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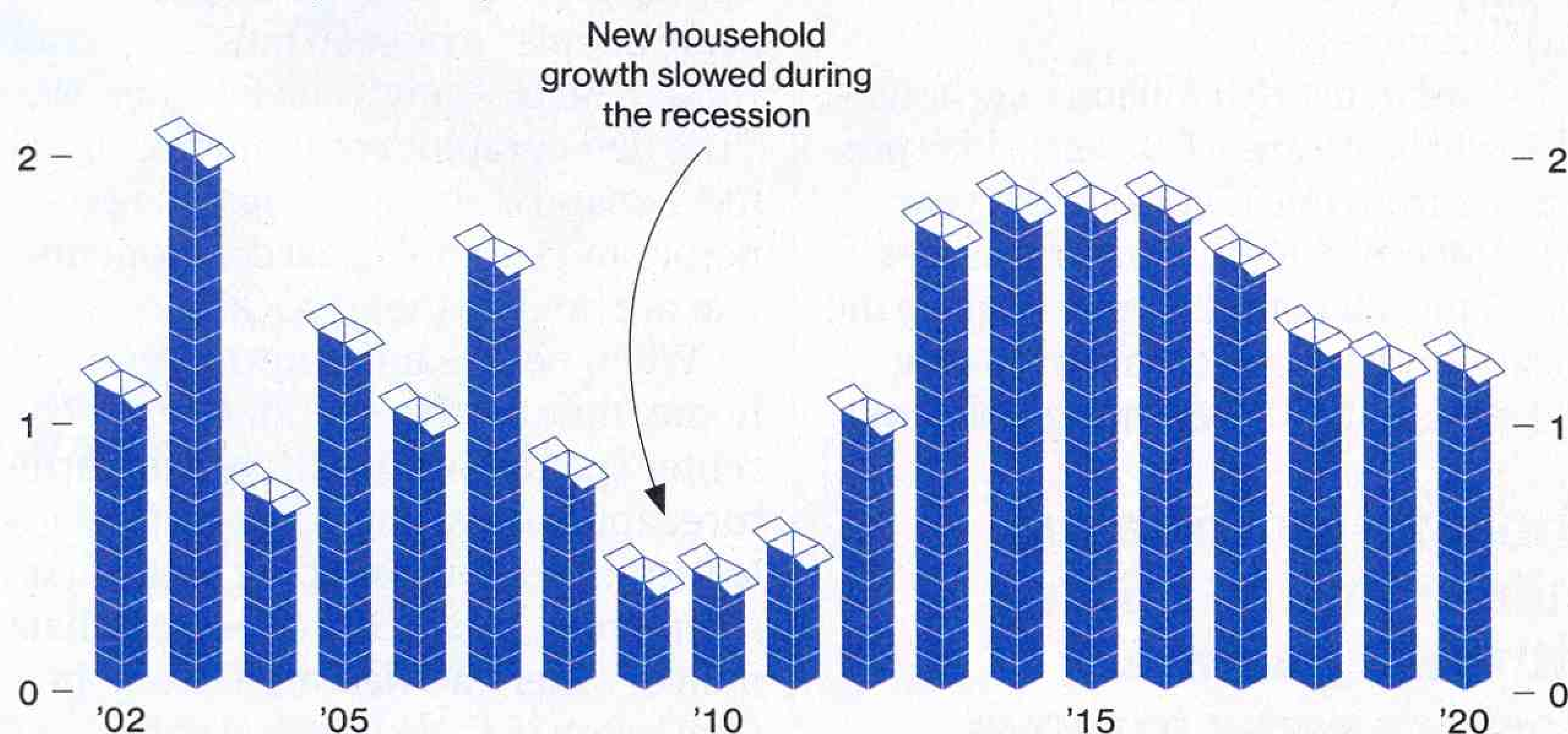
Bloomberg Businessweek

a washer-dryer combo at yard sales or from classified ads, she did lay out some cash at **Wal-Mart** for new housewares. And Stokkebye has bought several hundred dollars' worth of paint, tools, dishes, and other supplies. "I just cleaned out **Ikea** on Sunday," she says.

A Bloomberg survey of 59 economists in early April predicts that consumer spending will rise 2.8 percent both this year and next, vs. an average of 1.8 percent in the last eight quarters. Jim O'Sullivan, chief economist at MF Global Holdings in New York, is more bullish, predicting increases of 3.2 percent for 2011 and 3.4 percent next year. Young people leaving their parents' homes "have the ability to spend, and they spend on all of the things associated with setting up a household," O'Sullivan says.

Another demographic shift should play a role as well: more divorces, which also create new households. The number of divorces dropped to 6.8 per 1,000 people in 2009 from 7.4 in 2006, prior to the recession, government figures show. A survey this year by the National Marriage Project at the University of Virginia found that 38 percent of people considering a divorce or separation put aside those plans because of the recession. St. Louis-based divorce-law specialist **Cordell & Cordell** says its customer count rose by about 20 percent in the first quarter. "We see things moving in a positive direction, from our perspective," says principal partner Joseph E. Cordell. —*Steve Matthews*

The bottom line *Some young adults are finally leaving the nest and creating new households, spending up to $1,900 on furnishings.*



Consumer Debt

Brazil's New Middle Class Goes on a Spree

▶ As the economy booms, consumers buy on installment

▶ "There's no culture of managing debt at all"

Francisca de Carvalho lives in Rocinha, a shantytown that climbs a hillside just beyond the fancy Rio de Janeiro neighborhood of Leblon. Her fourth-floor apartment isn't what you'd expect in a *favela*: It's spic-and-span, with modern furnishings and a sweeping view. Carvalho, 54, recently spent about $400 to remodel her bathroom. She borrowed the money on her **Banco Itaú** credit card and pays 14 percent interest–per month. "I like nice things," she says.

More and more Brazilians are developing a taste for nice things and borrowing to pay for them. The world's seventh-largest economy expanded by 7.5 percent last year, and the Finance Ministry predicts growth of 4.5 percent this year, energized by demand for the goodies of the good life. Consumer debt is growing so fast that President Dilma Rousseff's government, in an attempt to deflate a possible credit bubble, has boosted the taxes that consumers pay on loans. The central bank has raised rates to discourage spending.

Brazilian stores encourage shoppers to buy on the installment plan. In Rio's Copacabana beachfront barrio, the **Casas Bahia** and **Ponto Frio** emporia trumpet stoves and washing machines for "10 Payments Without Interest." Down the street, you can make four payments to buy sneakers at **Ultraflex**.

Under such an arrangement, a store would appear to be assuming all the risk–and with inflation running at 6.5 percent, losing money to boot. In fact, the sticker price already has a steep interest rate built in, so large chains are making money more as consumer-finance houses than as retailers. Their profits reflect the boom: **Lojas Americanas**, Brazil's biggest publicly traded discount retailer, saw earnings jump 33 percent in the first quarter from a year ago, and at **Hering**, a clothing chain, quarterly profits rose 74 percent. Shoppers who can afford to pay upfront can often bargain the price down or find the same item online for less.

During President Luis Inácio Lula da Silva's eight years in power, from 2003-2011, 24.5 million people officially escaped poverty, and 35.5 million moved into the lowest rung of the middle class, the so-called Class C, earning $1,100 to $3,900 a month, according to researchers at the Getulio Vargas Foundation university. For these strivers, credit abounds for the first time. Total consumer loans rose sixfold over the past eight years, to $495 billion, and jumped from 24 percent of gross domestic product in 2003 to 46 percent today, according to the central bank. About a fifth of these loans are paid by automatic deduction from paychecks. Since 2004, bank credit cards have tripled, to 159.5 million, and retailer cards have nearly quadrupled, to 233.5 million. The average interest rate on credit cards is 238 percent annually, while loans from retailers cost 85 percent, and personal loans from banks 47 percent.

Because of stiff Brazilian tariffs that shield the domestic market, items can cost far more than they do, say, in the U.S. The cheapest model of an LG Electronics 32-inch flat-screen TV goes for $749 at Casas Bahia, vs. $449 at a P.C. Richard & Son electronics store in New York.

Borrowers often don't know what they're getting into. "These are people with no experience of credit," says Andrew Frank Storfer, president of Anefac, a São Paulo association of finance and accounting executives.

Shopping in central Rio: Borrowers often don't know what they're getting into

"There's no culture of managing debt."

Maria de Matos can testify to that. A neighbor of Carvalho's in Rocinha, Matos got her first credit card five years ago and began frequenting the Barra da Tijuca shopping mall. Every month she took a bus there with the money she earned cleaning houses to make minimum payments, to do some shopping. At age 48 and illiterate, Matos says she had no idea what rates the stores were charging. A year ago she declared bankruptcy on her $1,100 debt. "It was like I was swimming but just sinking deeper and deeper," she says.

While the central bank regulates how much banks must set aside to cover risky loans, the banks can lend at whatever rates and terms they want. Partly as a result, Brazilian banks enjoy an average profit margin of 15 percent, compared with 7.8 percent for U.S. lenders, according to Bloomberg data. Brazil also lacks consumer credit bureaus, which means there's no way for consumers to earn cheaper loans with a good credit score, because the government only tracks borrowers who have defaulted.

So far, with the economy roaring and labor markets tight, consumer delinquency rates haven't risen dangerously. **Itaú Unibanco Holding**, the nation's biggest bank by market value, just beefed up provisions for bad loans, saying it expected defaults to rise. Lula boosted bank reserve and capital requirements in December, while Rousseff nearly tripled, to 6.6 percent, a tax Brazilians pay on any credit-card purchases made abroad.

Although more credit-throttling moves are expected, it may be tough to keep Brazilians at home now that they've tasted the pleasures of mall-crawling. "Shopping was such a temptation," says Matos of her life before bankruptcy. "Now I regret it so much. It dirtied my name."
—*Harry Maurer and Alexander Ragir*

The bottom line *Brazil's newly prosperous consumers may endanger the country's economy by borrowing at sky-high rates.*

Energy

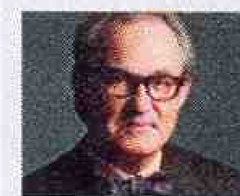
China's Power Outages Come Early and Often

▸ The power companies want to charge more to produce more

▸ "It's not as if these plants are maxed out"

Every summer for the past decade, China has had to endure power shortages in its most heavily industrialized provinces, as air conditioning use drove electricity consumption sharply upward. This year the government started rationing power in April. All told, China could face an electricity shortfall of 30 million kilowatts this summer, warned the China Electricity Council, the industry group for operators of power plants and utilities, on Apr. 28.

Companies are starting to feel the pain. Shane Lou, a small factory operator in Zhejiang province,



Tom Keene's EconoChat

Tom talks with **Chris Whalen,** managing director of Institutional Risk Analytics, about banks in the U.S. and Europe

Do the challenges in Europe have a knock-on effect on U.S. banks?
Oh, yes, very much. They've really decapitalized much of the banking system in Europe. You're talking about government-supported banks with almost no private-sector capital, really, in these areas. It's still too dangerous to play there. You don't see entrepreneurs starting new banks in the U.K.

What banks in Europe could be affected negatively?
The state sector is either going to support the banks in the case of France and Germany, or in the case of Ireland and the U.K., they may actually restructure and take apart these banks and then try and entice private equity to come in and help them.

You're cautious on U.S. banks, too.
You have margin compression. You don't have any pricing power. You don't have a lot of demand, frankly, for bankers, and banks' costs are starting to go up for a variety of reasons.

Do you subscribe to the idea that we are not clearing our markets like we used to? Are we trying to have a pain-free crisis?
Yes, exactly. You buy time with interest rate policy, and we have pushed trillions of dollars worth of subsidies through the banks, but they're still deflating because we are muddling along and unfortunately, you don't get growth. You don't get job creation because the top four banks can't grow, Tom. They've got to retrench.

Keene hosts Bloomberg Surveillance *7-10a.m. ET on 1130AM in the NY metro area & nationally on SiriusXM 113.*