

ENGAGING BRAZIL IN THE ERA OF CLIMATE ACTION

CAN EUROPE AND THE UNITED STATES DEVISE A NEW GLOBALISATION?

Lauri Tägtinen



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- Increased deforestation in the Amazon is the outcome of Brazil's long political crisis. What started in 2013 with a bus fare hike has traversed through contestable impeachment and populist uprising into a constitutional stalemate.
- European institutional investors have been in the vanguard of checking Brasília's lax approach to deforestation and other environmental challenges. While investors continue to carry a big stick, European and US political leadership should consider what carrots they can offer Brasília.
- Brussels and Washington have changed course rapidly from an approach that emphasised closer ties with Brasília to one of dissatisfaction and distancing. This is both a cause and an effect of Brazil's international standing diminishing both in terms of economy and country brand.
- In recent years, Brazil has simultaneously tried to raze more rainforest and build North Atlantic trading relations; the two cannot be done at the same time.
- A politics of rapprochement with Brazil requires much closer coordination between Europe and the United States than the parties are accustomed to; a commitment to a climate-sensitive globalisation is necessary from Brasília.



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INTRODUCTION: BRAZIL ON A DOWNWARD SLOPE

Many a Brazilian will tell you that the outside world's interest in their country tends to be cyclical: moments of intense scrutiny are followed by neglect. Some countries, such as larger European ones, tend to enjoy a steadier international focus, even if nothing compares to the constant attention given to the United States. Brazil is given more thought than the vast majority of the world's countries, yet it is given sporadically. A boom and bust cycle seems to remain Brazil's fate.

Over the past few years, Brazil has been undergoing some increased scrutiny due to a cascade of spectacular events. A political crisis that began with a transit fare hike in 2013 led to the impeachment of President Dilma Rousseff in 2016, the 2018 imprisonment — and later release — of former President Luiz Inácio Lula da Silva, and culminated in the right-populist President Jair Bolsonaro.¹ Bolsonaro's inauguration on 1 January 2019 also augured a particularly difficult time for Brazil's Amazon rainforest whose deforestation rates had already been climbing during the descent into political crisis.

Now, in the rainforest's third burning season (during the northern hemisphere's summer and autumn) of the Bolsonaro presidency, the Amazon's fate has received less attention for four reasons. The first, a positive note, is that for the year ending 31 July, the Bolsonaro administration is recording its first reduction in deforestation.² The second, a relatively neutral factor, is that the world may be becoming tired of tracking the Bolsonaro presidency and its many travails, including the constitutional stalemate at which Brazil appears to have arrived. The third, a negative but unrelated element, is how the twentieth anniversary of September 11 and associated decisions have sucked the oxygen out of other global politics. The fourth, a negative but profoundly related reason, is that, in recent months, the world has been witnessing so many spectacular climate change-driven upheavals that less media oxygen has been left over for the Amazon rainforest and its fate.

This Briefing Paper assesses Brazil's North Atlantic relations at a moment when the ocean is already widening, and Brazil is becoming distanced from both Europe and the United States. It takes the measure of this moment, of the events leading to it, and the prospects for the near future. To borrow from a long line of social theory, the superstructure of Brazilian environmental practice requires an analysis of the base of ongoing globalisation, particularly the reshaping of global finance in the age of climate change and pandemic.

In this setting, Washington and Brussels find themselves both unleashing some of these forces, while simultaneously having to play catch up. This is especially the case with the activists, investors, and activist investors who have been rhetorically and regulatorily summoned by politicians to act on the environment. By doing so, these actors have sometimes caught the very same politicians flat-footed, as investors have advocated precisely the things that their regulators expect them to prioritise.

First, this paper assesses why and how European, as well as US institutional investors and fund managers, are formulating policy for Brasília, practising geofinancial statecraft. The second issue examined is how Europe and the United States have engaged Brazil on trade, practising geoeconomic statecraft. The third perspective considered is Brasília's outlook on the Amazon and the country's relations with the outside world, or how Brazil practises its geopolitical statecraft. Finally, the paper establishes a clear need for a more consistent and shared Brazil policy from Brussels and Washington, not least due to the challenge posed by China.

GEOFINANCIAL STATECRAFT AT BRASÍLIA

Two secular investing trends are on a collision course, and Brazil lies at the point of impact. In 2019, US index funds overtook active funds for the first time, 45 years after their inception. Such funds were understood to democratise investing by allowing amateurs to track past performance instead of trying to outperform the market — whether by directly picking one's own stocks or paying a fund manager to do so.

¹ A brand new extensive account of Brazil's crisis is available in Richard Lapper, *Beef, Bible and Bullets: Brazil in the Age of Bolsonaro* (Manchester: Manchester University Press, 2021).

² "Amazon forest loss hits second highest level since 2008", *Mongabay*, <https://news.mongabay.com/2021/08/amazon-forest-loss-hits-second-highest-level-since-2008/>.

The problem with tracking a previous record is that you end up doubling down on the good, the bad and the ugly. Past performance may not only fail to be a guarantee of future performance, it may also have been attained through means that are now considered unacceptable or, in some cases, outright criminal. This is especially the case with the environmental impact of business.

Pure index investing meant that there was little distinction between the “is”, or “was”, and the “ought”. A new secular investing trend focuses on how the world ought to be. While Socially Responsible Investing (SRI) has been around for decades, it remained a limited phenomenon, even in the US where it did attract some enthusiasts.

Since the dawn of the new millennium, a much more potent force has emerged and, this time, primarily in Europe: Environmental, Social and Governance (ESG) investing. Investors began not simply to screen for ESG harms committed but sought to understand which companies or sectors were best prepared for the world of the twenty-first century. In this line of thought, it is not merely ethically correct to attempt to mitigate against climate change, but necessary for an organisation to remain competitive or even in existence. Moreover, the first year of Covid-19 demonstrated how sustainability had come of age; ESG funds beat out the S&P 500, a benchmark index.³

The immediate moral of these two investing stories is that financial professionals see in ESG the answer to the income lost to index-tied funds. Investors are happy to pay fund managers to do better in at least two ways: first, they want to change the world according to their values, not simply to track past performance; second, they believe that future financial performance depends on adhering to ESG standards. To earn their keep, fund managers and a slew of other financial professionals assess which stocks, sectors, or geographies contain ESG shortcomings or risks.

This is the point at which Brazil enters the picture. The country’s political crisis happened to fuel Amazonian deforestation exactly at the moment when, especially, European fund managers needed a new public enemy number one or, less poetically, an exemplary target of ESG divestment. Understandably, it is compelling to introduce a new policy emphasis with a teachable moment.

The European Green Deal, an effort launched in late 2019 and early 2020, is predicated on sustainable finance pushing change not only within the EU but around the world. As part of these efforts, financial services need to adopt climate benchmarks and provide sustainability-focused disclosure. Such requirements formed a tidal wave that, for a moment, looked like it might have swallowed Brazil or, at least, have created a riptide that would pull the country’s business and governing class into open sea without a life raft. In the most spectacular example, during the northern hemisphere summer of 2020, a coalition of institutional investors with \$4.6 trillion in assets, led by Nordic household brand names, went directly to the Brazilian government with their demands.⁴

As a result of the first high-level meeting, the Brazilian government instituted a temporary fire ban, but the coalition wanted more. The investors laid out a set of areas in which they would keep an eye on Brazil, including not only deforestation and forest fire prevention but also the broader enforcement of Brazil’s Forest Code, the strengthening of environmental and human rights agencies, as well as a renewed focus on traceability and transparency. This set of investors made it plain that, for example, the health of Brazil’s sovereign debt is deeply integrated with the sustainability of the country’s policies.

Once Brazil risked becoming a financial pariah, it was also the business elites in São Paulo who quickly moved to lobby Brasília for policies that matched the expectations of not only European or, say, Canadian, but increasingly US investors as well. While Europe receives almost twice the number of Brazilian exports, and the US is mostly Brazil’s direct competitor in the agricultural sector, it is US finance that is deeply intertwined with Brazil. The annual US direct investment in Brazil had reached over 80 billion USD in 2019, although the indirect impact of US finance is much greater in Brazil’s trillion-dollar asset market and overseas holdings.

As major stateside asset managers — including the world’s largest private ones — have fallen in line with sustainability, we have witnessed sights that until recently would have been unbelievable. In August 2021, Brazil-based JBS, the world’s largest meat company, joined the Race to Zero, the United Nations-sponsored carbon reduction programme. Yet the pressure remains strong for the aforementioned coalition of investors, now grown to \$7 trillion in assets under management,

3 Esther Whieldon and Robert Clark, “ESG funds beat out S&P 500 in 1st year of Covid 19”, S&P Global Market Intelligence, 22 July 2021, <https://www.spglobal.com/marketintelligence/en/news-insights/blog/corporate-credit-risk-macro-economic-recovery-projections-post-covid-19>.

4 Alexandra Pinzon, Nick Robins and Gabriel Thoumi, “Ending deforestation: what next for sovereign investors?”, 22 July 2020, <https://www.lse.ac.uk/granthaminstitute/news/ending-deforestation-what-next-for-sovereign-investors/>.

to make Brazil “pay for not halting deforestation”. That was the exhortation delivered by the *Financial Times* editorial board in mid-July, opening with a restatement of the, by now, broadly shared belief: “Investor activism can be a powerful force for good”.⁵

GEOECONOMIC STATECRAFT WITH BRASÍLIA

It is not exactly novel for multinational companies to be associated with the actions of their home nations. In one infamous example, energy companies from the countries which made up the Coalition of the Willing that invaded Iraq in 2003 found their way to the regime-changed country. In that case the nation-states acted first, and the actions of the corporations could be seen as following those of their home countries.

In the case of Brazil and geofinancial statecraft, EU-level regulation had been passed but it had not spread into the many limbs of the European body politic. The 2019 halting of Norwegian or German governmental contributions to the Amazon Fund may have paved the way for later action, but in 2020 that road was travelled by a much larger convoy of concerned parties. It was the investors who moved en masse and also helped force a change in the geoeconomic statecraft employed by their home countries and the EU.

The extent of the shift in EU and US policy becomes apparent when one looks at the recent history of their relations with Brazil. In June 2019, a quarter century of negotiations appeared to have arrived at a conclusion when the EU signed a trade deal with Mercosur, a South American trade bloc of which Brazil makes up the lion's share. Even more recently, in October 2020, the US and Brazil inked a trade facilitation agreement with the understanding that more would follow.

However, as we have seen, darker clouds had already appeared on the horizon, as trade policy with Brazil became a partisan affair in Washington with a campaign-trail Biden threatening Brazil with “significant economic consequences”. Meanwhile, Brussels is demanding new “meaningful” commitments on deforestation and climate change, nominally from all Mercosur countries but, in reality, primarily from Brazil. Major policy change often engenders an exemplary case, one that encapsulates the priorities of the emerging agenda and makes them more visible and obvious to the wider world. Brazil has become such an example.

Many long-term Brazil watchers, and some Brazilians themselves, have noted a shift in public sentiment towards the country. Brazil now elicits strong, unsolicited negative reactions from people beyond its borders. This is a marked change from not only the “Lula mania” of the first decade of this century, when the president was a coveted partner for photo ops with other world leaders, but also from a longer-term positive image.

Despite its infamous inequality and notorious lawlessness, Brazil managed to build fame on its claim to racial democracy, an early commitment to greener energy, and its avowal to emerge as the country of the future. In the past century, this Brazilian brand was built through both democracy and dictatorship, but it is now being bulldozed by demagoguery. The bulldozer-in-chief has built global name recognition for his lax enforcement of environmental law, lackadaisical handling of Covid-19, and lousy political table manners, including outbursts in defence of Donald Trump's challenge to US democracy.

Although Bolsonaro has certainly made himself the star of his country's show, he also arrived on the scene at a time of already rising deforestation and heightened climate change awareness. The year 2021 has lifted climate change to the top of the global agenda, notably due to the change of occupancy at 1600 Pennsylvania Avenue NW in Washington, DC. As President Biden continues to re-imagine the US climate stance, the priorities of other policy areas are being reshaped, as witnessed in the recent infrastructure bill.

Another such area is trade, whose globalisation was for several decades promoted and celebrated as a matter of US and EU policy with little regard for its climate impact at home or abroad. This attitude is now subject to a radical rethinking in Washington and in Brussels, where the EU has unveiled its new trade strategy focused on multilateral action against climate policy. With Brazil already in the crosshairs of institutional investors from the North Atlantic, Brasília can scarcely afford to alienate its counterparts in Brussels and Washington.

This does not mean that Bolsonaro will not try, as his recent escalation shows. In early September, following a prolonged struggle between the president and Brazil's judiciary and legislature, Bolsonaro declared that he would no longer respect Supreme Court decisions, or leave the presidential office alive. Although the president was forced into a tactical retreat, he remains strong enough to stay in power, causing a “permanent constitutional crisis”.⁶ This is a terrible state

5 “Brazil should pay for not halting deforestation”, *The Financial Times*, 14 July 2021, <https://www.ft.com/content/3dd66868-3dec-4d3b-b428-10f4e9d9308d>.

6 Oliver Stuenkel, “Stalemate: The Main Outcome of Bolsonaro's Day of Protest”, *Americas Quarterly*, 8 September 2021, <https://www.americasquarterly.org/article/stalemate-the-main-outcome-of-bolsonaros-day-of-protest/>.



Brazilian President Jair Bolsonaro greeted his supporters by Palácio do Planalto, the official workplace of the President, in September 2021.
Source: Marcos Corrêa/PR (CC BY 2.0)

of affairs for Brazilians, but also has diminishing shock value for the outside world.

The country is simply not what it once appeared to have become. In 2011, it claimed to have become the world's fifth largest economy; ten years later, it is struggling to remain the world's 12th largest in 2021. A decade ago, it was a question of possibly overtaking France, a major cultural influence, as well as the UK, a country that had lorded over Brazil's 19th century trade. Now, it is a matter of possibly falling behind a former British colony heavily invested in extraction and primary production; to make matters worse, Australia has a mere eighth of Brazil's population. The wind is decidedly out of Brazil's sails.

GEOPOLITICAL STATECRAFT IN BRASÍLIA

The distance by plane from Miami to Manaus, Brazil's seventh largest city and the economic heart of its Amazon, is shorter than the overland trip from São Paulo to the state capital of Amazonas. To make Manaus even more distant, the last 885 kilometres from Porto Velho, the capital of Rondônia state, are, in

parts, barely passable at a better time of the year and impassable during the rainy season.⁷

Without a functional road, Manaus can only be reached by river boat or airplane. After being abandoned at re-democratization in 1988, in recent years the Porto Velho—Manaus Highway BR-319 has been undergoing “maintenance”, to use governmental language or, according to critics, “re-construction”. In early 2021, the Brazilian government requested proposals for the paving of over 400 kilometres of the highway and, by doing so, providing increased access to virgin rainforest.

While the Amazon is distant to most Brazilians with economic and even political might, the fires of 2019 brought home what it is like to live under smoke, especially in a megacity such as São Paulo. Similarly, in 2021, the extreme drought in Brazil's southern economic heartland is showing the impact of deforestation in ecosystems far removed from the Amazon basin, which is no longer a distant frontier that can be safely ignored.

In the past, Highway BR-319, a lightning rod since its inception, could be seen as a distant symbol of Brazil's development. Order and progress, the emblematic

⁷ Ana Ivanova, “Illegal deforestation intensifies along Brazilian highway as agribusiness hopes swell”, *Mongabay*, 23 July 2021, <https://news.mongabay.com/2021/07/illegal-deforestation-intensifies-along-brazilian-highway-as-agribusiness-hopes-swell/>.

pairing on Brazil's flag, depended on occupying the Amazon in order not to surrender it. Half a century ago, this made the future of the Amazon a national security question of the highest order for the military regime ruling Brazil. While such questions never disappeared from Brazilian political discourse, Bolsonaro has brought them back with full force.

Even if Bolsonaro has made matters worse for the rainforest, deforestation is part of the long political crisis that Brazil has undergone since 2013. A year earlier, in 2012, Brazil had been able to cut official Amazonian deforestation rates by 84% from the peak of 2004. This meant a reduction from almost 28,000 km² (practically a "Belgium") to below 5,000 km² (or less than two "Luxembourgs"). In 2020, the official loss was around 11,000km² — approximately a "Kosovo".

The reversal is certainly bad news, but the good and even better pieces of news are that things have been worse, and that Brazil has demonstrated in the past that it can change course. Both the problems and solutions for Brazil's deforestation or environmental agendas reach beyond Bolsonaro's persona or policies. That is an important lesson to keep in mind as the 2022 Brazilian general election promises to become highly combustible, especially against the backdrop of forest fires. Both Bolsonaro and, presumably, Lula have their reasons to call out northern imperialism.

The first thing that Europeans in particular need to appreciate is how the Brazilian sense of sovereignty is at least as strong and dense as that of US elites. Whenever a Brazilian president is able to find an Emmanuel Macron to speak out against, as happened in 2019, they will be able to rally citizens around the flag. This is not an aspect peculiar to Bolsonaro's populism but a near universal in Brasília, and powerful elsewhere in the country. In this vein, the Amazon basin remains the litmus test for sovereignty elsewhere. If Brazil can remain sovereign over the Amazon, against threats to "internationalise" its status, the rest of Brazil will also fare well.

To some outsiders, this may be a difficult worldview to approximate. The worldview and its unfamiliarity have to do with Brazil remaining a largely closed economy and, in some ways, society. In late 2018, Bolsonaro ran on an agenda of both domestic (uncontrolled) agricultural expansion and (controlled) liberalisation of foreign trade, bucking global trends towards sustainability and protectionism in both instances. By late 2019, it had become clear that at least one part of that twin agenda would have to give. In

2020, Covid upset the hopes for global trade expansion and drew further attention to deforestation and zoonotic disease, while Brazil's disastrous handling of the spread of the novel coronavirus brought it further unwanted attention.

This year has seen two reversals: first, the Brazilian government has been backpedalling its (anti-) environmental policies and, second, globalisation is swinging back in ways that few would have predicted a year ago. In the United States, in particular, trade came back in dramatic fashion with the spring months delivering three out of the four strongest months in history, in nominal terms. This speaks to a growing realization that humans desperately need trade, as it makes us more resilient and capable of dealing with global challenges such as the Covid-19 health crisis or climate change. It also suggests that a new globalisation is waiting in the wings.

Indeed, as economic historian Harold James argues, the Covid crisis may well deliver a "Golden Age" of globalisation, reducing the inflation that our recoveries are driving not only in traditional zones of inflationary pressure such as Brazil, but also in the United States.⁸ After all, the long era of low inflation has also been an era of increasing global integration.

Against such a backdrop, Brazil could do worse than to seek further integration at a moment when globalisation is being re-ordered, in more than one sense. Some of the recently proposed measures to control more freewheeling jurisdictions, such as the imposition of a global minimum tax rate, may actually help Brazil play on a level field as it opens up to the world. However, in order for Brazil to reap the benefits of novel arrangements, it must accept once and for all that its further integration is predicated on being a positive force in the fight against climate change and for environmental preservation.

CONCLUSIONS: ENGAGING BRASÍLIA?

In recent history, Europe and the US have been travelling on separate tracks towards — and away from — Brazil; this needs to change. Washington has emphasised the defence relationship with Brazil and has preferred to keep Europeans out of questions of New World security. Unfortunately, Washington has also been attached to a rather mercantilist outlook, due not least to the fact

8 Harold James, "Globalization's Coming Golden Age: Why Crisis Ends in Connection", *Foreign Affairs*, May/June 2021, <https://www.foreignaffairs.com/articles/united-states/2021-04-20/globalizations-coming-golden-age>.

that Brazil exports many of the same products, such as soy, beef and ethanol, as the United States.

Meanwhile, Brussels has focused on getting a trade deal through, while not fully appreciating the security and environmental aspects of Chinese involvement in Brazil and its neighbourhood. Tragically, Brazil and the EU spent the best years of the old globalisation consensus trying to get a trade deal done, only to cross the line moments too late. The EU should now seek paths out of today's impasse, for example with a Mercosur–EU pilot of digital product passports for the tracking and tracing of goods.⁹

Both Europeans and Americans need to come to see their relationship with Brazil holistically in terms of both trade and security and, by doing so, also engage Brasília on the environment. North Atlantic governments should, at least, be aware of the impact of the public and private diplomacy of investment funds as their advocacy has many public nexus points. If anything, with investors playing bad cop, the situation should provide ample opportunity for governments to provide some balance with a good cop act.

Making the situation even more complicated is the EU's new commitment to impose tariffs on carbon-intensive products arriving in its internal market, a reality to which not only Brazil but most other countries will have to quickly adjust. Meanwhile, the Biden administration is looking to increase pressure on Brazil to act on the environment, but without pushing Brasília into a rival's arms: to simultaneously distance itself from Bolsonaro but move closer to Brasília.¹⁰

The broader context of US and European engagement with Brazil is provided by the Great Game with China. Brazil already exports more to China than to the EU and US combined, and the exigencies of both Covid-19 and climate work suggest that this trend should only strengthen. For example, if Europeans sanction Brazilian agricultural products, Brazil will look more exclusively to China, where fewer tend to care how many trees have been felled for their meat.¹¹

Similarly, if Brazil were to shun Chinese 5G — to follow Washington's preferences this late in the game — China may well refuse to buy soy from Brazil, and the United States would stand to benefit instead.

Yet such a scenario is unlikely because, in early 2021, Brazil already allowed Huawei participation in its 5G bids, just as Sinovac vaccines started flowing into the country.

As Brussels and Washington become further alienated from Brasília, Beijing stands to benefit. Chinese delegations can receive quite the welcome; recently, Lula has praised the Communist Party of China for its strong leadership on Covid. China will also not require Nordic levels of compliance from Brazilian production processes. Such a conglomeration of forces promises to become a tragedy for the world, with the Amazon rain-forest already at a tipping point at which deforestation is becoming a self-reinforcing process. As that happens, the climate work of the rest of the world becomes increasingly futile.

Thus, the only way forward is tough-minded engagement. We know that Brazil can change course because it has done so before. Potential divestments and other “sticks” have already been introduced; we need to quickly start thinking of possible “carrots”.

It will be an uphill battle. While Bolsonaro becomes increasingly erratic, he is likely to face a corruption-stained and prison-hardened Lula, whose scepticism of the “blue-eyed white people” of North America and Europe is a matter of public record from the time of the 2009 financial crisis during his previous presidency.¹² Friends of Brazil need to become more determined, and work on forming North Atlantic ties with Brazil that carry over from one administration to another without assuming any easy fixes from the general election of late 2022.

For their own well-being, Brazilians should be engaged in processes that foster broader Atlantic integration, their country's societal and economic development, and new emphases on sustainability. Due to China's growing counterweight, it is imperative that Europeans and Americans act together, forming at least trilateral forums for conversation and cooperation. They are already starting from behind; the North Atlantic cannot take turns preaching southward. Instead, for the sake of our planet, it should address Brazil together, engage it in open dialogue, and breathe air into a new globalisation. /

9 Annika Hedberg and Stefan Sipka, “Towards a green, competitive and resilient EU economy: How can digitalization help?”, EPC Discussion Paper, 13 July 2020, <https://www.epc.eu/en/Publications/Towards-a-green-competitive-and-resilient-EU-economy-How-can-digital-35bfc4>.

10 Brian Winter, “The Silent Partner”, *Piauí*, September 2021, <https://piaui.folha.uol.com.br/materia/the-silent-partner/>.

11 Lauri Tähminen, “Only China Can End Brazil's Climate Crisis”, *Foreign Policy*, 1 July 2021, <https://foreignpolicy.com/2021/07/01/brazil-deforestation-china-amazon-climate-change/>.

12 On Lula's recent and past stances, see: “Lula elogia Partido Comunista Chinês: ‘Países deveriam aprender’”, *Poder360*, 28 June 2021, <https://www.poder360.com.br/brasil/lula-elogia-partido-comunista-chines-paises-deveriam-aprender/> and “Brazil's Lula repeats ‘blue eyes’ crisis comment”, *Reuters*, 15 April 2009, <https://www.reuters.com/article/uk-financial-lula-blueeyes-sb/brazil-lula-repeats-blue-eyes-crisis-comment-idUKTRE53E76B20090415>.