



BANCO CENTRAL DO BRASIL

Minutes of the 134th Meeting of the Monetary Policy Committee (Copom)

Summary

Recent Economic Developments
Assessment of Inflation Trends
Monetary Policy Decision
Inflation
Economic Activity
Surveys and Expectations
Labor Market
Credit and Delinquency Rates
External Environment
Foreign Trade and International Reserves
Money Market and Open Market Operations

Date: April 15th, from 4:50PM to 6:50PM, and April 16th, from 4:50PM to 7:40PM

Place: BCB Headquarters meeting rooms - 8th floor on April 15th and 20th floor on April 16th – Brasília – DF

In attendance:

Members of the Committee

Henrique de Campos Meirelles – Governor
Alexandre Antonio Tombini
Alvir Alberto Hoffmann
Anthero de Moraes Meirelles
Antonio Gustavo Matos do Vale
Maria Celina Berardinelli Arraes
Mário Gomes Torós
Mário Magalhães Carvalho Mesquita

Department Heads (present on April 15th)

Altamir Lopes – Economic Department
Carlos Hamilton Vasconcelos Araújo – Research Department (also present on April 16th)
Luiz Donizete Felício – Open Market Operations Department
Luiz Fernando Cardoso Maciel – Department of Banking Operations and Payments System
Márcio Barreira de Ayrosa Moreira – International Reserves Operations Department
Renato Jansson Rosek – Investor Relations Group

Other participants (present on April 14th)

Adriana Soares Sales – Deputy Head of the Research Department
Alexandre Pinheiro de Moraes Rego – Press Secretary
Alexandre Pundek Rocha – Advisor to the Board
Flávio Pinheiro de Melo – Advisor to the Board
Katherine Hennings – Advisor to the Board
Sergio Almeida de Souza Lima – Executive Secretary

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

Recent Economic Developments

1. IPCA inflation remained virtually unchanged in March (0.48%) relative to 0.49% in February. As a consequence, inflation reached 1.52% in the first quarter of 2008, up from 1.26% in the same period of 2007.



BANCO CENTRAL DO BRASIL

Twelve-month trailing inflation continued to accelerate. After reaching 4.56% in January, it totaled 4.61% in February and 4.73% in March (2.96% in March 2007). Under this comparison basis, the acceleration of consumer price inflation essentially mirrors the behavior of market prices, which increased more rapidly than regulated prices. In fact, market prices and regulated prices increased 6.03% and 1.83%, respectively, in the twelve months through March, compared to 2.82% and 3.15% in the twelve months through March 2007. Moreover, despite the BRL appreciation, the prices of tradable goods accelerated, reaching 5.33% (compared to 1.10% in March 2007), according to the same comparison basis. Regarding non-tradable goods, greatly pressured by the behavior in the prices of perishable food and services, twelve-month trailing inflation was even higher (6.67%). The recent behavior of IPCA inflation has been remarkably less benign than that observed in previous quarters, so that since the end of 2007 inflation has signaled that it could be diverging from the targets path, reaching 2.97% in the last six months.

2. The three main underlying inflation measures calculated by the BCB showed divergent behavior in the first three months of the year. The core inflation by exclusion of household food items and regulated prices increased from 0.40% in January to 0.69% in February (under the impact of seasonal elevation of education costs), but retreated to 0.36% in March. The smoothed and non-smoothed trimmed means core inflation measures varied from 0.37% and 0.41% in January 2008, to 0.27% and 0.36% in February, and 0.39% and 0.41% in March, respectively. Similarly to headline inflation, the three core inflation measures remarkably accelerated in the first quarter of the year, in comparison to the same period of 2007, with increases from 1.17%, 0.92% and 0.81% to 1.46%, 1.03% and 1.18% for the core inflation by exclusion, smoothed and non-smoothed trimmed means core inflation, respectively. On a twelve-month trailing basis, the three core inflation measures accelerated, following the behavior of headline inflation. Core inflation by exclusion of household food items and regulated prices increased significantly, to 4.41% in March 2008, up from 4.27% in February and 4.09% in January. Smoothed trimmed means core inflation showed similar behavior (4.16% in March, up from 4.05% in February and 4.02% in January), while the non-smoothed trimmed means core inflation, which tends to present less inertial behavior, increased to 4.01% in March, up from 3.83% in February and 3.68% in January. Still on a twelve-month trailing basis, inflation core measures, despite remaining below the central target, currently stand at levels significantly higher than the record lows reached in 2007.

3. The General Price Index (IGP-DI) inflation retreated to 0.38% in February, down from 0.99% in January, but accelerated to 0.70% in March. On a twelve-month trailing basis, IGP-DI inflation accelerated to 9.18% in March, up from 8.65% in February and 8.49% in January (compared to 4.49% in March 2007). In the twelve months through March, the IGP-DI increase reflected both the behavior of the Consumer Price Index-Brazil (IPC-Br), which totaled 4.52% (2.69% in March 2007), and also of the IPA-DI (Wholesale Price Index), whose variation totaled 11.39% (5.09% in March 2007). According to the same comparison basis, the Civil Construction National Index (INCC) increased 6.69% (5.25% in March 2007). Regarding agricultural IPA, inflation reached 24.68% (12.83% in the twelve months through March 2007). It bears emphasizing the acceleration of industrial prices, which began in the second half of 2007 and seems to have intensified lately. In the first quarter of 2008, the industrial IPA increased 2.63%, up from 0.18% in the same period of 2007. In the last twelve months, wholesale industrial price inflation increased to 6.98% in March, up from 6.20% in February, 5.26% in January and 4.42% in December 2007. As highlighted in previous Copom Minutes, the Copom evaluates that the effects of wholesale prices over consumer price inflation will depend on current and prospective demand conditions and price-setters' expectations for the future inflation path.

4. After the last Copom meeting, the IBGE released GDP data for the fourth quarter of 2007, as well as the results for the whole year. The data showed significant acceleration of growth in the last quarter of 2007, according both to the accumulated change in the year (5.4%, up from 5.1% in the third quarter), and to the year-over-year change (6.2%, up from 5.6% in the previous quarter). On the aggregate demand side, it bears highlighting the acceleration of gross fixed capital formation, which grew 16% year-over-year and, especially the change in the expansion pace of domestic consumption, which tends to be less volatile than investment throughout the cycle, to 8.6% up from 6.0%, according to the same comparison basis. On the aggregate supply side, it bears noticing the acceleration of the services sector, with 5.3% year-over-year expansion, up from 4.6% in the previous quarter.

5. On a three-month moving average basis, according to data seasonally adjusted by the IBGE, industrial output increased 0.2% in February, after retreating 0.3% in the previous month. Still considering the seasonally adjusted series, after the 1.7% month-on-month expansion observed in January, industrial output reduced 0.5% in



BANCO CENTRAL DO BRASIL

February, partially as a result of the technical interruptions in the pharmaceutical sector. It bears mentioning that general industrial output and manufacturing output grew 9.2% in the year. On a year-over-year basis, industrial output shows consistent growth acceleration: 9.7% in February, up from 8.5% in January and 6.3% in December 2007. The data already released for 2008 point, in short, to the continuity of the industrial production expansion cycle, which will continue to be favored by several incentive factors that influence economic activity, such as credit, employment and income expansion, the fiscal impulse and, in some sectors, the recovery of inventory levels.

6. Among the use categories, according to data seasonally adjusted by the IBGE, capital goods production increased significantly in February (3.1%), after stability observed in January. Regarding other use categories, it bears emphasizing the production of durable consumer goods, which increased by 0.9% (5.9% in January). The scenario of solid expansion of capital goods production observed in 2007, mainly driven by the consolidation of positive prospects for the continuity of economic growth, underpinned by the perception of macroeconomic stability consolidation, seems to persist in this year. On its turn, the dynamism of durable consumer goods production reflects, predominantly, the remarkable improvement in credit conditions, when compared to historical patterns. It should be highlighted that the appearance of signs pointing to pressure over the availability of production factors, as suggested in some industrial surveys, indicates that possible reductions in the pace of industrial activity expansion could be associated to productive capacity restrictions.

7. Labor market continues to present quite favorable performance. The unemployment rate in the six metropolitan regions covered by the Monthly Labor Survey (PME) increased, according to the seasonal pattern, to 8.7% in February (a record low for the month in the historical series), up from 8.0% in January and 7.4% in December). As a result, the average unemployment rate in the first two months of the year was 1.2 p.p. below that observed in the same period of 2007. According to data seasonally adjusted by the BCB, the unemployment rate increased to 8.6% in February, up from 8.5% in January, remaining in levels close to the record low of the historical series. In February, average real earnings increased 1.1% month-on-month and 2.5% year-over-year. As a consequence, real payrolls expanded by 6.2% in February, in year-over-year terms (and by 7.1% in January 2008, according to the same comparison basis), and continue to constitute a key driver for sustained aggregate demand growth. According to the National Industry Confederation (CNI) data seasonally adjusted by the BCB, manufacturing employment reduced by 0.1% in February (+0.8% in January). In year-over-year terms, employment grew 4.9%, totaling 4.0% growth in the last twelve months. Still regarding employment, data from the Ministry of Labor and Employment (MTE) indicate the continuity of strong expansion in formal employment at the start of the year, with the creation of 205 thousand jobs in February (up from 142.9 thousand in January), a record high for the month and for the first two-month period of the year. Formal employment grew by 0.5% in the month, seasonally adjusted. Observed data point to a 6.1% expansion in formal employment in February, year-over-year, the highest rate recorded since April 2005, according to this comparison basis, an evidence of strong dynamism in the labor market. The services sector presented the highest hiring rate, with the creation of 74.4 thousand new jobs, followed by the manufacturing industry (46.8 thousand), the best performance of the series for the month, and civil construction (27.6 thousand). The retail sector recorded 13.8 thousand new jobs. The agricultural sector created 25.2 thousand new jobs, a record high for the period, due to the activities related to sugar cane plantations in the Mid-South region and to the soybean plantations.

8. In line with the positive developments in labor market and with credit expansion, retail sales continue to record positive performance, indicating that the pace of domestic demand growth remains robust, and signs of cooling cannot be perceived. Despite the 1.5% decrease month-on-month in February, according to data seasonally adjusted by the IBGE, retail sales grew 12.2% year-over-year, showing acceleration at the margin. It bears highlighting the 22.3% expansion in the sales of "furniture and domestic appliances". The steady growth of retail sales has reflected the performance of both the sectors more sensitive to income and employment expansions and those more sensitive to credit conditions. The expanded retail sales, which also include the sales of "vehicles, motorcycles, parts and pieces" and "construction material", increased 1% in February, month-on-month, according to series seasonally adjusted by the IBGE, and 18.1% year-over-year. For the next quarters, the continuity of the current expanding cycle is expected, and will continue to be underpinned by employment and income growth, credit expansion and the maintenance of consumer confidence at high levels. Sector indicators, for example, relative to automobile sales in the first quarter of the year, corroborate this assessment.



BANCO CENTRAL DO BRASIL

9. The installed capacity utilization rate (Nuci) in the manufacturing industry reached 83.2% in February, unchanged relative to January, according to CNI data seasonally adjusted by the BCB, and remained close to the record high of the series. According to data seasonally adjusted by the CNI, the Nuci in the manufacturing industry reached 82.9%, down from the 83.3% record high observed in November. Without the seasonal adjustment, the Nuci in February stood 1.5 p.p. above the level registered in the same month of 2007. Thus, the average rate of the first two-month period of the year was 1.6 p.p. above the level observed in the same period of 2007. The quarterly Nuci calculated by Fundação Getúlio Vargas (FGV) reached 85.2% in March, according to the observed series, 2.1 p.p. above the level registered in March 2007. For the consumer goods, capital goods and civil construction material sectors, the utilization rates in March were 4.3, 4.4 and 3.4 p.p. above those observed in the same month of 2007, respectively. The reduction of idle capacity, in relation to the margins usually observed, occurs in several sectors despite the significant increase of investment. Indeed, in February 2008, according to seasonally adjusted data, the absorption of capital goods increased firmly (1.8%), due to the vigorous growth of capital goods imports (6.8% in volume) and capital goods production (3.1%). Furthermore, the production of civil construction inputs increased 1.2% in the same period, showing robust performance. Recent data indicate that, although investment has been contributing to soften the increasing trend of capacity utilization rates, it has not been sufficient to contain this process. In this context, the timely maturation of investment projects will be crucial to limit mismatches regarding the evolution of aggregate supply and domestic demand in the relevant forecast period for monetary policy. As stressed in previous Copom Minutes, the inflation trajectory is closely linked to current and prospective developments related to the expansion of supply of goods and services, to adequately meet demand conditions.

10. The trade balance continues to present robust performance, compared to historical patterns, despite the already expected deceleration at the margin, in line with assessments present in Inflation Reports and previous Copom Minutes about important structural changes in Brazilian foreign trade. In the last twelve months through March the trade surplus reached US\$34.1 billion (25.5% below March 2007). Exports and imports totaled US\$165.3 billion and US\$131.2 billion, equivalent to 16.1% and 36.0% growth, respectively, year-over-year. As highlighted in previous Copom Minutes, imports have been growing faster than exports, both due to the strengthening of the BRL and to the robust economic activity in the country, despite the increases in the prices of several commodities included in the Brazilian export basket. The decrease in trade surplus contributed to the US\$4.9 billion current account deficit registered in the twelve months through February 2008, equivalent to 0.4% of GDP. Foreign direct investment reached US\$36.5 billion in the same period, equivalent to 2.8% of GDP.

11. Regarding the external scenario, the process of economic deceleration in the US has consolidated, as evidenced by the economic activity data in the last quarter of 2007 and first quarter of 2008, but uncertainties regarding its magnitude and duration still remain. More recent data about the housing market and consumer goods demand, as well as confidence indices and other leading indicators, point to a significant slowdown. Uncertainties still remain about the length and amplitude of the effects of the US subprime mortgages market crisis over US and European financial institutions and over credit conditions for households and corporate. Despite the dominant opinion still seems to point out to a transitory, but possibly intense deceleration, the negative assessments have become more disseminated. These assessments reflect, to some extent, uncertainties about the capacity of the monetary policy stance implemented by the central bank in the US, to which fiscal incentives will be added, to smooth in a timely manner the US economic weakening, in light of persistent difficulties in the financial system. Despite the reduction of systemic risk perception, due to the Federal Reserve stance and the recapitalization of important institutions, such difficulties, on their turn, could be worsened by a cyclic deterioration in credit quality, which would reinforce the already evident trend to financial contraction, increasing the risk of slowdown intensification. Prospects for economic activity in Europe and Japan, notwithstanding some favorable indicators in Germany, have also deteriorated, despite not provoking the same degree of concerns that surround the US economic activity. On the other hand, strong economic growth in main Asian emerging economies, which so far have been apparently little affected by the US mortgage crisis, has offset the effects of economic deceleration in mature economies. In fact, pressures over production factors availability have triggered inflationary pressures in many emerging economies, many of which are consequently in the midst of monetary tightening cycles. For mature economies, prospects for monetary policy are more diverse. Economies presenting more moderate inflationary pressures and more evident credit contraction tend to present additional monetary policy easing. On the other hand, in economies where inflation rates are at high levels relative to their respective targets, the scope for reaction to the contraction caused by the credit crisis seems more limited. In this context, volatility and risk aversion indicators in international financial markets have remained at quite high levels since the last Copom meeting,



BANCO CENTRAL DO BRASIL

although showing some contraction at the margin. Even if the prices of Brazilian assets present, at different magnitudes, sensitivity to the international scenario, Brazilian economic activity does not seem to have been significantly impacted by the persistent deterioration on global financial markets confidence, and, despite not decoupled from external economic developments, Brazilian economy should sustain its growth trajectory, essentially driven by domestic demand.

12. Oil prices, systematic source of uncertainty stemming from the international scenario, once more increased substantially since the last Copom meeting and continue highly volatile. This behavior reflects structural changes in global energy markets, which have blocked the recovery of inventory levels traditionally observed, in addition to recurrent geopolitical tensions. Despite significant uncertainties inherent to oil prices forecasts, the main scenario considered by the Copom forecasts unchanged domestic gasoline prices in 2008, despite the probability of materialization of an alternative scenario has increased. However, apart from the behavior of domestic gasoline prices, one should recognize that the elevation of international oil prices impacts domestic economy both through productive chains, such as the petrochemical, as well as through the deterioration of inflation expectations. The prices of other commodities, especially grains, which have also increased significantly since the last Copom meeting, despite more pessimism about the prospects for global economic growth and the turmoil on global financial markets, decreased last weeks, but continue to record significant increases in the year.

Assessment of Inflation Trends

13. The identified shocks and their impacts were reassessed according to newly available information. The scenario considered in the simulations utilized the following assumptions:

a) Compared to the assumptions considered in the March Copom meeting, projected adjustments for gasoline and bottled gas prices were both maintained at 0% for 2008;

b) Compared to the assumptions considered in the March Copom meeting, the projections for electricity price adjustments in 2008 were set at 0.1% down from 1.1%, while projections for fixed telephone prices were maintained at 3.5%;

c) The projection for regulated prices inflation, based on individual items, was maintained at 4.0% for 2008. This set of prices, according to data released by the IBGE, corresponded to 30.09% of the total March IPCA;

d) The projection for regulated prices inflation in 2009 was maintained at 4.5%. This projection is based on the endogenous determination model for regulated prices, which computes seasonal components, exchange rate changes, market prices inflation and the IGP (General Price Index) variation;

e) The projection for the spreads over the Selic rate, using a Vector Autoregressive model based on the 360-day swap rates – replacing the model based on the Selic and 180-day swap rates, estimates a 83bps spread in the fourth quarter of 2008, under the benchmark scenario. The swap rate trajectory points to a 55bps spread in the last quarter of 2009. The identified shocks and their impacts were reassessed according to newly available information.

14. Regarding fiscal policy, the projections assume the achievement of 3.8% of GDP for the consolidated public sector primary surplus in 2008 and 2009, adjusted by the possibility of a 0.45 p.p. reduction in this percentage, due to the implementation of the PPI (Investment Pilot Program). The related assumptions considered in the previous meeting were maintained.

15. Since the March Copom meeting, median IPCA inflation expectations for 2008, compiled by the BCB's Investor Relations Group (Gerin), increased significantly to 4.66%, up from 4.41%. Twelve-month ahead inflation expectations increased to 4.38%, from 4.30%, considering the composition of median monthly inflation market expectations. For 2009, inflation expectations increased to 4.40% up from 4.30%.

16. Considering the hypotheses under the benchmark scenario – which assumes the maintenance of the Selic rate at 11.25% and the exchange rate at R\$1.70/US\$ during the forecast period – the projection for the 2008 IPCA



BANCO CENTRAL DO BRASIL

significantly increased compared to the value considered at the March Copom meeting, above the 4.5% target established by the National Monetary Council (CMN) for the year. According to the forecast based on the market scenario – which incorporates the consensus exchange and Selic rates trajectories collected by Gerin on the eve of the Copom meeting – IPCA inflation forecast for 2008 also increased compared to the value considered at the March Copom meeting, and is also above the central target for the year. The projection for 2009 based on the benchmark scenario increased relative to the March Copom meeting, whilst the projection based on the market scenario decreased – in both cases, projections are above the 4.5% target.

Monetary Policy Decision

17. The Copom evaluates that monetary policy should contribute for the consolidation of a favorable long-term macroeconomic environment. Economic activity data indicate that the intensity of demand expansion continues quite robust, showing acceleration in some segments and regions in the first quarter of 2008, and is responsible, at least partially, for the inflationary pressures observed in the short-run, despite strong imports growth and the benign investment behavior. Even in the context of moderate deceleration of global growth this year and the higher volatility observed in global markets since mid-2007, the Committee believes, according to available information, that the balance of payments should not represent imminent risk to the inflationary scenario. On the other hand, there are signs that relevant inflationary pressures are intensifying both in mature and emerging economies, evidencing the existence of inflationary risks on the global outlook. The Copom reaffirms the view, stated in previous minutes, that an alternative scenario of more intense and generalized global deceleration represents an ambiguous risk factor for the Brazilian inflation. On the one hand, by reducing net exports it would act as a factor to restrain aggregate demand. Moreover, the potential decrease of some important commodities prices could contribute to a lower domestic inflation. On the other hand, the above-mentioned alternative scenario could unfavorably impact inflation prospects through two mechanisms. In the case of deceleration in the mature economies that comprise the global financial markets center, risk aversion could increase, resulting in decreased demand for Brazilian assets and depreciation of their prices. In addition, in the medium run, a possible reduction of net exports could similarly affect the price sustainability of certain Brazilian assets. Due to the deterioration of inflation prospects, in a more uncertain scenario, the Committee evaluates that the risk of materialization of a less benign inflationary scenario increased. The Copom emphasizes that the main challenge of monetary policy in this context is to guarantee the maintenance of positive results reached in the last years. Particularly, monetary policy should act so that impacts initially focused on price indices do not result in persistent deterioration of inflation dynamics through a worsening in expectations.

18. The Copom considers that the probability that emerging local inflationary pressures will represent risks to the domestic inflation trajectory has increased, because the heated demand and market of factors, in addition to the possibility of existence of supply restrictions in some sectors, can increase the pass-through of wholesale prices over consumer price inflation. The Committee understands that the prospects for this pass-through, as well as for the generalization of the local pressures initially focused on consumer price inflation, depend in a critical manner on inflation expectations, which increased significantly in the recent weeks, and continue to be carefully monitored. Additionally, it is worth noticing that although the external sector can restrain the inflationary pressures in the tradable sector, heated domestic demand can trigger inflationary pressures in the non-tradable sector, for instance, such as in the services sector. In this context, the Copom will continue to manage the monetary policy stance so that the gains obtained in inflation control in recent years become permanent. In this respect, the Copom will continue to carefully monitor the evolution of inflation and the several core inflation measures, as well as inflation expectations within the forecast period, promptly adjusting the monetary policy stance in order to avoid the consolidation of a scenario where one-off adjustments become persistent or generalized price increases.

19. The preservation of inflation rates in line with the targets path and the consequent consolidation of a long-lasting stable macroeconomic scenario will contribute to the continuous progressive reduction of macroeconomic risk perception that has occurred in the last years. The Copom evaluates that the persistence of a cautious and timely monetary policy stance has been critical to increase the probability that inflation will continue to evolve according to the targets path. For this to materialize, however, it is important that forward-looking inflation indicators, in particular the expected dynamic of aggregate supply and demand, converge during the relevant time for monetary policy.



BANCO CENTRAL DO BRASIL

20. The Committee emphasizes, once again, that there are important time lags in the transmission of monetary policy stance to economic activity and inflation. Therefore, the evaluation of alternative monetary policy stances should necessarily focus on the forward-looking inflation scenario and its risks, instead of current inflation indicators.

21. During the coming months, credit growth and real payroll expansion should continue to bolster economic activity. As mentioned in recent Copom Minutes, the effects of governmental transfers and other fiscal impulses expected for this and the next quarters should also add up to the factors that will sustain demand. These issues become even more relevant considering the clear signs of heated aggregate demand, and the fact that the monetary policy decisions will have concentrated effects in the second half of 2008 and in 2009.

22. The Copom recognizes the important contribution of investment to expand productive capacity. This factor, together with the external sector, has helped to mitigate inflationary pressures, which would be even more intense in their absence. However, the Copom evaluates that the pace of domestic demand expansion, which should continue to be sustained, among other factors, by fiscal transfers and by income and credit growth, continues to present risks to inflationary dynamics. In this context, the consistent reduction of the mismatch between the rhythm of expansion of supply of goods and services and the increase of demand is even more relevant to the assessment of different possibilities of monetary policy stance.

23. Aiming at consolidating a stable and predictable environment, the Copom adopts a strategy to avoid a volatile inflationary trajectory. This strategy takes into consideration the time lags in the transmission mechanisms and has proved to be the most adequate to deal with the uncertainty inherent to the process of monetary policy formulation and implementation. That is the reason why variables such as inflation projections, the balance of risks associated to the forward-looking scenario and especially the preventive stance in the decision-making process of the Copom are so important. At the current moment, characterized by the deterioration in current and expected inflationary dynamics, prudence assumes an even more important role in this process. In the current circumstances, there is the risk is that economic agents start to attribute higher probability that inflation increases will become persistent, which would reduce the efficacy of the monetary policy. Therefore, the Copom's assessment, backed by international experience, is that the performance of monetary policy tends to be more effective to reach their goals more quickly, when the deterioration of inflationary dynamics is in its early stages, rather than when it is consolidated.

24. The Copom evaluates that, in light of signals of economy heating, as illustrated by the acceleration of some wholesale prices and the evolution of core inflation measures, and by the fast increase in inflation expectations, the risks for the concretization of a benign inflationary scenario, in which IPCA would remain consistent with the targets path, are relevant. In fact, the deterioration of the forward-looking scenario is already present in the Committee's inflation projections. The Copom also considers that the persistence of the mismatch between the paces of expansion of aggregate supply and demand tends to increase the probability of such scenario to materialize. In these circumstances, monetary policy should act through the adjustment of the basic interest rate in order to, on the one hand, contribute to the convergence between the paces of expansion of aggregate supply and demand, and on the other hand, avoid that inflationary pressures initially focused on price indices lead to persistent deterioration of expectations and of the inflation forward-looking scenario. By remaining ready to act as the balance of risks to inflation dynamics so requests, the Committee believes that it is, in fact, helping to sustain economic growth, which requires stability, predictability and consequent extension of the planning horizon for businesses and families, as well as to protect the substantial increases in real income of workers observed in recent years.

25. In this context, evaluating the evolution of the macroeconomic scenario and inflation prospects, the Committee unanimously decided to raise the Selic target rate to 11.75% p.a., without bias. The Committee understands that the decision to promptly implement significant part of the adjustment in the basic interest rate will contribute to the timely reduction in the risks for the inflation scenario, reducing, therefore, the magnitude of the total adjustment to be implemented.

26. Under the inflation-targeting regime, the Copom decides according to inflation prospects, the analysis of several alternative scenarios for the evolution of the main variables that determine prospective price dynamics and the balance of risks associated to its projections. Domestic demand continues to expand vigorously, backing-up



BANCO CENTRAL DO BRASIL

economic activity dynamism, including sectors little exposed to external competition, at a time when the effects of important incentive factors are still perceived. On its turn, the contribution of the external sector to a benign inflationary scenario, in light of robust domestic demand growth, seems to become less effective, at a moment when the effects of investment over productive capacity of the economy still need to consolidate. In such environment, the monetary authority should act so that to avoid that short-term uncertainties contaminate longer time horizons. If the risk profile deteriorates in a matter that implies shifts in the basic inflation prospective scenario, the Committee will promptly adjust monetary policy stance to the circumstances.

27. At the conclusion of the meeting, it was announced that the Copom would reconvene on June 3rd 2008, for technical presentations, and on the following day, to discuss the monetary policy decision, as established in Communiqué 16,051 of September 3rd, 2007.

SUMMARY OF DATA ANALYZED BY THE COPOM

Inflation

28. IPCA inflation increased 0.48% in March, up from 0.49% in February and 0.37% in March 2007. In the first quarter of the year, IPCA inflation reached 1.52%, up from 1.26% year-over-year. On a twelve-month trailing basis, the IPCA increased 4.73% in March, up from 4.61% in February.

29. Food prices increased 0.89% in March, up from 0.60% in previous month, contributing 0.2 p.p. to the monthly IPCA result. Housing and transportation, which increased by 0.65% and 0.42%, respectively, contributed both 0.09 p.p. to the IPCA monthly result. Market prices decelerated, increasing 0.48%, down from 0.66% in February, while regulated prices registered inverse trend, with a 0.47% increase, up from 0.10% in the previous month. On a twelve-month trailing basis through March, market prices expanded by 6.03% and regulated prices, 1.83%, up from 5.98% and 1.57%, respectively, in the previous month. Amongst market prices, in the last twelve months, the prices of tradable goods increased to 5.33% in March, up from 5.00% in February, while the prices of non-tradable goods decelerated, to 6.67%, down from 6.89%, following the same trend of the prices of services, which increased 5.11% in March, down from 5.19% in February, according to the same comparison basis.

30. Trimmed means core inflation measures accelerated and, for seasonal reasons, the core excluding household food and regulated prices decelerated in March, while on a twelve-month trailing basis the three measures increased, compared to February. The core excluding household food and regulated prices increased 0.36% in March, down from 0.69% in February, totaling 4.41% in the last twelve months (the highest rate since May 2006) and up from 4.27% in the previous month. The smoothed trimmed means core increased 0.39% in March, up from 0.27% in February, totaling 4.16% in the last twelve months. The non-smoothed trimmed means core increased 0.41% in March, up from 0.36% in February, accumulating 4.01% in the last twelve months, also the highest rate since May 2006.

31. IGP-DI inflation increased 0.70% in March, up from 0.38% in February, accumulating 2.08% in the first quarter of the year and 9.18% in the last twelve months. The three index components accelerated in the month, with highlights to food prices, both at wholesale and consumer levels. IPA-DI inflation increased 0.80%, up from 0.52% in the previous month, totaling 11.39% in the last twelve months. IPC-Br inflation increased 0.45% in March, after stability in February, accumulating 4.52% in twelve months. INCC inflation increased 0.66% in March, up from 0.40% in February, reaching 6.69% in twelve months.

32. The IPC-Br acceleration reflected the behavior of five out of the seven groups, with highlights to food (0.62% up from -0.38%) and housing (0.47% up from 0.09%). At the wholesale level, both agricultural and industrial prices increased in March, highlighting the elevations in the prices of tomato, composed fertilizers, bovines, iron ore, *in natura* milk, while soybean, manioc, coffee, corn and poultry were the main negative drivers.

Economic Activity



BANCO CENTRAL DO BRASIL

33. According to IBGE's monthly survey (PMC), retail sales increased 12.2% in February 2008, year-over-year, with generalized growth sales in all segments, mainly driven by office, computing and communication equipment and material (38.9%); other items for domestic and personal use (27.5%); furniture and home appliances (22.3%); books, newspapers, magazines and stationery (17.9%); and pharmaceutical, medical, orthopedic and perfumery items (14.1%). Expanded retail sales, which include the activities vehicles, motorcycles, parts and pieces, and construction material, increased 18.1%, influenced by the expansions of 30.5% in the automotive sector and 19.0% in construction material.

34. Retail sales declined 1.5% in February, month-on-month seasonally adjusted, recording 12.4% growth in the sales of office, computing, and communication material and equipment, and declines in fabric, clothing and shoes (4%); hyper- and supermarkets sales, food products, beverages and tobacco (3.8%); and fabric, pharmaceutical, medical, orthopedic and perfumery items (2.8%). Expanded retail sales increased 1% in February, month-on-month seasonally adjusted, as a result of increases in the sales of vehicles and motorcycles (5.2%) and construction material (3.6%).

35. According to São Paulo Trade Association (ACSP) data, related to the city of São Paulo and seasonally adjusted by the BCB, the consultations to the Usecheque system and database consultations for credit sales in March increased, respectively, 4.5% and 1.1% month-on-month. Year-over-year, there were respective increases of 3.2% and 3.5%. In the first quarter of 2008, these indicators increased 6.5% and 6.3%, respectively, compared to the same period of 2007.

36. Regarding investment indicators, the production of construction inputs and domestic production of capital goods increased by 1.2% and 3.1% in February, month-on-month seasonally adjusted. These indicators grew 12.9% and 25.0%, respectively, year-over-year. Still according to this comparison basis, the positive evolution of capital goods production reflects mainly the good performances in the following sectors: agricultural equipment (57.5%), equipment linked to investment in infrastructure, such as transportation equipment (35.3%), construction (26.3%) and energy (19.9%).

37. Capital goods imports increased month-on-month 6.8% in February, according to data from Fundação Centro de Estudos do Comércio Exterior (Funcex), seasonally adjusted by the BCB. Confirming the expansionist trajectory of investments in Brazilian economy, capital goods imports increased 55.3% year-over-year.

38. CNI indicators, seasonally adjusted by the BCB, showed expansion of industrial activity in February, month-on-month, with increases of 1.0% in industrial real revenues and 0.6% in hours worked in production. Compared to February and the first two months of 2007, industrial real revenues increased 11.5% and 10.9%, respectively, and hours worked in production, 8.8% and 7.8%, in the same order. Installed capacity utilization (Nuci) reached 83.2% in February, remaining relatively stable month-on-month seasonally adjusted, and increased 1.5 p.p. year-over-year, according to the observed series.

39. According to IBGE's Monthly Industrial Survey (PIM), on a month-on-month basis, industrial production decreased 0.5% in February, while the three-month moving average remained stable. These results were influenced by the 33.2% decline in monthly pharmaceutical production, which responds for approximately 4.3% of industrial production, reflecting the effects of technical interruptions in an important company in the sector. Fourteen out of the twenty seven activities surveyed recorded production increase in February and, by use categories, the production of capital goods and durable consumer goods increased by 3.1% and 0.9%, respectively. The production of intermediated goods showed relative stability (-0.2%), after two consecutive months of positive results, expanding by 2.2%. The production of semi-durable and non-durable consumer goods declined 3.9%, mainly reflecting the interruption in the pharmaceutical industry previously mentioned. Year-over-year, industrial activity increased 9.7%, with expansion in all use categories, with highlights to the increases of 25% in capital goods production and 20.7% in durable consumer goods production. In the first two months of 2008, these rates reached 9.2%, 19.9% and 18.1%, respectively, year-over-year. In the same period, the production of intermediate goods and semi- and non-durable consumer goods expanded by 9.2% and 3.5%, respectively. On a twelve-month trailing basis, industrial output expanded 6.8% in February, up from 6.3% in January, showing acceleration at the margin, contrary to month-on-month and the three-month moving average seasonally adjusted data comparisons.



BANCO CENTRAL DO BRASIL

40. Vehicles production reached 280.6 thousand units in March, according to Anfavea, increasing 13.4% year-over-year. Total sales of vehicles increased 9.8%, with a 17.1% expansion in domestic sales and an 8.8% contraction in exports relative to March 2007. Considering seasonally adjusted data, the production of vehicles increased 2.5% month-on-month, with expansions in the production of automobiles and light commercial vehicles (1.9%) and trucks (1.7%), and a 1.5% decrease in the production of buses. Year-over-year, the production of the same items changed 13.3%, 21.5%, and -0.6%, respectively. Considering seasonally adjusted data, the production of agricultural machinery decreased by 6% month-on-month, but expanded by 33.2% relative to March 2007 and by 56.2% in the first quarter, year-over-year.

41. According to the survey carried out by the IBGE in March, the grains harvest should reach 140.5 million tons in 2008, increasing 5.6% year-over-year. Planted area was estimated at about 46.5 million hectares, a 2.5% increase relative to March 2007, being the plantations of corn and soybean responsible for 76% of the total. Good weather conditions have been contributing to the confirmation of the expected favorable results, with highlights for the growth in the productions of rice and soybean (8.1% and 3.4%, respectively) and in the first harvest of corn (7.5%). The survey also estimated a 7.9% increase in sugar cane production, with an 8.0% expansion in planted area, and a 22.9% increase in coffee production.

Surveys and Expectations

42. The Fecomercio-SP survey showed a 0.4% month-on-month elevation in the Consumer Confidence Index (ICC) in March, reflecting the 0.7% increase in the Consumer Expectations Index (IEC), while the Current Economic Conditions Index (Icea) remained stable. The ICC grew by 15.2% year-over-year, due to expansions of 15.7% and 14.9% in the Icea and IEC, respectively.

43. According to the FGV survey, the ICC grew 3.5% in March, month-on-month. This result reflected a 5.2% increase in the Current Situations Index (ISA) and a 2.6% elevation in the Expectations Index (IE), which computes 6-month ahead expectations. The survey registered increases of 12.1%, 25.7% and 5.6% in the ICC, ISA and IE, respectively, year-over-year.

44. Still according to the FGV, the Industry Confidence Index (ICI) increased 5.8% in March, month-on-month. The same index increased by 4.5% in March, up from 3.7% registered in February, both in year-over-year terms, after four consecutive months of deceleration. The IE expanded by 8.3% and the ISA grew by 3.8%, month-on-month, and 4.4% and 4.7%, respectively, in year-over-year terms. Amongst the IE components, it is noteworthy the monthly nine-point growth of the six-month ahead business conditions, approaching the record of the series, occurred in July 2000. According to the same comparison basis, expected employment and output both increased eleven points, showing the continuation of favorable expectations of businessmen for the near future.

45. According to the FGV Manufacturing Industry Survey, installed capacity utilization (Nuci) reached 85.2% in March, standing 0.5 p.p. above the February level and 2.1 p.p. year-over-year. The Nuci reached 89.9% in capital goods industry, a 4.4 p.p. growth relative to March 2007, reaching a record high. Nuci also grew 1.4 p.p. in the consumer goods industry and 0.4 p.p. in intermediate goods industry, but retreated 1.3 p.p. in the construction inputs industry, according to the same comparison basis. The same survey showed that, based on either planning or investment decisions already approved by their boards, firms expect a 11% expansion in manufacturing installed capacity, on average, for 2008 and 22% for the 2008-2010 period, the highest rates in five years. According to the same firms, the current level of the domestic demand and the expected returns of new investments were the key drivers for investment decisions.

Labor Market

46. According to the Ministry of Labor and Employment, 205 thousand new formal jobs were created in February 2008, totaling 347.9 thousand year-to-date, a record high for the month and for the two-month period. Employment level increased by 0.5% month-on-month in seasonally adjusted terms, expanding in all sectors, with highlights to the 1.6% expansion in the construction sector and the creation of 74.4 thousand new jobs in the



BANCO CENTRAL DO BRASIL

services sector. In the first two-month period, year-over-year, employment expanded by 6%, with highlights to the 15.5% expansion in the construction sector.

47. According to the IBGE employment survey (PME) in the six main metropolitan areas of the country, the unemployment rate reached 8.7% of economically active population (PEA) in February, a record low for the month in the historical series. Considering seasonally adjusted data, the rate remained almost stable, recording 8.6% against 8.5% in January. Year-over-year, the unemployment rate reduced 1.2 p.p., reflecting a 3.6% increase in the number of employed workers, 732 thousand, and a 2.3% expansion in the PEA. Formal workers in the private sector increased 8.4%, according to the same comparison basis, representing 722 thousand jobs, while the number of informal workers decreased 3.4%, with the reduction of 96 thousand jobs. The number of self-employed workers grew by 1.9% in the same period.

48. The same survey showed that average real earnings of occupied workers grew 1.1% in February month-on-month and 2.5% year-over-year, reaching the highest value since December 2002. Real payrolls increased 0.6% in February month-on-month and 6.2% year-over-year.

49. According to CNI data seasonally adjusted by the BCB, employment in manufacturing industry retreated 0.1% in February, month-on-month, and increased 0.5%, year-over-year. In the first two-month period of 2007, employment and real payroll in the manufacturing industry increased by 5.0% and 13.0%, respectively.

Credit and Delinquency Rates

50. Credit operations in the financial system expanded by 1.1% in February, expanding by 27.9% on a twelve-month trailing basis. According to the same comparison bases, non-earmarked credit operations increased 1.3% and 32.8% respectively, while earmarked credit operations elevated 0.6% and 17.4%, respectively. Among the non-earmarked operations, leasing operations remained strong, with expansions of 120.8% and 78.9% for credit to individuals and to corporate, respectively, in the last twelve months. Regarding earmarked credit, it bears highlighting the 24.1% and 17.7% increases in operations related to housing and the agricultural sector, respectively, according to the same comparison basis. Considering other sectors, loans to industry increased 1% month-on-month and 30.6% in twelve months, in February, while credit to commerce expanded by 0.8% and 26.8%, according to the same comparison bases.

51. The average interest rate on non-earmarked credit operations, used as reference for interest rates, reached 37.4% p.a. in February, standing 0.1 p.p. above the January result. The average rate on credit for individuals reached 49.0% p.a., up from 48.8% p.a. in the previous month. The average rate on corporate credit increased 0.1 p.p. in the month, reaching 24.8% p.a.

52. The average tenure of non-earmarked credit operations, used as reference for interest rates, reached 369 days in February, compared to 371 in January and 302 in the same month of the previous year. The average tenure of corporate credit operations decreased 4 days in February, reaching 303 days, while the average tenure for credit operations to individuals totaled 447 days, up from 376 days in February 2007.

53. Delinquency rates in the financial system (non-earmarked loans in arrears for more than ninety days) reached 4.3% in February, a 0.7 p.p. decrease relative to the same month of 2007. Delinquency rates for credit operations with corporate and individuals reached 2.0% and 7.1%, respectively, decreasing by 0.8 p.p. and 0.2 p.p. in the period.

54. Net delinquency rate for retail credit, measured by the ACSP, reached 7.6% in March, up from 7.1% in the same month of 2007.

External Environment

55. The perception of a longer and more severe deceleration in the US economic activity has increased and negative spillovers on global economic performance have been expected. The Federal Reserve recognizes a slight recession in the first semester in the US economy, followed by a modest recovery in the second half of the year.



BANCO CENTRAL DO BRASIL

56. In Europe, the fears regarding the UK real estate market increased. After several banks had adopted more restrictive policies to mortgage grants, real estate prices fell 2.5% in March, the greatest retraction of the last sixteen years. Economic growth in the Euro Area cooled in the last three months of 2007, as government and consumer expenditures reduced. According final data released, GDP in the thirteen countries that adopted the Euro increased 0.4% in the fourth quarter, quarter-over-quarter, and 2.2%, year-over-year.

57. At the beginning of 2008, it is important to notice, the persistent characteristic of inflation, even in light of global deceleration. Food and energy remain driving inflation, which spreads worldwide. In addition to increases in large economies, it bears emphasizing inflation rises in Hong Kong (6.3%), India (6.11%) and Saudi Arabia (8.7%, the highest rise in 27 years). Similar situation concern the central banks in Latin America, Russia and Philippines, among others.

58. In China, inflation reached a record high in twelve years, 8.7% p.a. in February, mainly driven by food prices, which increased 23.3% only in February. In the US, activity cooling has offset inflationary pressures stemming from food and energy prices, added to the effect of the devaluated exchange rate.

Foreign Trade and International Reserves

59. In March 2008, Brazilian trade surplus reached US\$1 billion, totaling surpluses of US\$ 2.8 billion in the year and US\$ 34.1 billion in the last twelve months. In the first quarter of the year, exports reached US\$38.7 billion, and imports, US\$35.9 billion, growing by 13.8% and 41.8%, year-over-year.

60. In March, exports totaled US\$12.6 billion, reaching a US\$630.7 million daily average, a 7.6% growth year-over-year. Imports totaled US\$11.6 billion in March, with a US\$580.1 million daily average, a 33.2% increase year-over-year. Imports, both in value and in daily average terms reached record highs for the month.

61. International reserves totaled US\$195.2 billion in March, with increases of US\$2.3 billion in the month and US\$14.9 billion, compared to the end of 2007.

Money Market and Open Market Operations

62. In the period between the March and the April Copom meetings, the yield curve shifted upwards in all extension, with a slope increase. This movement was mainly driven by the economic agent's perception about the March Copom Minutes and the Quarterly Inflation Report, the release data for inflation above market expectations, the increase of inflation expectations and the worsening of the external outlook. Between March 3rd and April 14th, one-, three-, and six-month rates went up by 31 bps, 50 bps and 70 bps, respectively. Moreover, one-, two- and three-year rates increased by 95 bps, 88 bps and 90 bps, respectively. Real interest rates, measured by the differential between the one-year forward nominal interest rate and the smoothed twelve-month ahead inflation expectations, increased to 8.07% on April 14th, up from 7.31% on March 3rd.

63. On March 26th, the BCB carried out reverse FX swap auctions amounting US\$2.0 billion, with the total rollover of the April 1st redemptions.

64. In its open market operations, the BCB carried out, from March 4th to April 14th, weekly five- and seven-month fixed rate repo operations, borrowing. The average daily balance of these operations reached R\$84.6 billion, of which R\$59.0 billion were seven-month operations. In the same period, the BCB conducted 30 overnight repo-borrowing operations. The BCB also conducted daily liquidity management operations with tenures up to two working days. Operations with tenors less than thirty days, including daily liquidity management operations, averaged R\$29.1 billion, borrowing. In addition, on March 6th, 17th and 26th and on April 1st, the BCB conducted borrowing operations with tenure of 29, 9, 16 and 12 working days, respectively, amounting R\$83.8 billion, R\$8.9 billion, R\$19.9 billion and R\$29.2 billion. These operations totaled R\$108.6 billion on a daily average basis.



BANCO CENTRAL DO BRASIL

65. Between March 4th and April 14th, the National Treasury raised a total of R\$28.2 billion, of which R\$13.1 billion in fixed-rate securities: R\$9.7 billion via issuance of LTNs maturing in 2008, 2009 and 2010, and R\$3.4 billion in NTN-Fs maturing in 2012, 2014 and 2017. Issuance of LFTs totaled R\$9.7 billion, for securities maturing in 2012 and 2014. Issuance of inflation-linked NTN-Bs reached R\$5.4 billion, for securities maturing in 2011, 2013, 2017, 2024, 2035 and 2045.

66. In the same period, the Treasury conducted auctions to sell LTNs maturing in October 2008, and April and July 2009 and bought LTNs maturing in April and July 2008, totaling R\$2.8 billion. Issuance of inflation-linked NTN-Bs for securities maturing in 2011, 2013, 2017, 2024, 2035 and 2045, settled in other National Treasury securities, totaled R\$4.9 billion. The Treasury also conducted sales auctions of LFTs maturing in 2012 and 2014, which totaled R\$2.2 billion, receiving LFTs maturing in 2008 as payment, and purchase auctions to buy LTNs and NTN-Bs, totaling R\$2.0 billion and R\$0.3 billion, respectively.