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WORLD

# Brazil's Woes Multiply as Manufacturers Move to Paraguay

Paraguay has attracted scores of foreign factories, as predominantly Brazilian companies respond to new incentives by flocking there to make everything from toys to motor scooters.

*By Jeffrey T. Lewis*

CIUDAD del ESTE, Paraguay—This remote South American country, long known for contraband traffickers and a 35-year dictatorship, is now becoming something else: a manufacturing hub.Paraguay has attracted scores of foreign factories since 2013, as predominantly Brazilian companies respond to new incentives by flocking to this gritty border city to make everything from toys to motor scooters for export.

Koumei SA, a family-run Brazilian light-fixtures company, is typical. Its owners moved the plant and about 150 jobs here last year, saying they were fed up with Brazil's high taxes and complicated labor rules.

"It's just easier here," Seijii Abe, who directs the company with his father.

The shift from Brazil comes as Latin Americas's biggest country is trying to stabilize an economy that has contracted 7.2% in the past three years. A series of corruption scandals has also roiled the political class, leaving Brazilian President Michel Temer in a tenuous position as he tries to revamp the economy.

Brazil ranked 123rd out of 190 in the World Bank's 2017 survey on ease of doing business, right behind Uganda and Egypt. Companies there say they are bedeviled by rules that smother entrepreneurial impetus. They point to labor regulations that make hiring and firing difficult, high energy bills, a legal system that encourages employee lawsuits and taxes of up to 35% on imported goods."The regulations are absurd," said João Carlos Komuchena, owner of Kompar SA, a company which makes small plastic bottles used for packing soy sauce and other products that moved to Paraguay from Brazil last year. "We need to wake up in Brazil; there is a lot of prejudice against business."

Enter Paraguay. The poor, landlocked country, ruled until 1989 by dictator Alfredo Stroessner, was long known for corruption, violent crime and drugs, tobacco and armaments smuggling, as well as its commodity agricultural exports. Paraguay began trying to attract manufacturers in 2000 with a series of incentives President Horacio Cartes has hawked enthusiastically since he took office in 2013.Paraguay's sales pitch to manufacturers: cheap electricity, less onerous labor rules, zero import taxes and only a 1% levy on the value of finished exported products. So far, 115 factories have opened up in Paraguay under the so-called maquila program, 89 of them since 2013, with another 20 preparing to start operations, the government says.

"Paraguay is the least developed country in Mercosur, we need to industrialize if we want to catch up," said Industry Minister Gustavo Leite, speaking of the trade union in South America of which Paraguay is a member. "Our obsession is jobs."

To be sure, Brazil, with thousands of factories and 65 times the economic power of tiny Paraguay, still dwarfs its neighbor. But for a small, landlocked country of nearly seven million people the shift is significant, not least for the 13,000 people employed directly by the factories.

Maida Soto, 23 years old, is among those benefiting from a Paraguayan factory job in a Brazilian-owned plant, allowing her to continue her nursing studies while providing her with enough of a salary to buy a motor scooter.

"The work conditions here are better" than in the hospital where she previously worked, she said, taking a break from drilling holes in a lighting fixture at the Koumei plant. "I have more money and more time."

The Paraguayan cities profiting most from the influx of foreign manufacturers are Ciudad del Este and nearby Hernandarias—scrappy border outposts on the mighty

Paraná River long known for their bustling contraband trade. Now, factories hum at industrial parks and trucks haul finished components along clogged highways into Brazil and elsewhere abroad.

One company that moved here to Ciudad del Este, toy-maker X-Plast SA, employed about 20 people to handle accounting in Brazil. In Paraguay it uses only five.

“It’s both the complexity and the cost,” said Cainã Chen, vice president of X-Plast, adding that up to 40% of the cost of producing a toy in Brazil was attributable to taxes.

Koumei, the lighting fixtures maker, turned to Paraguay after it was outbid by a Chinese rival for a contract to supply office lighting because of what it said were Brazil’s high costs. Seiji Abe, the owner’s son, found out that an expensive brand of soccer jerseys were made cheaply in Ciudad del Este.

“I never would have thought of Paraguay because of its reputation,” Mr. Abe said. But the low costs “really opened our eyes,” he said.

Brazil’s government acknowledges the flow of manufacturing investment into Paraguay and agrees that it is a result of the red tape, bureaucracy and taxes that Mr. Temer’s administration is trying to overhaul.

Finance Minister Henrique Meirelles said the administration wants to change bankruptcy law, simplify the tax system and reduce the cost of credit. But the unpopular government doesn’t have broad backing for its efforts and has put in place only 12 of 213 proposed business reforms since taking office last year, Mr. Temer’s office said.

Those companies that have moved to Paraguay aren’t looking back.

Hipasa SA, which used to make diapers in Brazil’s south, said it left because bigger competitors were beating them on price. It now has a plant near the Paraguayan capital of Asunción, where it produces more cheaply than in Brazil and makes a bigger profit, said the company’s president, Marcos Gomes.

“There’s a series of costs that we can eliminate, we’re much leaner here,” Mr. Gomes said. “Now we can compete with the big guys.”