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## INVESTMENT NOTE

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### **Hermes: Silva brings reform hopes to Brazil investors**

*The new leader of Brazil's socialist party is rallying opposition against the incumbent government and stoking the nation's desire for reform, says Gary Greenberg, Head of Hermes Global Emerging Markets.*

#### **Vale Eduardo Campos**

Since the socialist PSB party's presidential candidate Eduardo Campos was tragically killed in an aeroplane crash last Wednesday, the political outlook for Brazil has taken a new turn. Campos only had about 10% of votes in the last poll, lagging the social democrat PSDB party candidate Aécio Neves by 10% and current president Dilma Rousseff, of the PT workers' party, who had over 30% of the votes. The new twist in the story is the rise of Marina Silva, the most likely replacement for Eduardo Campos, who is expected to be confirmed as leader this Wednesday.

#### **Enter Marina Silva**

Silva joined the PSB socialist party late last year when she failed to raise enough necessary signatures to register her own political party. However when she ran as the PV green party's presidential candidate in 2010, she won nearly 20% of the vote. The Brazilian market rallied on Friday on speculation that Silva would attract enough opposition votes to provoke a second round in the elections.

Her popularity was shown by a Datafolha poll on Monday morning showing that if Silva replaced Eduardo Campos she would win 47% of the votes, beating Rousseff's 43% in a run-off. In the first round, Silva would have received 21% of the votes, while Rousseff would have 36% and Neves 20%. Also, Silva's rejection rate came in at 11% versus 18% for Neves and 37% for Rousseff.

#### **Pragmatic idealist**

Silva is like Lula, the popular ex-president of the PT party: idealistic, charismatic, and from a poor background, but she has recruited an economic team that is more in line with Neves' market-friendly PSDB party. This attractive combination is what drew not only 'undecided' voters to vote for her but also PT supporters that want to continue spending on social programmes but with more prudent fiscal management.

There are also reports that Beto Albuquerque, the Congressman of Rio Grande do Sul, will run as Marina's vice president. He is from the south of Brazil whereas Marina is from the north, which not only widens the national appeal of the PSB party but also threatens the PT party's southern stronghold.

#### **'Anyone but Dilma'**

Silva has a decent chance of making it to the second round against Rousseff, where polls imply she could win the elections. Even if Neves makes the second round instead of her, we expect her voters will vote for Neves as 'anyone but Dilma' sentiment has gained traction as a theme. Thus there is now a good chance that Dilma will not win the elections which we believe would be positive for the Brazilian market.

#### **No radicalism**

Initially concerned that Silva, a staunch environmental activist, would implement policies that would adversely affect business, the market sold off. However it now appears unlikely that Silva will be anti-business – and even if she wanted to, she will not find it easy to make radical changes to the pro-market policies that have been presented by Eduardo Campos. It is fair to

assume she may target businesses with a high environmental impact through tighter environmental standards, taxes and fines. But on the other hand, she has shown support for the country's biofuel industry (we own shares in Cosan, a leading ethanol refiner with operations in Latin America and the UK) and has stated that the country's growing oil industry is a "necessary evil".

### **Silva lining**

The Brazilian market has been under a cloud for several years, appropriately, due to an interventionist administration which has been unable to resist using the private sector to facilitate government policy goals. The prospect of a reformist government, distant at present, would take the market to new heights. Currently, markets are relieved by the possibility of a more *laissez-faire* approach, which in the case of our holdings (Petrobras, Cosan, and Itaú Unibanco), should mean better valuations over time.

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### **Notes to Editors:**

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- **Responsibility:** We believe it is our responsibility to lead discussion and debate about the fiduciary responsibilities of fund managers to our clients, their stakeholders and, ultimately, society at large. We have always sought positive engagement with the firms in which we invest.
- **Innovation:** We have the entrepreneurial culture to identify forward-looking products that meet those needs, along with the resources and speed-to-market mentality to develop them rapidly.

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