BANCO CENTRAL DO BRASIL

Minutes of the 146th Meeting of the Monetary Policy Committee (Copom)

Summary

Date: October 20th, from 4:50PM to 6:45PM, and October 21st, from 4:45PM to 6:30PM
Place: BCB Headquarters meeting rooms - 8th floor on October 20th and 20th floor on October 21st – 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 October 20th)
Altamir Lopes – Economic Department
Carlos Hamilton Vasconcelos Araújo – Research Department (also present on October 21st)
João Henrique de Paula Freitas Simão – Open Market Operations Department
Jose Antonio Marciano - Department of Banking Operations and Payments System
Marcio Barreira de Ayrosa Moreira – International Reserves Operations Department
Renato Jansson Rosek – Investor Relations Group

Other participants (present on October 20th)
Adriana Soares Sales – Advisor to the Board
Alexandre Pundek Rocha – Advisor to the Board
Eduardo José Araújo Lima – Advisor to the Research Department
Fabio Araujo – Advisor to the Research Department
Katherine Hennings – Advisor to the Board
José de Ribamar Oliveira Júnior – Press Secretary

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

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Recent Economic Developments

1. IPCA inflation increased to 0.24% in September up from 0.15% in August, returning to the level observed in July. As a consequence, in the year through September inflation reached 3.21%, decreasing 1.54 p.p. relative to the same period of the previous year. In the last twelve months, inflation reduced to 4.34% in September down from 4.36% in August (5.90% in December 2008 and 6.25% in September 2008), remaining near the target. The deceleration of twelve-month consumer price trailing inflation in the first nine months of the year mirrored the behavior of market prices, as regulated price inflation increased. Considering market prices, both prices of tradable and non-tradable goods cooled on a twelve-month trailing basis, reaching 3.38% and 5.41%, respectively, in September, down from 6.99% and 7.10% in December 2008 (6.78% and 8.49% in the same month of the previous year). However, according to the same comparison basis, the prices of services, whose dynamics tends to show more persistence than that of the prices of goods, increased to 6.84% in September up from 6.39% in December (6.27% in September 2008). Preliminary data for October point to consumer inflation above the level observed in September. In short, information available suggest that the inflationary acceleration cycle observed last year has been gradually overcome by a process led by the behavior of market prices, specially goods, while regulated price and services inflation continue to show more persistence.

2. The three main underlying inflation measures calculated by the BCB increased between August and September. The core inflation by exclusion of household food items and regulated prices changed from 0.23% in July to 0.29% in August and 0.35% in September. Smoothed and non-smoothed trimmed means core inflation measures also accelerated, recording 0.30% and 0.21% in July, 0.25% and 0.18% in August and 0.39% and 0.31% in September, respectively. The twelve-month trailing inflation measures changed from 6.09%, 4.82% and 4.92% in December to 5.04%, 4.30% and 3.54% in September, for the core inflation by exclusion, smoothed and non-smoothed trimmed means core inflation, respectively. Moreover, it bears emphasizing that the behavior of the IPCA diffusion index reduced from 61.7% in December to 54.2% in September (compared to 60.9% in September 2008).

3. The General Price Index (IGP-DI) inflation changed from -0.64% in July to 0.09% in August and 0.25% in September. On a twelve-month trailing basis, the IGP-DI inflation changed from -1.00% in July to -0.53% in August and -0.65% in September (11.90% in September 2008). The slowdown of the IGP-DI has basically reflected the behavior of all its three components. Its main component, the Wholesale Price Index (IPA-DI), reached -3.40% in the last twelve months through September (14.33% in September 2008). On its turn, the Consumer Price Index-Brazil (IPC-Br) increased 5.02% in September (5.6% in September 2008) and the Civil Construction National Index (INCC) increased 4.27% (11.88% in September 2008). Regarding the IPA-DI, the inflationary deceleration, under this comparison basis, derives basically from the behavior of both agricultural and industrial prices. The agricultural IPA reached -3.72% (15.84% in September 2008), while wholesale industrial prices reached -3.30% (13.78% in September 2008). As mentioned 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. The IBGE released Q2 2009 GDP data, which showed a 1.2% contraction in activity, under the criterion of the year-over-year comparison. From the aggregate demand side, expansion was led by the household consumption and public administration consumption, which increased 3.2% and 2.2%, respectively, year-over-year. Gross fixed capital formation, exports and imports contracted 17.0%, 11.4% and 16.5%, respectively, according to the same comparison basis. The contribution of domestic absorption to output growth was -1.9 p.p. in the second quarter of 2009, year-over-year, overweighing the 0.7 p.p. positive contribution of the external sector. From the aggregate supply side, still according to the year-over-year basis, the services sector performed positively, with a 2.4% growth, year-over-year, while all the other sectors contracted. The GDP deflator measured by market prices, according to the same comparison basis, changed from 7.4% in the fourth quarter of 2008, to 4.7% in the first quarter of 2009 to 4.9% in the second quarter of 2009.

5. On a three-month moving average basis, according to data seasonally adjusted by the IBGE, industrial output increased 1.3% in July and August. Still considering the seasonally adjusted series, industrial output increased by 2.2% in July and 1.2% in August, month-on-month, the eighth consecutive month of expansion. On a year-over-year basis, industrial output retreated by 10.0% in July and 7.2% in August, with respective falls of 7.0% and 10.3% in manufacturing and mining industries. The analysis of the behavior of IBGE industrial output series, and its

components, suggests that production reached its record low in December-January, and has been followed by gradual recovery. However, industrial activity recovery continues to be influenced by the international outlook, by business and households' expectations, as well as by the developments of domestic financial conditions.

6. Among the use categories, according to data seasonally adjusted by the IBGE, similarly to the observed in July, it bears highlighting the 3.1% increase in August in the durable consumer goods production, strongly influenced by the automotive sector. Regarding the other use categories, intermediate goods production increased 0.7%, non-durable and semi-durable consumer goods production increased 0.6%, while the production of capital goods increased by 0.4%. The recovery, at the margin, in the dynamism of industrial production, led by production of durable goods, reflects, to a great extension, tax exemption measures and also some easing in credit conditions. The future behavior of industrial production recovery, which should not be uniform over time, will depend on these factors, as well as on the evolution of consumer and businessmen confidence, counterbalancing the still emerging recovery of external demand.

7. Labor market has behaved more favorably, with resilient aspects prevailing over signs of loss of strength. The unemployment rate in the six metropolitan regions covered by the IBGE Monthly Labor Survey (PME) changed from 8.0% in July to 8.1% in August (7.6% in August 2008). According to the seasonally adjusted series, the unemployment rate remained unchanged at 8.0%, the same level reached in June and July. Average real earnings increased by 2.2% in August, in year-over-year terms. Employment, on its turn, expanded by 0.9% in August, according to the same comparison basis. As a consequence, real payroll reached 3.2% in August, continuing to constitute a key driver for domestic demand growth. Still regarding the labor market, data from the Ministry of Labor and Employment (MTE) indicate that the generation of formal employment has continued to record significant recovery. In September, 252.6 thousand jobs were created (compared to the positive result of 242.1 thousand in August), representing the second best result for the series in the month. The manufacturing industry showed positive balance of 123.3 thousand jobs, the sixth consecutive month of expansion and the best result of the series for the month. Similarly, the commerce sector continued the recovery trajectory initiated in April, with the positive result of 50.3 thousand jobs. Also, the civil construction sector, the most dynamic one with a 5.9% cumulative growth in 2009, and the services sector continued hiring workers this month: 32.7 and 62.8 thousand jobs, respectively. The agricultural and livestock sector, on its turn, lost 17.1 thousand jobs.

8. According to data seasonally adjusted by the IBGE, expanded retail sales increased by 3.3% in August, after retraction of 5.7% in July. On a year-over-year basis, the indicator increased by 5.5%, growing by 3.7% in the year. The three-month moving average of expanded retail sales reached 1.3% in August, according to seasonally adjusted data, after recording 1.7% in July. On a month-on-month basis, according to seasonally adjusted data, it bears emphasizing the expansion in the sales of "vehicles, motorcycles, parts and pieces" (2.5%) and "hyper-, supermarket, food products, beverages and tobacco" (1.4%). The negative key drivers were "office material and equipment" (-4.9%) and "fabric, clothes and shoes" (-2.0%). In the year, cumulative growth was more significant in "office, information technology and communications material and equipment" (13.3%) and "pharmaceutical and medical products" (12.5%). After consecutive falls in the last months of 2008, expanded retail sales data have evidenced recovery, mainly influenced by the increase in the sales of vehicles, in response to sector incentives granted by the government and to the improvement in the access to vehicle credit supply. For the next quarters, the retail sales trajectory will continue to be sustained by fiscal transfers, as well as by real payroll growth, whose evolution should be favored by the reduction of inflation, but it will also be affected by the recovery in the access to credit supply, influenced by the lagged effects of monetary policy and by the evolution of consumer confidence.

9. The installed capacity utilization rate (Nuci) in the manufacturing industry reached 79.9% in August, below the level observed in July, according to CNI data seasonally adjusted by the BCB, but 1.91 p.p. above the record low reached in January. The series seasonally adjusted by CNI changed from 79.9%, in July, to 80.1%, in August. Considering the monthly series without seasonal adjustment, in August the Nuci was 2.6 p.p. below the level registered in the same month of 2008. On its turn, the monthly Nuci without seasonal adjustment, calculated by Fundação Getúlio Vargas (FGV), increased in September to 82.8%, up from 81.6% in August, 3.5 p.p. below the level observed in the same month of 2008. The reduction in the Nuci according to the year-over-year comparison is also observed in the production of consumer goods (-2.9 p.p.), intermediate goods (-2.7 p.p.), capital goods (-11.1 p.p.) and construction inputs (-1.4 p.p.). The same indicator, seasonally adjusted by FGV, changed from 81.3% in August to 81.9% in September, increasing 4.30 p.p. relative to the record low observed in February, and is close to

the average of the series. The reduction on the Nuci calculated by CNI and FGV, according to the same comparison basis, results from a combination between the maturity of investment projects and accommodation of economic activity, and points to some idle capacity in the manufacturing industry. Data regarding the absorption of capital goods show retraction compared to the same periods of 2008 and expansion at the margin. The absorption of capital goods data indicate stability in August (after a 7.9% increase in July), a 3% increase in the quarter ended in August, compared to the quarter ended in May, according to seasonally adjusted data, and a decrease of 20.9% in year-over-year terms, according to observed data. On its turn, the production of construction inputs increased by 0.8% at the margin in August (2.8% increase in the quarter), after a 2.1% decrease in July, accumulating a 9.6% fall in the year. In short, evidences suggest that demand pressures over the productive capacity level of the manufacturing industry are contained, although the utilization rates have increased in the last months. 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 twelve-month cumulative trade balance reduced at the margin. According to the same comparison basis, the trade surplus reached US$28.0 billion in August, decreasing to US$26.5 billion in September. This total resulted from US$ 158.9 billion in exports and US$132.3 billion in imports, equivalent to -18.5% and -20.3% changes, respectively, year-over-year. The greater resilience of domestic demand relative to the external demand contributes to the recent narrowing of trade surplus. The reduction in remittances of profits and dividends, on its turn, has contributed to limit the twelve-month trailing current account deficit, which reached US$28.2 billion in December 2008, decreasing to US$17.6 billion in August, equivalent to 1.3% of GDP. On its turn, foreign direct investment reached US$36.3 billion in the twelve months through August, equivalent to 2.8% of GDP.

11. The period since the last Copom meeting was marked by the continuity of stress reduction in international financial markets, despite not in a monotonic way. The unprecedented actions taken by the authorities in mature economies, using a wide range of instruments, in order to ensure minimum conditions of operation and liquidity in monetary markets, have continued to moderate the perception of systemic risk. In this environment, the signs of reduction in risk aversion continue, as evidenced by the behavior of international equity markets, although this process remains subject to reversals. Anyway, the improved trend of risk aversion and of the scarcity of capital flows, as well as some concern among investors about the fiscal situation in the US, continued to encourage the recovery of currencies, both from emerging and mature economies, against the US dollar.

12. Regarding the global macroeconomic scenario, contraction trends prevail over inflationary pressures, but recovery of economic activity seems to have been consolidating. The current predominant view points to the contraction of global economic activity in 2009, followed by recovery in 2010. The consensual projections point to a retraction of activity in the US, Europe and Japan (G3), which wouldn't be totally offset by the economic dynamism of some emerging economies, especially in Asia. However, there are evidences of gradual recovery in the economic activity, but still subject to reversals, particularly due to the weakness in the labor market and economic activity in G3. On the other hand, the risk that the problems in the international financial system become aggravated by the cyclical deterioration in the quality of credit - which could contain the distension in financial conditions and, as a consequence, hinder the consolidation of economic recovery - still persists, but it seems to be reducing. Therefore, the prospect of deflation in mature economies has retreated, despite the persistence, on a twelve-month trailing basis, of the disinflation process in several emerging economies. In this context, after a period of aggressive monetary policy easing, in a significant number of countries, monetary policy seems to have begun a phase of stability and, in some cases, started a period of reversing the stimulus introduced during the sharpest international contraction period, whereas the increase in public sector debt imposes limits on the scope of any additional fiscal stimuli.

13. Oil prices, including future markets quotations, have increased significantly since the last Copom meeting. Uncertainty concerning these quotations remains high, as the prospective scenario depends on the evolution of demand, in the context of global economic recovery, on the prospects for the evolution of global supply, subject to the pace of investments maturation in the sector, in addition to the geopolitical issues that affect the price of this commodity. Nonetheless, despite the high uncertainty inherent to the projections regarding the trajectory of oil prices, the main scenario adopted by the Copom assumes unchanged gasoline prices in the rest of 2009. However, it bears highlighting that, regardless the behavior of domestic gasoline prices, the evolution of international oil prices can affect domestic prices through productive chains, such as the petrochemical, as well as through the

potential effect over inflation expectations. It bears emphasizing that the behavior of agricultural commodity prices, which have particularly important impact in the evolution of food costs, such as wheat, soybeans and corn, had heterogeneous behavior since the last Copom meeting, while quotations of metallic industrial commodities, such as aluminum, copper, and nickel, showed relative stability.

Assessment of Inflation Trends

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

a) similarly to the September Copom meeting, the projected adjustments for gasoline prices for 2009 were kept unchanged at 0%, while the projection for bottled gas prices rose from 6.9% to 11.2% in the same period;
b) regarding the projected adjustment for fixed telephone and electricity prices for 2009, the first one reduced to 0.3% from 1.1%, percentage considered in the September meeting, while the second reduced from 5.4% to 4.8%;
c) the projection for regulated prices inflation for 2009, based on individual items, was kept unchanged at 4.5%. This set of prices, according to data released by the IBGE, corresponded to 29.56% of the total September IPCA;
d) the projection for regulated prices inflation for 2010 was reduced to 4.0% from 4.3% considered in the September meeting. Such projection is based on the endogenous determination model for regulated prices, which computes, among other factors, seasonal components, foreign exchange rate changes, market prices inflation and the IGP (General Price Index) variation;
e) the projection for the spreads over the Selic rate, based on the 360-day swap rates, on the benchmark scenario, estimates a 94bps spread in the fourth quarter of 2009 and a 47 bps spread in the last quarter of 2010.

15. Regarding fiscal policy, projections assume the achievement of a public sector primary surplus target of 2.5% of GDP in 2009 and 3.3% in 2010, unchanged relative to the September meeting. Those figures do not take into account Petrobras contribution to the public sector primary surplus and are adjusted by the possibility of reduction by up to 0.50 p.p. in 2009 due to the implementation of the Investment Pilot Program (PPI), and in up to 0.65 p.p. in 2010, due to the PPI implementation and the Growth Acceleration Program (PAC). The additional assumptions considered in the previous meeting remained unchanged.

16. Since the last Copom meeting, the median of the expectations compiled by the BCB's Investor Relations Group (Gerin) for the 2009 IPCA remained relatively stable (4.30% in comparison to 4.29% at the September meeting). For 2010, the median of inflation expectations increased to 4.41%, up from 4.30%.

17. Considering the hypotheses under the benchmark scenario – which assumes the maintenance of the exchange rate at R$/US$ 1.70 and the Selic rate at 8.75% p.a. during the forecast period – the projection for 2009 inflation slightly increased relative to the figure considered at the September Copom meeting, but remained below the 4.5% target established by the National Monetary Council (CMN). According to 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 2009 remained stable and, therefore, below the inflation midpoint target. For 2010, under the benchmark scenario, the projection remained stable relative to the figure considered in the September meeting and, therefore, is close to the midpoint target, whereas the projection under the market scenario increased, although remaining close to 4.5%.

Monetary Policy Decision

18. The Copom evaluates that the monetary policy should contribute to the consolidation of a favorable long-term macroeconomic environment. The risk aversion and the liquidity conditions prevailing in international markets continue to show a normalization trend at the margin. In fact, since the last Copom meeting, signs of global risk aversion reduction have continued to accumulate, despite still subject to reversion, with impacts over both Brazilian

asset prices, as well as over selected commodities, which had also been influencing domestic financial conditions. However, it bears emphasizing that the trajectory of price indices still evidences reduction of external inflationary pressures. Consequently, the impact of the international scenario over the domestic inflation path continues to be, until present, predominantly benign. On its turn, the possible consolidation of the world economy recovery, which, to a certain extent, has been reproducing the disequilibrium observed in the period prior to the 2008 crisis, might impact, although in a heterogeneous fashion, the global inflationary dynamics. On the top of this, it should be added the uncertainty generated by the effects of the unprecedented liquidity expansion on mature economies, over the price behavior of both assets and commodities. The Copom emphasizes that the main challenge of monetary policy in such context is to ensure that the favorable results obtained over the last years are preserved.

19. The Copom evaluates that the probability that initially localized pressures impose risks to the inflationary trajectory remains limited. The moderation of domestic demand pressures over the market of factors, at least in the short run, should contribute to contain the risk of pass-through of possible upward pressures over consumer prices stemming from wholesale prices. The Committee understands that the materialization of such pass-through, as well as the generalization of pressures, initially localized over the consumer prices, still depends critically on economic agents' inflation expectations. Incidentally, inflation expectations for 2010 and 2011 remain in line with the targets path and continue to be closely monitored. Additionally, it is worth noticing that the domestic demand behavior tends to exert less pressure over non-tradable items, such as services, over the upcoming quarters. Nonetheless, the Committee reaffirms that it will conduct its actions in order to ensure that the gains on inflation control obtained in recent years become permanent.

20. The Copom emphasizes, once more, that there are important time lags between the implementation of monetary policy and its effects on both economic activity and inflation. Therefore, the assessment of alternative options for monetary policy should necessarily focus on the forward-looking inflation scenario and its risks, instead of current inflation figures. Such considerations become even more relevant in periods surrounded by heightened uncertainty. The Committee reaffirms that specific asset price movements are only relevant for monetary policy if they impact the forward-looking inflationary path.

21. Prospects for the evolution of domestic economic activity have continued to improve since the last Copom meeting, although industrial data remain reflecting the relative accommodation of external demand. In light of the international crisis effects over domestic financial conditions, credit contribution for the support of domestic demand diminished, but signs of recovery continue to accumulate, in particular regarding loans to individuals. The severity of the international crisis negatively impacted consumers and businessmen confidence, but also in this case there are consistent signs of recovery. Under such circumstances, the rhythm of economic activity resumption strongly depends on real payroll expansion, on the effects of fiscal stimulus measures and on incremental governmental transfers, which will occur in the upcoming months. It should also benefit from the easing of financial conditions. In short, the most recent data on domestic economic activity seem to reinforce the evaluation mentioned in previous Copom meetings minutes that the contractionist effects of the international financial crisis over the domestic economy dynamism and, consequently, over the context on which the monetary policy operates, could become persistent, but would not be permanent. These considerations become even more relevant considering the fact that the current monetary policy decision will have concentrated impacts in 2010.

22. The Copom understands that the loss of domestic demand dynamism that occurred at the end of 2008 caused an increase in the idleness margin of production factors utilization, resulting in reduction of inflationary pressures. On the other hand, the risks to the consolidation of a benign inflationary scenario derive, on the short term, from price adjustment mechanisms that contribute to lengthen inflationary pressures observed in the past, as evidenced by the behavior of services prices and certain regulated items since the beginning of 2009, as well as from a possible hike in commodities prices. On the medium term, the risk stems from cumulative and lagged effects of the financial conditions easing and from the fiscal stimulus over the evolution of domestic demand, taking into account the dynamics of consumption and investment, in a context of recovery of production factors utilization. The balance of such influences over the inflationary prospective trajectory will be crucial to the assessment of the various alternatives available for the monetary policy stance.

23. International evidence, as well as the Brazilian experience, indicates that high inflation rates lead to the increase of risk premium, for both private and public funding, to the shortening of planning horizons and,

consequently, to lower potential economic growth, besides having regressive effects over income distribution. Therefore, the Copom strategy aims to ensure that inflation remains in a level consistent with the target path in 2009, 2010 and 2011. Such strategy, which should have its results evidenced throughout time, takes into account the time lags in the transmission mechanisms and is the most adequate to deal with the uncertainty inherent to the process of monetary policy formulation and implementation.

24. The Copom evaluates that, in light of the idleness margin of the economy, and the behavior of inflation expectations for relevant horizons, the materialization of a benign inflation scenario, in which the IPCA would continue to evolve according to the target path, has remained favorable. By the way, such evolution of the forward-looking scenario continues to be reflected on the inflation projections considered by the Committee. Under such circumstances, in order to preserve the improvement of the prospective inflationary path, under a macroeconomic scenario with significant uncertainty, the Copom evaluates that monetary policy should maintain a cautious stance, aiming to assure the maintenance of inflation convergence to the targets path.

25. The Committee understands that the accommodation of demand, motivated by the tightening of financial conditions and by deterioration of the agents' confidence, as well as by the global economic activity contraction, could have been overcome, although significant idleness margin of production factors still persists, which should not be rapidly eliminated in a basic scenario of gradual recovery of economic activity. The Copom also highlights that there are uncertainties around such basic scenario, which should be clarified over the upcoming months, with both positive and negative biases over the pace of economic activity recovery. Anyhow, under such scenario of gradual recovery, which has been corroborated by current available data, inflationary pressures should remain restrained. On the other hand, the Committee notices that the significant monetary policy easing, implemented between January and July, will have cumulative effects over the economy, which will be evidenced with a time lag.

26. The Committee understands that decisions regarding the evolution of the basic interest rate have to take into account the magnitude of the total adjustment carried out between January and July, whose impacts on several economic indicators will be evident over time, in a context of gradual recovery of production factors utilization. The Copom also understands that a more cautious stance will contribute to mitigate the risk of abrupt reversals of monetary policy in the future and, therefore, to the consistent recovery of the economy over the upcoming quarters. The Copom also evaluates that the preservation of benign inflationary prospects will require the behavior of the financial system and the economy under a new level of interest rates to be closely monitored over time.

27. Under such context, in light of the inflation prospects for the targets path, the Copom has unanimously decided to maintain the Selic rate at 8.75% p.a. without bias. Taking into account, on the one hand, the monetary policy easing implemented since January and, on the other hand, the idleness margin of production factors, among other factors, the Committee evaluates that such level of basic interest rate is consistent with a benign inflationary scenario, contributing to assure the maintenance of inflation in line with the targets path over the relevant horizon for the non-inflationary recovery of economic activity.

28. Under the inflation targeting regime, the Copom guides the decisions according to projected inflation, the analysis of several alternative scenarios for the evolution of the main variables that determine the forward-looking dynamics for prices, and the balance of risks associated to the projections. After a short period of contraction, domestic demand started to show signs of recovery, due to the stimulus factors effects, such as income growth. Additionally, it bears noticing that, evidencing the credibility achieved by the Copom on the implementation of the regime, inflation expectations for 2010 and 2011 remain in line with the targets path. It is also noteworthy that global economic deceleration has generated downward pressures over wholesale industrial prices. On its turn, important monetary and fiscal stimuli were introduced into the economy over the last quarters and should contribute to the activity recovery and, consequently, to the reduction of the idleness margin of production factors. Those stimuli effects should be closely monitored over time and are important in the context where future monetary policy decisions, which should ensure the materialization of the convergence to targets path over relevant horizons, will be taken.

29. At the end of the meeting it was announced that the Committee will reconvene on December 8th, 2009 for technical presentations and on the following day, to discuss the monetary policy decision, as established in Communiqué 17,327 of August 27th, 2008.

SUMMARY OF DATA ANALYZED BY THE COPOM

Inflation

30. IPCA inflation reached 0.24% in September, up from 0.15% in August, totaling a 3.21% increase in the nine first months of 2009 and a 4.34% increase in the last twelve months. The housing group increased 0.62% in September relative to 0.47% in August, and was the key driver over the September IPCA result (0.08 p.p.).

31. Market prices increased from 0.15% in August to 0.18% in September, with increases of 0.01% on tradable items and 0.35% on non-tradable items, while regulated prices increased 0.37% in September, up from 0.16% in August. On a twelve-month trailing basis, market prices and regulated prices increased 4.45% and 4.08%, respectively, in comparison to 4.57% and 3.88% in the previous month. The diffusion index reached 54.17%, 1.57 p.p. above the August figure.

32. All the core IPCA measures increased in September, but decelerated on a twelve-month trailing basis. The core excluding household food items and regulated prices increased from 0.29% in August to 0.35% in September; the smoothed trimmed means core reached 0.39%, up from 0.25% over the previous month; the non-smoothed trimmed means core reached 0.31%, up from 0.18%, in the same periods. In the last twelve months through September, the smoothed and non-smoothed trimmed core measures reached 4.3% and 3.54%, respectively, in comparison to 4.37% and 3.65%, respectively, in August, while the core by exclusion recorded 5.04% and 5.32%, according to the same comparison basis.

33. The IGP-DI accelerated to 0.25% in September, up from 0.09% in August, reflecting primarily the IPA increase, which reached 0.29% in September, up from 0.07% in August. The IPC-Br decreased, from 0.20% in August to 0.18% in September, and the INCC increased 0.15% in September, after a 0.05% fall in the previous month. The IGP-DI decreased 1.35% in 2009 and 0.65% on a twelve-month basis. The IPA acceleration was motivated exclusively by the 0.63% increase in the prices of industrial products in September, up from 0.1% in August, while crop and livestock product prices contracted 0.76% in September, after increasing by 0.01% in the previous month. The IPA reached -3.69% and -3.4%, respectively in the year through September and on a twelve-month basis, respectively; in the same periods, the IPC-Br reached 3.41% and 5.02%, and the INCC reached 2.78% and 4.27%, respectively.

34. The IGP-10 reached 0.10% in October, down from 0.25% in September, reflecting decelerations in both IPA (0.09% in October, down from 0.46% in September) and the IPC-Br (0.11% in October, down from 0.24% in September). The INCC increased 0.20%, after a 0.11% fall in the previous month. The IGP-10 accumulated falls of 1.68% in 2009 and 0.94% on a twelve month trailing basis. The IPA deceleration reflected the 1.18% fall on crop and livestock products, down from a 0.52% increase in September, totaling –2.86% in 2009 and –3.88% in the last twelve months, while the prices of wholesale industrial products increased 0.50% in October, relative to 0.43% in the previous month, totaling declines of 4.73% in 2009 and 3.60% in the last twelve months. The IPA reached -4.20% in 2009 and –3.64% in the last twelve months; according to the same comparison basis, the IPC-Br reached 3.79% and 4.95%, and the INCC reached 2.92% and 4.03%, respectively.

Economic Activity

35. According to data seasonally adjusted by the IBGE’s monthly survey (PMC), expanded retail sales increased 3.3% in August, month-on-month, after a 5.7% fall in July and increases of 6.8% and 4.6% in June and May, respectively. As a consequence, the average change of the quarter ended in August reached 5.9%, relative to the quarter ended in May. Year-over-year, expanded retail sales increased by 5.5%, while growth reached a 3.7% increase in the eight first months of the year. The month-on-month result revealed that sales increased in five out of ten segments surveyed, with highlights for the increase in “vehicles and motorcycles, parts and pieces” (2.5%); and “hyper-, supermarkets, food products, beverages and tobacco” (1.4%). Among the negative drivers, it bears highlighting “office and information technology and communications material and equipment”, which retreated by 4.9%.

36. Year-over-year, it bears highlighting the expansions in pharmaceutical and perfumery items (14.9%), and books, newspapers, magazines and stationary (11.1%), in August. Among the negative drivers, it bears noticing the 6.9% decrease in construction inputs. In the year through August, seven out of the ten segments surveyed increased, and it bears emphasizing office material and equipment (13.3%); pharmaceutical, medical, orthopedic, perfumery and cosmetic items (12.5%); books, newspapers, magazines and stationary (9.2%); as well as other personal and domestic items (9%). As negative drivers, according to the same comparison basis, construction inputs presented the sharpest decrease, with a 9.8% fall.

37. São Paulo Trade Association (ACSP) data, related to the city of São Paulo, indicated a 5.8% increase in database consultations for credit sales (SCPC) and a 1.9% fall in consultations to the Usecheque system on a month-on-month, seasonally adjusted basis. In 2009, those indicators decreased 12.8% and 0.6%, respectively, in comparison to the same period of the previous year, and decreased 9.2% and 0.1%, respectively, on a twelve-month basis.

38. Automobile sales by dealers, which take into account automobiles, light commercial vehicles, trucks and buses, increased 24.1% in September, month-on-month, seasonally adjusted by the BCB, according to Fenabrave (Brazilian Federation of Vehicles Distribution). Such increase reflected expectations regarding the progressive suspension of the IPI (tax on industrialized products) reduction, as of October. Total sales increased 14.9% year-over-year, with highlights for automobiles, which increased 19.8%, while buses and trucks decreased 21.2% and 16.3%, respectively. In the year through September, vehicles sales increased 4.2% year-over-year, as a result of the expansion on automobiles (5.8%) and light commercial vehicles (4%), as well as of the decline of trucks sales (20.3%) and buses sales (16.6%).

39. Capital goods imports increased 2.7% in September, month-on-month, according to the Funcex quantum indices, seasonally adjusted by the BCB. The September indicator decreased 19% year-over-year, reaching a 14.1% decline in the year through September, year-over-year. Capital goods exports increased 3.1% in September, month-on-month, and decreased 39.0% and 40.1% year-over-year and in the year through September, respectively.

40. Capital goods production increased 0.4% in August, month-on-month seasonally adjusted, but showed decreases of 22.3% year-over-year and of 23.0% in the year through August, according to IBGE. The monthly result showed greater expansion in the production of capital goods directed to the electric energy sector (11.4%), while the worst performance was registered for agricultural capital goods, which dropped 9.1%. The production of inputs for civil construction increased 0.8%, according to the same comparison basis, and declined 10% in the first eight months of the year.

41. The disbursements of BNDES increased 53.2% in the last twelve months through August, year-over-year. Industry was the most benefited sector, with expansion of 108.7%, according to the same comparison basis.

42. General industrial physical production increased 1.2% in August, month-on-month seasonally adjusted, according to IBGE's Monthly Industrial Survey – Physical Production (PIM-PF). In the year and also on a twelve-month basis, the sector contracted by 12.1% and 8.9%, respectively. Among the four use categories, it bears highlighting the performance of durable consumer goods production, with a 3.1% increase, while capital goods production presented the mildest increase (0.4%). Mining production increased 0.9% in the period, after a 0.4% decrease in July, reaching falls of 12.8% in 2009 and of 9.4% in the last twelve months.

43. CNI indicators signaled a more moderate recovery of industrial activity than that signaled by the IBGE data, having only employment, among the surveyed variables, increased in August, month-on-month (0.6%), the first increase since September 2008. Manufacturing industry real revenues remained stable in the period, while hours worked in production declined 0.5%. In August, the Nuci increased 0.2 p.p. relative to July, corresponding to 80.1%, according to the seasonally adjusted series. Among the nineteen activities in the manufacturing industry, five showed increase in Nuci in August 2009, year-over-year.

44. Vehicles production reached 275.3 thousand units in September, according to Anfavea, which was 8.4% below that recorded in September 2008. According to seasonally adjusted data, vehicles production decreased 1.5% month-on-month. In the year through September the production of vehicles and agricultural machinery declined 11.6% and 27.8%, respectively, while in the last twelve months through September the same indicators declined 14.7% and 16.4%, respectively, year-over-year. Domestic sales of vehicles increased 13.9% in September and declined 1% in the first nine months of 2009, year-over-year, while exports decreased by 30.6% and 42.8%, respectively.

Surveys and Expectations

45. According to the Fecomercio-SP survey, the Consumer Confidence Index (ICC) increased 5.6% in October, month-on-month. This result reflected mainly an expansion of 7% in the Consumer Expectations Index (IEC), while the Current Economic Conditions Index (Icea) increased by 3.3%. Year-over-year, the ICC increased 11%.

46. According to the Consumer Expectations Survey carried out by the FGV nationwide, the ICC remained stable in September, month-on-month seasonally adjusted. In September, the Current Situation Index (ISA) increased 0.4%, and the Expectations Index (IE) decreased 0.3%. The ICC decreased 1.1% year-over-year, reflecting the fall of 3.2% in the ISA and the expansion of 0.2% in the IE.

47. In relation to the expectations for the manufacturing industry, the FGV Manufacturing Industry Survey showed, in September, an increase of 3.8 p.p. in the Industry Confidence Index (ICI) seasonally adjusted. Year-over-year, the indicator decreased 5.5 p.p. in the observed series. Among components, according to the month-on-month seasonally adjusted series, there were increases of 2.1 p.p. for the Current Situation Index (ISA) and 5.4% for the IE, and retreats of 9.3 p.p. and 1.8 p.p., respectively, year-over-year, according to the observed series.

Labor Market

48. According to the General Record of Employment and Unemployment (Caged) of the Ministry of Labor and Employment (MTE), 252.6 thousand formal jobs were created in September (the second best result of the series for the month). In the year through September and on a twelve-month basis, respectively, 932.7 thousand and 298.3 thousand new jobs were created. The main economic activities expanded in September, with highlights for the manufacturing industry, with 123.3 thousand hires, reaching the best result of the series for the month. Seasonally adjusted data showed a 0.3% increase in employment in September, month-on-month, with highlights, once again, for the increase in the construction sector (0.7%). According to the average of the year, the level of employment increased 2%, reflecting increases of 5.9% in the construction sector, 4% in the services sector and 3.9% in the retail sector, whereas the manufacturing industry declined by 2.5%.

49. According to the IBGE employment survey (PME), carried out in the six main metropolitan regions of the country, the unemployment rate reached 8.1% in August 2009, showing relative stability month-on-month (8% in the previous month) and a 0.5 p.p. increase year-over-year. The stability in the unemployment rate is a result of increases of 112 thousand jobs (0.5%) and 148 thousand people (0.6%) in the economically active population (PEA). The same survey pointed out that average real earnings of employed workers grew for the second consecutive month (0.9%, relative to July), growing by 3.8% in the year through August. Real payroll increased 1.5% month-on-month and 4.6% in the year through August.

Credit and Delinquency Rates

50. Outstanding credit in the financial system reached R$1,327 billion in August, equivalent to 45.2% of GDP, with increase of 1.5% in the month and 19.5% on a twelve-month trailing basis. Non-earmarked credit operations increased 1.1% in the month and 13.9% in the last twelve months. Among the non-earmarked operations, which represent a share of 68.5% in the total of the financial system, credit operations to individuals increased 1.4% in the month and 18.4% in the last twelve months, while non-earmarked credit operations to corporate increased 0.7% and 9.8%, according to the same comparison bases. Earmarked credit operations increased 2.5% in the month and 33.9% on a twelve-month trailing basis.

51. The average interest rate on non-earmarked credit operations, used as reference for interest rates, declined for the ninth consecutive month in August, reaching 35.4%, the lowest level since December 2007. The average annual rate on credit for individuals decreased 13.8 p.p. relative to December, reaching 44.1%. The average rate on corporate credit decreased by 4.3 p.p. relative to December, reaching 26.4%.

52. The average tenure on non-earmarked credit operations, used as reference for interest rates, decreased in August, reaching 367 days. The average tenure of corporate credit operations reached 264 days, while the average tenure for credit operations to individuals totaled 498 days.

53. Delinquency rates in the financial system (non-earmarked loans used as reference for interest rates, in arrears for more than ninety days) remained stable in 5.9% after increasing for eight consecutive months. Delinquency rates for credit operations with corporate increased 0.1 p.p., reaching 3.9%, and with individuals, declined 0.1 p.p., reaching 8.4%.

54. Net delinquency rate for retail credit, measured by the ACSP, reached 6.5% in September, compared to 6.7% in August, 7.4% in July and 5.9% in the same month of 2008, representing a record low in 2009.

External Environment

55. The stabilization of financial markets and the inventories adjustments, whose trajectory has been suiting final demand, were crucial factors for the recovery of global economic activity. Preliminary data suggest that economic recovery, already observed in Japan and in some emerging economies, has spread to other countries, with highlights to the USA and the Euro Area. Recent projections from the International Monetary Fund (IMF) indicate a –1.1% change in global economic activity in 2009, up from the –1.4% July estimate. For 2010, the IMF projects global growth at 3.1 %, up from 2.5% in the previous estimate.

56. Signs of industrial production recovery in the developed countries strengthened, although they have slowed in the last months in Japan. Data through August show that the USA, the Euro Area and Japan recorded two, four and six consecutive months of positive monthly changes, respectively. Since May, China has recorded increasing growth rates on an annual basis.

57. The twelve-month consumer price indices through September recorded deflation in the USA (-1.3%) and in the Euro Area (-0.3%). With data up through August, Japan recorded a -2.2% deflation. The persistence of low rates of installed capacity occupation, added up to the stability of inflationary expectations in the medium-term, should continue to contribute inflation does not become a problem in the short- and medium-term in G3.

58. The financial market continues to recover, with key indicators pointing to increasing preference for risk. The stocks exchanges of the major mature and emerging economies kept an upward trend, and among these last ones, except for China, are close to the record highs observed in the pre-crisis period.

59. Considering this scenario, the central banks of the main mature economies, except for Australia (RBA), which resumed the increase in its basic interest rate, maintained the accommodative stance of their monetary policy, having the United Kingdom extended its programs of financial system aid. Among emerging economies, the central bank of Russia deepened the cuts in its basic interest rate, reducing it by 25 basis points in two opportunities during September, setting the rate at 10% p.a..

Foreign Trade and International Reserves

60. The Brazilian trade surplus reached US$1.3 billion in September, totaling US$21.3 billion in the first nine months of the year, increasing by 9.2%, year-over-year, on a daily average basis. In the month, exports reached US$13.9 billion, and imports, US$12.5 billions, decreasing by 27.4% and 23.9%, respectively, year-over-year, on a daily average basis. Total external trade reached US$26.4 billion in September, decreasing by 25.8%, year-over-

year, on a daily average basis. In the year through September, total external trade reached US$202.3 billion, 27.5% below that registered last year, according to the same comparison basis.

61. Based on the liquidity concept, international reserves, which encompass the repurchase lines and borrowing operations in foreign currencies, reached US$224.2 billion in September, recording a US$5.2 billion increase in the month. Under the cash concept, international reserves totaled US$221.6 billion, recording a US$5.9 billion increase, according to the same comparison basis. It bears highlighting, in the month, a US$0.4 billion new receivable of the Special Drawing Rights (SDR), a special allocation of the International Monetary Fund (IMF), totaling US$4 billion in the August-September period.

Money Market and Open Market Operations

62. Since the September Copom meeting, the yield curve slope increased for all maturities, especially for the intermediary. Domestically, the release of improved data for the labor market, the increase of GDP growth projections, concerns with a possible reduction in the fiscal restriction and the expectation of a tax creation over foreign capital inflows contributed to this movement. In the international scenario, the improvement of some US economic indicators and the decision of the Central Bank of Australia to increase its basic interest rate, being the first monetary authority to take this decision since the beginning of the crisis, have also influenced the upward movement of the yield curve. Between August 31 and October 19, one- three- and six-month rates increased by 0.04 bps, 0.08 bps and 0.22 bps, respectively, whereas one- two- and three-year rates increased by 0.84 bps, 0.88 bps and 0.67 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 from 4.91% on August 31 to 5.48% on October 19.

63. In its open market operations, the BCB carried out, between September 1 and October 19, long fixed rate repo operations, borrowing R$23.2 billion for a six-month period. The average daily balance of the five-, six- and seven-month operations reached R$68.7 billion, of which R$63.1 billion were six-month operations. In the same period, the BCB conducted borrowing operations with tenures of 33 working days on September 3; of 31 working days on September 8; of 27 working days on September 14; of 22 working days on September 21; of 17 working days on September 28 and 12 working days on October 5. These operations drained from the market R$251.9 billion, R$16.3 billion, R$11.2 billion, R$17.8 billion, R$1.1 billion and R$5.4 billion, respectively. The average daily balance of these short-run borrowing operations reached R$290.3 billion. The BCB also borrowed money through 34 overnight repo operations and conducted daily, at the end of day, one- and two-working-day tenure liquidity management operations. Operations with tenors less than thirty days, including daily liquidity management operations, averaged R$88.7 billion, on a daily basis, borrowing. The average daily balance of these short-run borrowing operations reached R$447.7 billion between September 1 and October 19, up from R$412.5 billion between July 21 and August 31. The main determinant factors of the liquidity increase in the period were the FX market interventions and the net redemption of securities by the National Treasury, during this period.

64. Between September 1 and October 19, the National Treasury issuance regarding the traditional auctions raised a total of R$25.8 billion. The issuance of fixed-rate securities reached R$22.0 billion, being R$15.2 billion via issuance of LTNs maturing in 2010 and 2011, and R$6.8 billion via NTN-Fs maturing in 2013 and 2017. Issuance of LFTs totaled R$1.7 billion, for securities maturing in 2013 and 2015. Issuance of inflation-linked NTN-Bs reached R$2.1 billion, for securities maturing in 2011, 2014, 2020, 2024, 2035 and 2045.