BANCO CENTRAL DO BRASIL

Minutes of the 94th Meeting of the Monetary Policy Committee (Copom)

Date: March 16th, from 3:45PM to 7:15PM, and March 17th, from 3:45PM to 7:15PM
Place: BCB's Headquarters meeting room of the 8th floor (on March 16th) and 20th floor (on March 17th) – Brasília – DF

In attendance:
Members of the Committee
Henrique de Campos Meirelles – Governor
Afonso Sant'Anna Bevilaqua
Alexandre Schwartsman
Antônio Gustavo Matos do Vale
Eduardo Henrique de Mello Motta Loyo
João Antônio Fleury Teixeira
Luiz Augusto de Oliveira Candiota
Paulo Sérgio Cavalheiro
Sérgio Darcy da Silva Alves

Department Heads (present on March 16th)
Altamir Lopes – Economic Department
Daso Maranhão Coimbra – International Reserves Operations Department
José Antonio Marciano – Department of Banking Operations and Payments System
José Pedro Ramos Fachada Martins da Silva – Investor Relations Group
Marcelo Kfoury Muinhos – Research Department (also present on March 17th)
Sérgio Goldenstein – Open Market Operations Department

Other participants (present on March 16th)
Alexandre Pundek Rocha – Advisor to the Board
Flávio Pinheiro de Melo - Advisor to the Board
Hélio José Ferreira – Executive Secretary
João Batista do Nascimento Magalhães – Special Advisor to the Governor
Jocimar Nastari – Press Secretary
Katherine Hennings – Advisor to the Board

The members of the Monetary Policy Committee analyzed the recent performance of and prospects for the Brazilian and international economies under the monetary policy framework, which is designed to comply with the inflation targets established by the government.

Recent Evolution of Inflation

1. In February, there was price deceleration in most part of consumer goods. This fact impacted the evolution of both consumer price indices and core inflation measures, which cooled down in the month. However, there are still pressures coming from the rise in the international prices of commodities, especially over wholesale industrial prices. Yet, it is important to highlight the effects of the change in the Cofins legislation over the relative prices, whose most evident impacts also affect wholesale industrial prices.

2. The Broad National Consumer Price Index (IPCA) rose 0.61% in February, before a 0.76% rise in the previous month, after three consecutive months of acceleration. The IGP-DI reached 1.08%, remaining in an upward trend for the fourth consecutive month. This acceleration, in comparison to the one verified in the previous month, was mainly a consequence of the IPA-DI acceleration to 1.42% from the 0.75% previously recorded, once that the IPC-Br decelerated to 0.28% in

February, from 1.08% in January. The 12-month accumulated variation of the IPCA, IGP-DI and IPA-DI remained in a downward trend in February, standing at 6.69%, 5.69% and 4.45%, respectively.

3. The most important individual contribution to the IPCA variation came from the readjustment of school fees, with a 0.31 p.p. contribution to the overall monthly index. The group food and beverage items, which recorded a variation of 0.15% compared to the 0.88% increase in the previous month, reflected the effects of the new harvest into prices, a paramount factor that contributed to the IPCA deceleration in February. The fall in the prices of fuel-alcohol is also highlighted, as a consequence of an excessive production.

4. Still regarding the February IPCA, free prices increased 0.75%, accounting for 0.54 p.p. of the monthly index variation, while the 0.26% increase in the regulated prices accounted for the remaining 0.07p.p. In the first group, the rise in school fees and in the prices of cars, fresh food items and beans are highlighted. Concerning regulated prices, the rise in water and sewage tariffs as well as in the prices of bottled gas and health insurance prevailed, fact that was partially offset by the decrease in fuel prices.

5. The Wholesale Price Index (IPA) presented a 1.42% variation in February, compared to the 0.75% variation in the previous month. Despite the continuous fall in agriculture prices, industrial prices showed sharp increase in the period. The agriculture IPA dropped 0.76% in February, compared to the 0.34% fall in January. This pattern reflects mainly a trend reversion in the prices of cereals and grains (rice, beans and corn) due to the new harvest period. The price decreases in the group animal and by products (cattle, pork and milk) also contributed to the negative IPA result. The industrial prices variation reached 2.3%, as against a 1.2% increase in January, mainly influenced by the price behavior of food products (oils and greases), chemical products (plastic materials and fertilizers), mechanics and electric material. The rise in metallurgy prices (iron, steel and by products, and non-ferrous metals) still presented the greatest contribution to the absolute variation of the industrial IPA, 0.36 p.p., despite the decrease in the monthly variation from January (5.2%) to February (4%). It is worth mentioning that the generalized pattern of items with positive variations in the industrial-IPA – 66.7% of the items presented price increases – indicates the influence of the change in the Cofins legislation over prices.

6. The core IPCA inflation calculated excluding household food items and regulated prices was the only core measure to increase in February, posting a 1% rise in the month, in comparison to a 0.64% increase in January. The intense variation of school fees, with a total weight of 8.8% in the IPCA, explains the rise in the index in the period. The 12-month accumulated variation stood at 7.39% in February, repeating the previous month result.

7. The core IPCA inflation calculated under the smoothed trimmed-mean method rose to 0.48% in February against 0.73% in January, posting a 9.97% accumulated variation in the last 12 months. The result calculated without the smoothing procedure for pre-selected items reached 0.28% in February, in comparison to 0.63% in the previous month. The 12-month accumulated variation totaled 6.45%, the lowest result recorded since the end of 2002.

8. Core IPC-BR inflation, calculated under the symmetric trimmed-mean method by Fundação Getúlio Vargas (FGV), reduced to 0.46% in February, compared to 0.65% in January, posting an 8.45% accumulated variation in the last 12 months.

9. The consumer prices deceleration is expected to continue in March, and the IPCA should show this behavior, following the food items trend and the end of educational items readjustments. As to the wholesale prices, agriculture prices should maintain their favorable performance, reflecting the price trends of cereals and fresh food items. Industrial prices should be pressured by inputs readjustments, albeit in a lower intensity than the one observed in February.

Assessment of Inflation Trends

10. The identified shocks and their impacts were reassessed according to new available information. The scenario considered in the simulations assumes the following hypotheses:

    a. The projections for the evolution of gasoline and bottled cooking gas prices in 2004 were maintained at 9.5% and 10%, respectively;

    b. The projection for household electricity tariffs was slightly increased to 6.9%, from 6.3% in the previous Copom meeting. Regarding telephone tariffs, the assumption of a 6.8% elevation in 2004 was maintained;

    c. Regarding all regulated prices, with a total weight of 28.9% in the February IPCA, a 7.3% rise is projected, 0.4 p.p. below the projection made in the previous meeting;

    d. The projection for the readjustment of all regulated prices for 2005 was maintained at 6.0%. This figure results from a model of endogenous determination, which takes into account seasonal components, the exchange rate behavior, market prices inflation and the IGP-DI change;

    e. The projection for the 6-month spread over the Selic rate, following the specification of a Vector Autoregressive model using the Selic and swap rates on the eve of the Copom meeting, starts from an –80 b.p. average in the first quarter of 2004 and reaches 50 b.p. in the end of 2005.

11. Regarding fiscal policy, it is assumed that the primary surplus target of 4.25% of the GDP for 2004 and the following two years will be achieved. The related assumptions considered in the previous meeting were maintained.

12. Considering the benchmark scenario hypotheses, including the maintenance of the Selic interest rate at 16.5% p.a. and of the exchange rate close to the level prevailing on the eve of the Copom meeting (R$2.91), IPCA inflation was projected below the 5.5% target for 2004 and below the 4.5% target for 2005. According to the market scenario, which takes into account the consensus exchange rate and Selic rate paths as surveyed by the BCB´s Investor Relations Group (Gerin) on the eve of the Copom meeting, inflation is projected above the central targets of 5.5% and 4.5% for 2004 and 2005, respectively.

Monetary Policy Decision

13. After three consecutive months of increases, the inflation registered by the IPCA decreased to 0.61% in February, 0.15 p.p. below the January result. There was a significant decrease in inflation in tradable and regulated items, which fell to 0.07% and 0.26%, respectively. Inflation in the non-tradable items rose almost 0.7 p.p. in the period, reaching 1.64% in February, strongly influenced by the increase in school fees. If this item were excluded, non-tradable items inflation would have been 0.73%, what would represent a 0.24 p.p. fall, compared to January. Inflation measured by other consumer price indices, such as IPC-Fipe and IPC-Br, showed a decrease of 0.5 p.p. and 0.8 p.p., respectively, compared to January. However, general price indices showed mixed evidences, with a decrease in the IGP-M and an increase in the IGP-DI. This increase was mainly caused by the higher inflation in wholesale industrial prices, which reached 2.29% in February, 1.1 p.p. above the value registered in January.

14. The fall of consumer inflation in February can be more clearly seen in the behavior of the core inflation calculated under the trimmed-mean method. Core inflation calculated under the smoothing of pre-selected items method decreased to 0.48% from 0.73%, the lowest figure recorded since June 2002, and the core inflation calculated without the smoothing procedure decreased to 0.28% from 0.63%. Core inflation calculated by excluding household food items and regulated prices rose to 1.00% from 0.65%. However, as occurred in the non-tradable items group, this increase is due to the school fees behavior. If this item were excluded, core inflation calculated by excluding household food items and regulated prices would have decreased to 0.45% in February. The better behavior of consumer inflation can also be seen in the the drop in the IPC-Br core and in the ratio of items of the IPCA with positive variation in the month, which decreased to 60.4% from 70.9%, below the average observed in the last three quarters of 2003.

15. According to the IBGE, the GDP fell 0.2% in 2003, in relation to 2002. Despite the fact that the GDP growth stood below the expected, output performance remained qualitatively consistent with the benchmark scenario that the Copom has been working with, especially regarding the economic cycle. More specifically, in the second semester of 2003, the economy began a recovery process, and posted a 1.5% growth in the last quarter of the year, compared to the previous quarter, which is equivalent to an annual rate of more than 6%. Economic indicators available so far suggest that there has been a sustained economic growth path at the beginning of the year. Due to the significant growth in the last quarter of 2003, it is likely that the GDP data in the first quarter of 2004 indicate a cooling down on economic activity.

16. Industrial production kept the recovery trend, having presented a 0.8% growth in January, compared to December, according to the IBGE seasonally adjusted data. Semi and non-durable goods output presented growth for the first time since last September, suggesting that growth recorded in the other sectors of economy has been influencing this sector, which had not presented recovery so far, through the marginal increase in employment and real earnings. Quarterly moving average behavior has presented a continuous industrial output growth, although in lower rates than the ones recorded in the last quarter of 2003. For February, considering previous indicators, it is not possible to discard a fall in the industrial production, which is perfectly compatible with the usual patterns of a sustained growth recovery, with short-term oscillations around the trend. Moreover, in February there were only eighteen working days, as against twenty working days in the same month of 2003, harming the comparison against the same month in 2003. In addition, in two out of the five last years, Carnival was in March, which may affect the seasonal adjustment of the series. Industrial production can benefit from the low inventory levels, compensating the negative short-term scenario. Considering that different sources provide data for industrial sales and industrial production, for the fourth consecutive month the former recorded higher growth than the latter, which was 2.8% in January, according to the National Confederation of Industry (CNI). This fact may give additional stimulus to production, associated to the inventories build-up dynamics.

17. According to IBGE data, seasonally adjusted by the BCB, retail sales fell 0.3% from November to December. Yet, retail sales in São Paulo grew 8.7% in January, in relation to the previous month, according to Fecomercio data, seasonally adjusted by the BCB. Considering the behavior of new credit concessions, it is likely that the data on the January-February period show some decrease in the consumption of durable goods, such as automobiles, furniture and domestic appliances. In March, the Consumer Intention Index (IIC) stood above the critic value of 100, signaling that there are positive perspectives; however, the fall in relation to February suggests lower consumption growth in the short-term. Following the growth in the real income observed in the last months of 2003, supermarket sales, which concentrate non-durable goods, have presented progressive recovery.

18. The consolidation of positive data in the economic activity continues to be followed by expressive indicators in the external sector, posting a favorable combination of economic policy results that had not been seen in Brazil for several years. In February, the trade balance surplus reached

US$2 billion and, for 2004, a US$24 billion surplus is forecasted, which is a very satisfactory result considering the expected economic growth for this year. Compared to the same period last year, in February, exports and imports grew 27.1% and 6.9%, respectively. Due to the favorable performance of the trade balance, the current account result presented a surplus in February, accumulating US$0.9 billion in 2004. Despite the excellent results in the external accounts, there was an increase in the sovereign risk perception: the country-risk measured by the Brazil Embi+ increased to 560 b.p. from values around 520 p.b. from the February to the March eves of the Copom meetings, after having increased almost 100 p.b. from January to February. In spite of the reduction in the private external funding, the dollar remained stable, at values around R$2.90 on the eve of the Copom meeting. Regardless of the higher volatility that has been observed in the last two months, the Copom maintains the evaluation that the external scenario is very favorable, presenting perspective of world economic growth and high international liquidity.

19. After three consecutive months of deterioration, inflation expectations for the first quarter of 2004 dropped, according to a survey conducted by the Investor Relations Group – Gerin. The 0.61% inflation in February was bellow the 0.70% expected on the eve of the previous Copom meeting. The median of March inflation expectations also dropped from the eve of the February meeting to the March meeting, to 0.42% from 0.43%, for the full sample of the institutions participating in the survey, and to 0.40% from 0.43%, for the institutions with more accurate forecasts in the short run (Top 5 Forecasting Institutions). Hence, for the full sample, the expectation for the first quarter fell to 1.80% from 1.90%, and for the Top 5 Forecasting Institutions, it fell to 1.78% from 1.98%. The median of market expectations to 2004 and 2005 remained stable at 6.0% and 5.0% respectively, and the expectations to the next 12 months decreased to 5.41% from 5.70% in the period.

20. According to the benchmark scenario considered by the BCB inflation forecasts, which assumes the maintenance of the Over-Selic rate at 16.5% p.a. and the foreign exchange rate at R$2.91, the projected inflation is below the targets of 5.5% for 2004 and 4.5% for 2005. In accordance with the market scenario, which includes the market expected path to the exchange rate and to the Over-Selic rate on the eve of the Copom meeting, the BCB inflation forecasts lie above the targets for 2004 and 2005. Compared to February, there was an increase in the projections, because in both scenarios the February inflation forecast was much below the effective one, even though both of them considered a GDP growth for the fourth quarter above the effective, a regulated prices variation greater than expected by the Copom, which has been revised downwards since its meeting in February, and a 12-month-ahead inflation expectations higher than the ones currently verified.

21. As in previous meetings, the Copom also examined the projections produced according to the same methodology, and according to the same benchmark and market scenarios for the interest and exchange rates paths, taking into account the Top 5 short-term inflation expectations for March and hence, projecting inflation for the following months. In this exercise, considering the benchmark scenario, the projected inflation for 2004 is slightly above the target, and for 2005, it is bellow the target. However, the projected inflation for 2004 and 2005 are below the February results for the same exercise, due to the substitution of the lower figure effectively observed for the expected inflation of the Top 5 forecasters for the month of February, to the reduction of expected inflation by those institutions for March and to the reasons mentioned in the paragraph above, regarding the GDP performance in 2003, the reduction in the projection for the regulated prices for 2004 and the downwards improvement of the 12-months-ahead inflation expectations. According to the same methodology, the projected inflation for the market scenario is above the 2004 and 2005 targets, although lower than the ones projected in February, due to the same reasons mentioned above.

22. The Copom also evaluated a third set of scenarios, which supposes lower inflation persistence. These scenarios consider the hypothesis under which part of the high inflation of the first quarter of the year will not impact the following quarters' and that there could even be a reversion in the inflation increases that occurred in the period due to momentary unfavorable weather conditions.

This hypothesis becomes more likely the more efficient the monetary policy is in exercising its coordinating role, preventing punctual inflation increases caused by supply shocks, by seasonal factors and by attempts to restore margins from contaminating inflation expectations. For this hypothesis the Copom considered that part of inflation in the first quarter was due to a seasonal shock and that other shocks of the same fashion will also affect inflation in each quarter of the year and in 2005. The magnitude of each quarterly typical shock was estimated to reproduce, in the Copom projection models, the same seasonal standard observed in the recent series of free prices. As in the exercise described in the previous paragraph, the inflation of the first quarter is the one expected by the short-term Top 5 institutions. According to this procedure, considering the benchmark scenario exchange and interest rates trajectories, the forecast inflations for 2004 and 2005 are below the targets. When market expected exchange and interest rates are considered, inflation remains above the target for 2004, although closer to the target value than in the exercise that only encompasses the expectations of the Top 5 institutions for the first quarter, and the inflation for 2005 remains unchanged.

23. The Copom members evaluated that the risk of not fulfilling the 2004 inflation target reduced since the last meeting, due to the IPCA result and its cores in February and to lower inflation expectations for the short run and for the next twelve months. Moreover, it was consensual that the evaluation of this more favorable scenario is a result of the recent monetary policy decisions, which have been mitigating the pass-through from the rises in industrial costs to retail costs and the second order effects of inflationary surprises of January and February. The conduction of the monetary policy at the beginning of the year was decisive to revert the environment in which the leading sectors in the economic rebound could pressure prices upward, expecting that demand conditions would absorb the increases. Therefore, the risk of higher inflation diminished while the risk of unsustained economic activity remained low.

24. It was also consensual the interpretation that the main risk for consumer inflation in the next months consists on the contamination of the increases of wholesale industrial prices to retail prices. It is important to notice that this element is not incorporated into any of the projected scenarios analyzed above, except for the limited effects on the results of the IPCA for the first quarter, since there is no perceptible signal of transmission through any other channel, such as market expectations for the IPCA during the next quarters. The experience of the last years suggests that when the industrial IPA pass-through influences the part of IPCA represented by the industrialized products, it is usually fast. In this sense, the recent results of the deceleration of consumer prices are quite encouraging, despite the acceleration of the wholesale prices. The usual high speed of this pass-through enables to foresee that the remaining uncertainties about the increase in consumer prices as a result of pressures caused by wholesale prices will soon be solved.

25. Great part of the increase in wholesale prices in the last months can be explained by supply shocks, among which the different impacts caused by the Cofins ratio and levies throughout the productive chains and the increase in the international price of some commodities and intermediate inputs. There are still no elements allowing for a satisfactorily accurate measure of the magnitude of the potential impact of these shocks over the consumer prices, although there are preliminary indications, for example, that the effect of the Cofins may be small. Economic theory and the best monetary policy practice recommend the partial accommodation of increases in consumer prices caused by supply shocks. The Copom adopted this procedure in the recent past, announcing during 2002 revisions in the objective to be sought in that year and establishing adjusted targets for the inflation in 2003 and 2004. However, there is no automatic procedure that can be adopted in any circumstance, as the optimum degree of accommodation may depend on factors such as the stage of the economic cycle at which the economy is found, the unique demand conditions among the sectors that are differently affected by the shocks, the distance between current inflation and the desirable inflation in the medium and long terms, and the direct response of the private agents' inflation expectations to the shock. The Copom understands that the current circumstances do not recommend the adoption of procedures willing to accommodate the recent supply shocks.

26. Three members of the Copom considered more appropriate to keep unchanged the basic Over-Selic rate in this meeting. These members recommended greater caution in the conduct of the monetary policy in the short term, proposing that eventual cuts in the target for the Over-Selic rate should be left for a subsequent moment, when there may be additional evidences that the higher inflation rates of January and February might not contaminate the inflation of the following months and when the impact of the recent increases in the wholesale prices over the future dynamics of the consumer prices may not be significant. This caution would increase the probability of both a steady anchorage of the inflationary expectations and the behavior of the price-makers to consolidate a favorable level of inflation, such as the one considered by the scenarios of low inflation persistence analyzed by the Copom. Therefore, these three members voted for the maintenance of the target for the Over-Selic rate at 16,5% a.a.

27. However, for most part of the members of the Copom, the immediate fall of the Over-Selic rate in 0.25 p.p can be justified by the recent behavior of the price indices, the lower inflation expectation for both the short-term and the next twelve months and the low intensity of the wholesale pass-through to the retail prices. These considerations indicate that the maintenance of the Over-Selic rate in January and February was enough to increase the probability of materialization of low inflationary persistence scenarios considered by the Committee, moving away the danger that the inflation increase recorded from December to February could contaminate inflation expectations and provoke a change in the inflationary dynamics. Therefore, this easing of the monetary policy reflects the necessary caution in the administration of the risks between inflation and the continuity of the restore of the economic activity.

28. As a result, the Committee decided, by six votes to three, to reduce the target for the Over-Selic rate to 16.25% p.a. from 16.5% p.a.

29. At the closing of the meeting, it was announced that the Copom would meet again on April 13, for technical presentations and on the following day, in order to discuss the monetary policy decision, as established in Communiqué 11,516, of October 15, 2003.

BANCO CENTRAL DO BRASIL

SUMMARY OF DATA ANALYZED BY THE COPOM

Economic Activity

30. According to the Federação de Comércio do Estado de São Paulo, retail sales in São Paulo metropolitan area increased 8.7% in January compared to December (seasonally adjusted). This result reflected a 8.9% increase in consumer goods sales, due to the increases of 8.7% and 12.3% in semi and non-durable goods sales, respectively, while the durable goods sales decreased 0.3%. The automotive sales increased 4% and construction inputs sales decreased 2.1%.

31. On February, consultations to the São Paulo Trade Association and the Usecheque showed a decrease of 2.8% and an increase of 0.3%, respectively (seasonally adjusted), indicating caution in the retail activity.

32. The Federação de Comércio do Estado de São Paulo survey on consumer confidence showed a 8.6% decrease in March, the second consecutive reduction in the consumption intentions. This result reflected the decrease not only in the present but also in the future consumption intentions. However, the result of 115.8, in a scale ranging from 0 to 200, reflects an overall positive sentiment, although weaker, mainly regarding future consumption intentions.

33. Regarding investment data, the capital goods output increased in January (compared to the previous month) after two months of decrease. Machinery and equipment production and construction industry input increased 4.5% and 1.1%, respectively, while capital goods imports decreased 14.1%. The machines and equipment exports increased 0.01% (all data seasonally adjusted). The increase in the capital goods production spread over all sectors, except for transport equipment.

34. According to the IBGE research, after the decrease of 1% in December, interrupting a sequence of five positive results, the Brazilian industrial production increased 0.8% in January, seasonally adjusted. Out of the twenty segments surveyed, seventeen presented increase, as well as in three out of four categories of use. Intermediary goods production decreased 0.8%, after six months of an upward trend, mainly reflecting the reduction of oil extraction due to platforms maintenance. After the decline of semi and non-durable goods production for three consecutive months, there was a 2.2% increase, while capital and durable goods productions increased 4.5% and 3%, respectively. Compared to the same month of the previous year, industrial production grew 1.7% in January.

35. Regarding the performance of the manufacturing activity in January, National Confederation of Industry (CNI) statistics showed sales dynamism. Real sales grew 2.7% in the month (seasonally adjusted), increasing for the seventh consecutive month. Compared to the same month of 2002, real sales increased 10.8%, registering the third consecutive positive rate. The seasonally adjusted worked hours increased 0.5% in January, after a decrease of 2.1% in December. The level of capacity utilization, seasonally adjusted, remained at 80.3% in January, practically the same level of December 2003.

36. In February, the automotive sector output presented a 1.6% decline. Vehicles production and external sales decreased 9.3% and 33.5%, respectively, compared to last month (seasonally adjusted data).

Labor Market

37. The index of employment increased 0.5% month-on-month in January compared to December (seasonally adjusted), and 3.2% year-on-year, according to the Ministry of Labor. According to the

IBGE's survey, the unemployment rate in the six main metropolitan areas, after two consecutive declines, increased to 11.7% in January, from 10.9% in December. The same survey also registered that the employed workers average real earning deflated by the INPC decreased 13.9% in December 2003, compared to the same month in 2002. Considering the average wage, which does not include extraordinary revenues, the available data up to January show a 6.2% decrease compared to the same month of 2003.

38. In the industrial sector, according to the CNI, there was a 0.2% (s.a.) increase in employment in January, after a decline of 0.3% in December 2003, compared to the previous month. After seven months of increase, seasonally adjusted industry real payroll decreased 0.4% in January, compared to December 2003.

Credit and Delinquency Rates

39. Non-earmarked credit increased 2.1% in February, after the seasonal decrease in January. Regarding credit to companies, there was a 2.1% increase, mainly due to advance on export contracts and vendor. Regarding credit to households, there was also a 2.1% increase, mainly in personal credit with payroll-discounted repayment. Regulated by the Provisional Measure 130, these modalities have been replacing other forms of credit that have higher cost, such as overdraft account and credit card, among others.

40. The average interest rate on non-earmarked credit registered another fall in February, 0.3 p.p., reaching 45.1% p.a. The decline in rates was more significant for households, which fell 1.2 p.p., reaching 64.2% p.a. The average interest rate on credit provided to companies reached 30.2% p.a., stable in relation to last month. The delinquency rate on non-earmarked credit increased 0.3 p.p. in February, reaching 8.3%, as a consequence of the 0.2 p.p. increase in non-performing credit to individuals and of the 0.5p.p. increase in credit to companies.

41. Regarding the retail sector, there was a slight seasonal worsening in the default figures in February, compared to the previous month. ACSO data show that net default rates increased to 7.2% in February from 4.7% in January.

External Environment

42. The latest indicators signal to the maintenance of the global economy recovery, although in a lower pace and below market expectations. World economy is still vulnerable to non-economic issues and the events in Madrid reinforce cautionary position when evaluating short-term trends for the economy.

43. In the U.S., negative indicators, as the broadening of budgetary and trade deficits, prevailed over positive figures, such as the increases in both wholesale sales and consumer credit, in January. The recovery is still slow in Europe, while Japanese growth rate was revised downward in the last quarter of 2003. The Japanese government points the improvement in private consumption as a factor favoring economic expansion this year, together with the significant increase in exports, despite the concerns about the effects of the appreciation of yen on the trade balance.

44. Labor market remains recovering at a modest pace in the main economies. In the U.S., unemployment rate remained at 5.6% in February, with not many new job positions, reinforcing the effects of a higher productivity in the recent economic recovery. Businessmen sentiment worsened in February in the U.S., and was it stable in Japan and Europe. Consumer confidence declined in the U.S., but it increased in Japan and in the Euro Area.

45. In the absence of inflationary pressures, the basic interest rates remained steady in the central economies. In the U.S., the poor performance in the labor market corroborates the evaluation that the fed fund rates should remain stable in the short-run. This behavior benefits the financing of external needs of the emerging countries, contributing to the downward trend for the country risk rates measured by Embi+, momentarily interrupted by the effects of the events in Madrid.

46. In the FX markets, there is a consensus about the continuity of the dollar depreciation due to the increasing U.S. current account deficit. The dollar depreciation together with the disequilibrium provoked by strong Chinese demand has been affecting commodity prices, which reached high levels in February.

47. The oil price has increased again since the beginning of February, reflecting the producers' decision to reduce output by 1 million barrels/day, starting April 1st. However, other factors have been contributing to prices increase, such as the crisis in Venezuela, the low levels of U.S. stocks of gasoline, and recently, the unpredictable effects of the Madrid events.

Foreign Trade and Balance of Payments

48. The Brazilian trade balance posted a US$2 billion surplus in February. Exports totaled US$5.7 billion and imports, US$3.7 billion, with increases of 27.1% and 6.9%, respectively, compared to the February 2003 daily averages. In the first 10 working days of March, the trade surplus totaled US$911 million, with increases of 22.7% and 26.9% in exports and imports, respectively, compared to same period of the previous year. Up to the second week of March, trade surplus reached US$4.5 billion in the year, compared to US$3.8 billion in the first three months of 2003.

49. The current account registered a US$0.2 billion surplus in February, reversing the deficit of the same magnitude registered in February 2003, and accumulating a US$5 billion surplus in 12 months (0.98% of the GDP). Income and services registered a US$2 billion deficit, compared to US$1.5 billion in February 2003. Financial account balance presented a US$1.1 billion deficit in the month, from a US$43 million surplus in February 2003, reducing the surplus accumulated in the year to US$2.7 billion. Rollover rates remained high not only for direct loans (164% from 39% in February 2003) but also for private securities placed abroad (255% from 188%). Net FDI totaled US$1 billion in February, accumulating US$2 billion in the year. At the end of February, international reserves stood at US$53 billion, and the net adjusted international reserves (IMF agreement concept) stood at US$21.2 billion.

Money Market and Open Market Operations

50. After the last Copom meeting, the future interest rates presented greater volatility, with the 1-year and 2-year rates ranging between 15.25% and 15.94%, and between 15.31% and 16.11%, respectively. In addition to the political scenario, other factors contributed to this movement, such as the 2003 GDP and the January industrial production results, the United States labor market data, inflation indices released showing different behavior between consumer and wholesale prices, and the lower market expectations for the next twelve months IPCA. However, despite the volatility observed, on March 16 the yield curve had already returned to a level similar to the one observed on February 18. Comparing both dates, the 3-month, 6-month and 1-year interest rates decreased 0.06 p.p., 0.08 p.p. and 0.13 p.p., respectively, while the 2-year interest rate remained stable. Real interest rate, measured by the quotient between the 1-year nominal rate and the inflation expectation for the next twelve months, increased to 9.4% from 9.1%, and the forecast real rate for 2004 increased to 9.1% from 8.9%.

51. The BCB did not carry out rollover auctions to the FX securities and swaps maturing on March 1st, 10 and 18. Including the biannually interest rates coupons, the net redemption of FX instruments in March, up to March 18, reached US$2.6 billion, and US$10.2 billion in the year.

52. The National Treasury carried out four LTN auction, totaling R$8.8 billion. In the two first tranches, securities maturing in January and July 2005 were placed, and in the last two tranches, securities maturing in April 2005 and January 2006 were placed. The National Treasury also carried out an auction of a NTN-F maturing on January 1st 2008, which financial volume reached R$278.4 million. The LFT and NTN (C and B) issues reached R$570.7 million and R$699.5 million, respectively.

53. The BCB maintained in its open market operations the 3-month fixed and the 2-week indexed repurchase operations, as well as the daily liquidity management operations, with tenor of two working days. The BCB also carried out 6 fixed rate repos with tenure up to 3 working days. The excess liquidity drained from the market averaged by the operations with tenure below thirty days was R$55.3 billion.

54. In February, the net securitized domestic public debt increased 0.8%, equivalent to R$5.8 billion. The dollar-linked share decreased to 19%, representing a reduction of 2 p.p. in the month and of 18 p.p. since the beginning of 2003.