers include the São Francisco in the northeast and the Paraná and the Paraguay Rivers, which flow south to empty into the Rio de La Plata. The considerable hydroelectric potential of Brazil’s rivers has been increasingly exploited over the last 35 years. Forests still cover vast expanses and farmland is found mainly in the South, Southeast and Central West with large areas suitable or adaptable for pasture. Brazil has some of the largest iron ore deposits in the world and mines significant quantities of many other metals, minerals and precious stones.

1. As a first step, KPMG performed an in-depth evaluation of the market size, the inherent growth opportunities in the immediate future and the relevant growth rivers in this geography.

2. Next, KPMG performed a broad industry and customer survey with interviewees ranging from subject matter experts such as market analysts and trade association leaders to industry participants such as contractors, architects, and building owners.

3. Lastly, KPMG extracted sensitive competitor information to generate an in-depth competitive landscape with rich company profiles via an extensive interview program of competing manufacturers that was subsequently validated through third-party research.
Climate
The equator runs just north of the Amazon while the Tropic of Capricorn passes slightly to the north of the city of São Paulo. This means that most of Brazil lies within the tropical zone. Only the southern region is in the temperate zone. The Amazon area is hot and humid with heavy rainfall.

Population
According to data published by the official statistics institute IBGE, Brazil had a population of approximately 197 million people in 2010 (161 million in 1996 and 170 million in 2000).

### Snapshot

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Size of the country</td>
<td>8,511,965 square kilometers</td>
</tr>
<tr>
<td>Population</td>
<td>197 million people in 2010</td>
</tr>
<tr>
<td>Capital</td>
<td>Brasília, Brazil</td>
</tr>
<tr>
<td>Currency</td>
<td>Real</td>
</tr>
<tr>
<td>Average exchange rate in 2009</td>
<td>US$ 1.74 = 1 Real</td>
</tr>
</tbody>
</table>

Source: The Economist Intelligence Unit, 2009 - 2010

### Ratings / Outlook

<table>
<thead>
<tr>
<th>Rating</th>
<th>Outlook</th>
</tr>
</thead>
<tbody>
<tr>
<td>EIU’s Sovereign Risk Rating (June 2010)</td>
<td>BB</td>
</tr>
<tr>
<td>Standard &amp; Poor’s Foreign Currency Risk Rating</td>
<td>BBB+</td>
</tr>
<tr>
<td>Ease of Doing Business Rank (2010)</td>
<td>129</td>
</tr>
<tr>
<td>Rigidity of Employment Index (2010)</td>
<td>46</td>
</tr>
</tbody>
</table>

Source: The Economist Intelligence Unit, The World Bank, Standard & Poor's Foreign Currency Risk Rating, 2010

### The relative areas and populations of the five regions described earlier according to the 2010 IBGE estimates were as follows.

<table>
<thead>
<tr>
<th>Region</th>
<th>Area</th>
<th>Population</th>
<th>GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>North</td>
<td>45%</td>
<td>8.16%</td>
<td>5.02%</td>
</tr>
<tr>
<td>Northeast</td>
<td>18%</td>
<td>27.50%</td>
<td>13.07%</td>
</tr>
<tr>
<td>Southeast</td>
<td>11%</td>
<td>42.58%</td>
<td>56.41%</td>
</tr>
<tr>
<td>South</td>
<td>7%</td>
<td>14.58%</td>
<td>16.64%</td>
</tr>
<tr>
<td>Central West</td>
<td>19%</td>
<td>7.17%</td>
<td>8.87%</td>
</tr>
</tbody>
</table>

Source: IBGE - Instituto Brasileiro de Geografia e Estatística, 2009

The North and Northeast are the underdeveloped regions of the country. Most industrial and commercial activities are concentrated in the South and Southeast regions. To reduce social tensions resulting from these regional inequalities in economic development, the government has allocated substantial resources, either directly or through tax incentives, to northern and northeastern economic development during the past forty years. Nevertheless, the practical result of this policy has been far less fruitful than expected.
Despite Brazil's vast territory, 80% of its population lives in urban areas (the metropolitan regions of São Paulo and Rio de Janeiro have populations of around 18 and 10 million respectively).

### The major capital cities of Brazil and related states by population, in accordance with the 2009 IBGE population estimates, are:

<table>
<thead>
<tr>
<th>Capital</th>
<th>Population</th>
<th>State</th>
<th>Population</th>
</tr>
</thead>
<tbody>
<tr>
<td>São Paulo</td>
<td>11.0</td>
<td>São Paulo</td>
<td>42.3</td>
</tr>
<tr>
<td>Rio de Janeiro</td>
<td>6.1</td>
<td>Rio de Janeiro</td>
<td>15.9</td>
</tr>
<tr>
<td>Salvador</td>
<td>2.9</td>
<td>Bahia</td>
<td>14.2</td>
</tr>
<tr>
<td>Belo Horizonte</td>
<td>2.4</td>
<td>Minas Gerais</td>
<td>19.9</td>
</tr>
<tr>
<td>Fortaleza</td>
<td>2.5</td>
<td>Ceará</td>
<td>8.4</td>
</tr>
<tr>
<td>Brasilia</td>
<td>2.6</td>
<td>Federal District</td>
<td>2.4</td>
</tr>
<tr>
<td>Curitiba</td>
<td>1.8</td>
<td>Paraná</td>
<td>10.6</td>
</tr>
<tr>
<td>Recife</td>
<td>1.5</td>
<td>Pernambuco</td>
<td>8.6</td>
</tr>
<tr>
<td>Porto Alegre</td>
<td>1.4</td>
<td>Rio Grande do Sul</td>
<td>11.2</td>
</tr>
</tbody>
</table>

(Source: IBGE - Instituto Brasileiro de Geografia e Estatística, 2009)

Over 50% of Brazilians are of first, second or third-generation foreign descent. The characteristics of various nations are apparent in the cosmopolitan makeup of the population. Portuguese, Native Brazilians and African influences become more evident towards the North, whereas Portuguese, German, Italian and Japanese influences are more apparent in the South.

### Language

Since the discovery and colonization of Brazil by Portugal, Portuguese has been Brazil’s language and Roman Catholicism the predominant religion. Brazil is the only Portuguese-speaking country in South America.

### Government

Brazil is a federal republic comprised of twenty-six states and the Federal District. Each state has its own constitution with a governor and state legislature. The states are divided into municipalities, which have some degree of autonomy, and these, in turn, are divided into districts.

The Federal Constitution provides that the executive branch of the federal government be headed by a president, elected by popular vote every four years. Legislative power is exercised by the National Congress, consisting of a Chamber of Deputies and the Federal Senate. Congress meets in the Federal District and capital, Brasília.

Judicial power is exercised by the Federal Supreme Court, the Superior Court of Justice, the Federal Court system as well as separate courts for military, electoral and labor matters. There is also a state court system with local jurisdiction. Private ownership of property is guaranteed, except when public interest or necessity justifies expropriation.

### Economy and fiscal policy

Government policy is focused on stimulating the business activities of the private and government sectors toward rapid industrialization and economic growth. However, this policy includes some protective measures for domestic industries considered to be of strategic economic importance, as well as monetary policies designed to keep inflation in check and maintain the availability of foreign exchange.

Today, Brazil is a world leader in the production of foods and minerals. Many other sectors - such as the steel, aluminum, automobile, aerospace, wood pulp, chemical and textile industries - are highly developed. Brazil’s GDP in 2009, was R$ 3.14 trillion (approximately US$ 1.80 trillion at the exchange rate in force on Dec 31, 2009).
The trade surplus for 2009 was US$ 25.3 billion. This surplus is basically attributed to the important number of export and import transactions, respectively, US$ 153.0 billion and US$ 127.7 billion. At the date of this publication, Brazil had more than enough foreign exchange and private credits abroad to settle all foreign public and private debt. No doubt this was important in Standard & Poor’s and Fitch Ratings’ decision to raise Brazil’s rating to “Investment Grade”.

### Key Indicators

<table>
<thead>
<tr>
<th></th>
<th>2010E*</th>
<th>2009</th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP (R$ billion)</td>
<td>3,461.4</td>
<td>3,143.0</td>
<td>3,004.9</td>
<td>2,661.3</td>
</tr>
<tr>
<td>Real GDP growth</td>
<td>7.8</td>
<td>-0.2</td>
<td>5.1</td>
<td>6.1</td>
</tr>
<tr>
<td>Unemployment rate</td>
<td>7.0</td>
<td>8.1</td>
<td>7.9</td>
<td>9.3</td>
</tr>
<tr>
<td>Consumer price index</td>
<td>5.4</td>
<td>4.9</td>
<td>5.7</td>
<td>3.6</td>
</tr>
<tr>
<td>Exchange Rate at Year end (Real / US$)</td>
<td>1.82</td>
<td>1.74</td>
<td>2.34</td>
<td>1.77</td>
</tr>
<tr>
<td>Total Public sector budget balance (% GDP)</td>
<td>-1.8</td>
<td>-3.3</td>
<td>-2.0</td>
<td>-2.8</td>
</tr>
<tr>
<td>Total Public sector debt (% GDP)</td>
<td>59.0</td>
<td>60.0</td>
<td>58.6</td>
<td>56.4</td>
</tr>
<tr>
<td>Goods exported (US$ billion fob)</td>
<td>178.2</td>
<td>153.0</td>
<td>197.9</td>
<td>160.6</td>
</tr>
<tr>
<td>Goods imported (US$ billion fob)</td>
<td>-171.7</td>
<td>127.7</td>
<td>173.1</td>
<td>120.6</td>
</tr>
<tr>
<td>Trade balance (US$ billion)</td>
<td>6.5</td>
<td>25.3</td>
<td>24.8</td>
<td>40.0</td>
</tr>
<tr>
<td>Current account balance (US$ billion)</td>
<td>-52.3</td>
<td>-24.3</td>
<td>-28.2</td>
<td>1.6</td>
</tr>
<tr>
<td>International reserves (US$ million)</td>
<td>NA</td>
<td>238,520</td>
<td>193,783</td>
<td>180,334</td>
</tr>
<tr>
<td>Inward direct investment (US$ billion)</td>
<td>30.0</td>
<td>25.9</td>
<td>45.1</td>
<td>34.6</td>
</tr>
<tr>
<td>Total external debt (US$ billion)</td>
<td>308.5</td>
<td>279.8</td>
<td>253.4</td>
<td>237.5</td>
</tr>
</tbody>
</table>

Source: The Economist Intelligence Unit, Banco Central do Brasil, 2010

*Estimate

### Key considerations when investing in Brazil

#### Strengths

- Brazil is the fifth most populous country after China, India, the United States and Indonesia.
- Consistent economic growth and governmental policies have boosted a solid enlargement of a middle class avid for durables goods and consumer products.
- The tenth largest economy (eighth in terms of purchasing power).
- Brazil’s diverse economy is characterized by well developed agricultural, mining, manufacturing and service sectors.
- There is increased globalization where the Brazilian government policies favor exports.
- A diverse economy offers many investment opportunities in several segments in manufacturing and services industries.
- All three ratings agencies classify Brazil’s government paper as investment grade.
- Inflation has been under control for over 10 years.
- Brazil is a self-sufficient nation in terms of oil and with new off-shore discoveries, is likely to be an oil exporter by the end of the next decade.
- Consolidated democracy, established institutions and enforced financial discipline – all state governments are required to run a primary surplus (before interest payments on public debt).
- More business friendly environment than other emerging countries.
- Established transportation networks and distribution channels in most industrialized areas.
- Two major sports events (2014 FIFA World Cup and 2016 Rio Summer Olympics) are likely to drive massive investments in infrastructure.

#### Challenges

- There is a large disparity in distribution of wealth.
- Productivity growth in the country is sluggish.
- Many of Brazil’s sectors are still highly guarded with protectionist import taxes.
- Natural targets, such as the family-owned businesses, often make use of aggressive tax schemes at the same time they lack on adequate corporate governance and financial reporting.
- Central bank’s headline interest rate is one of the highest real rates anywhere.
- Deep water drilling (pre-salt) requires high level of expertise, particularly with regards to environmental risks and technology to make it cost efficient and competitive.
- Transparency is sometimes lacking and corruption seems to be more apparent in government than in other developed nations.
- Complex tax and labor regulatory environment with high taxes and social charges on payroll.
- Considerable bureaucratic rules for certain businesses and industries.
- Infrastructure investment is still lacking.
Interested in expanding business in Brazil and/or penetrating new regions and markets?
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