Brazil

Economic and Financial Fundamentals:

A General View and Perspectives

Aldo Luiz Mendes

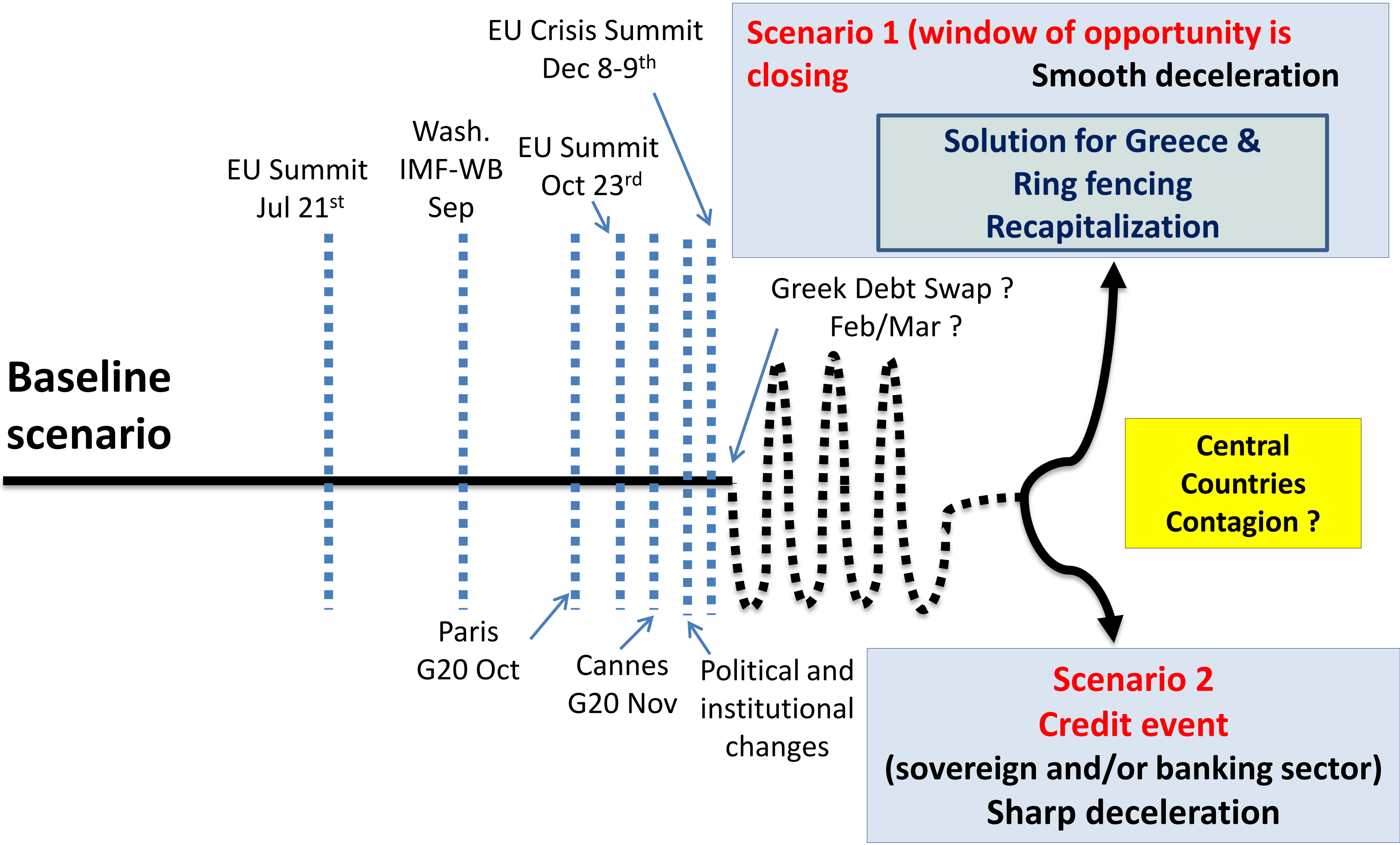
February 2012

Contents

1. International Scenario

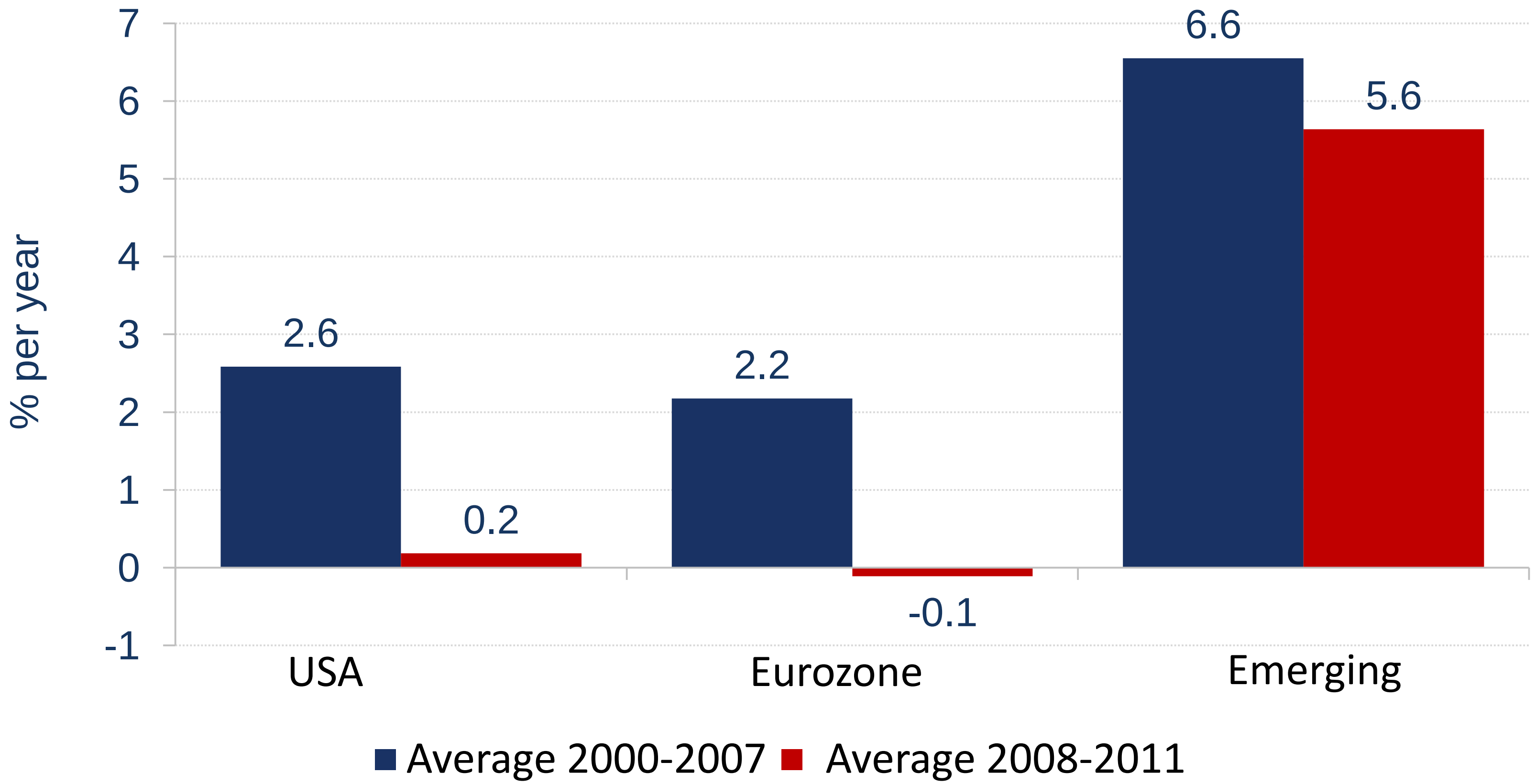
The 2nd Phase of the 2008 Crisis
Deterioration in Global Economic Conditions
Increasing Downside Risks

European Dilemma and (alternative) Scenarios



Slower Growth in Advanced Economies (AE)

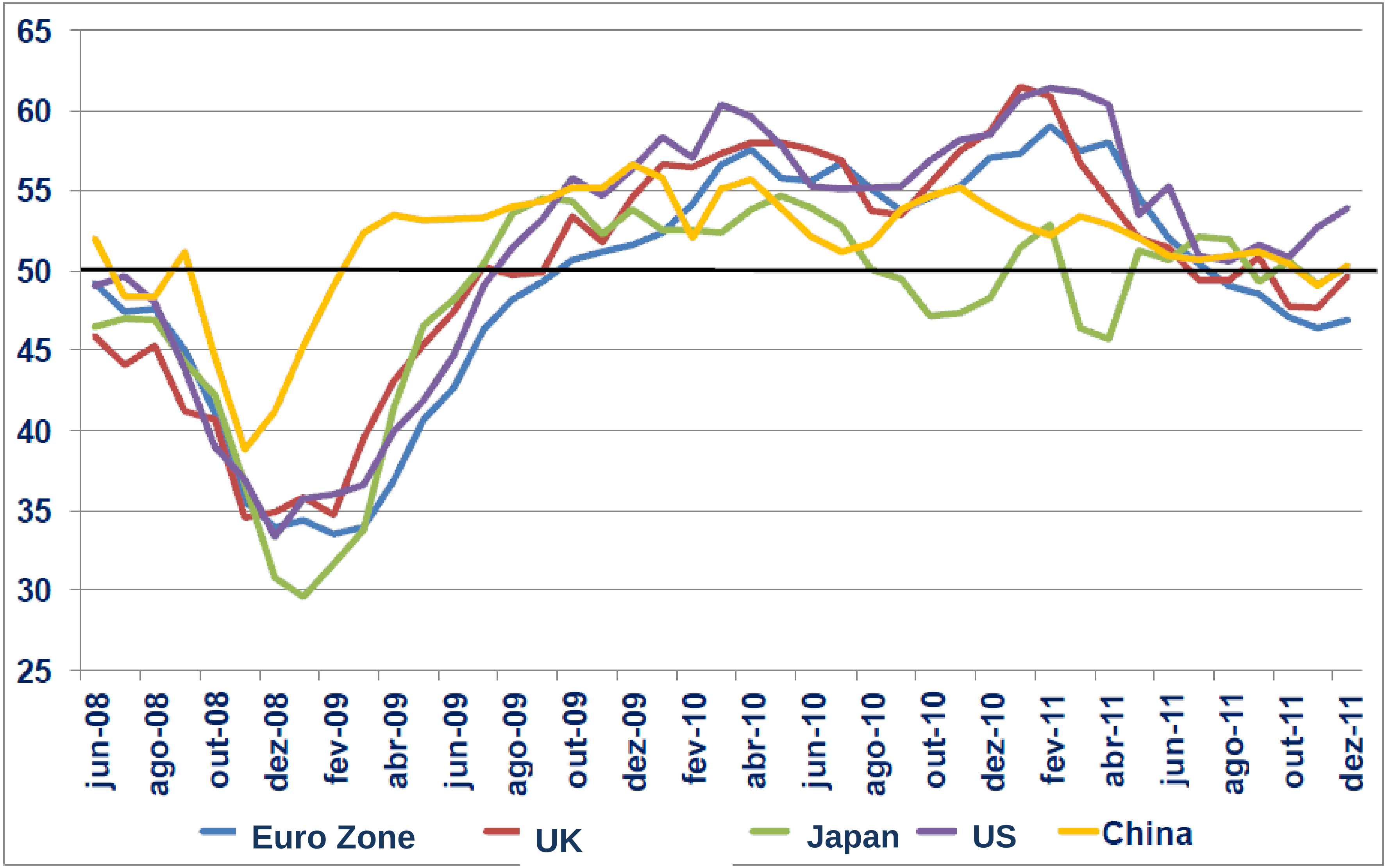
3 years after the most acute financial crisis the AE have not yet retaken a sustainable growth path



Source: FMI

BANCO CENTRAL DO BRASIL

Dev. Economies + China – Economic Activity (PMI)



PMI – Purchase Managers Index
Source: Bloomberg

World Economies – Growth Outlook

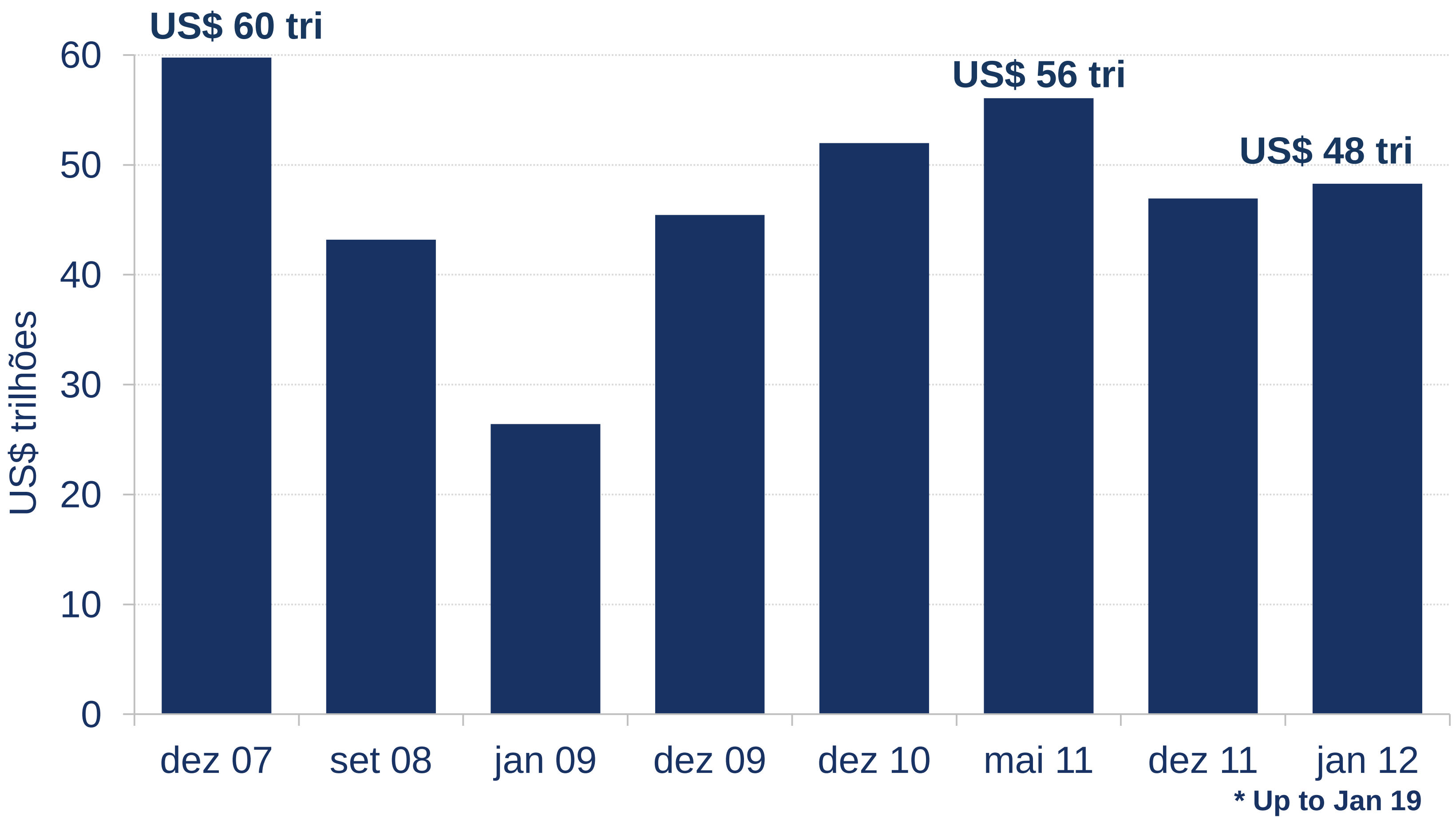
A difficult international backdrop exerted a negative effect on economic agents expectations, lending a downbeat sentiment to growth forecasts.

	WEO report (Jun 2011) 2012	WEO report (Sep 2011) 2012	WEO report (Dec 2011) 2012	Var Dec/Sep 11
GDP	**4.5**	**4.0**	**3.3**	**-0.70**
Developed Economies	**2.6**	**1.9**	**1.2**	**-0.70**
US	2.7	1.8	1,8	0.0
Eurozone	1.7	1.1	-0.5	-0.60
Emerging Economies	**6.4**	**6.1**	**5.4**	**-0.70**
Brazil	**3.6**	**3.6**	**3.0**	-0.60
China	9.5	9.0	8.2	-0.80

Source: WEO/IMF – September 2011

Wealth Loss – Companies' Market Value

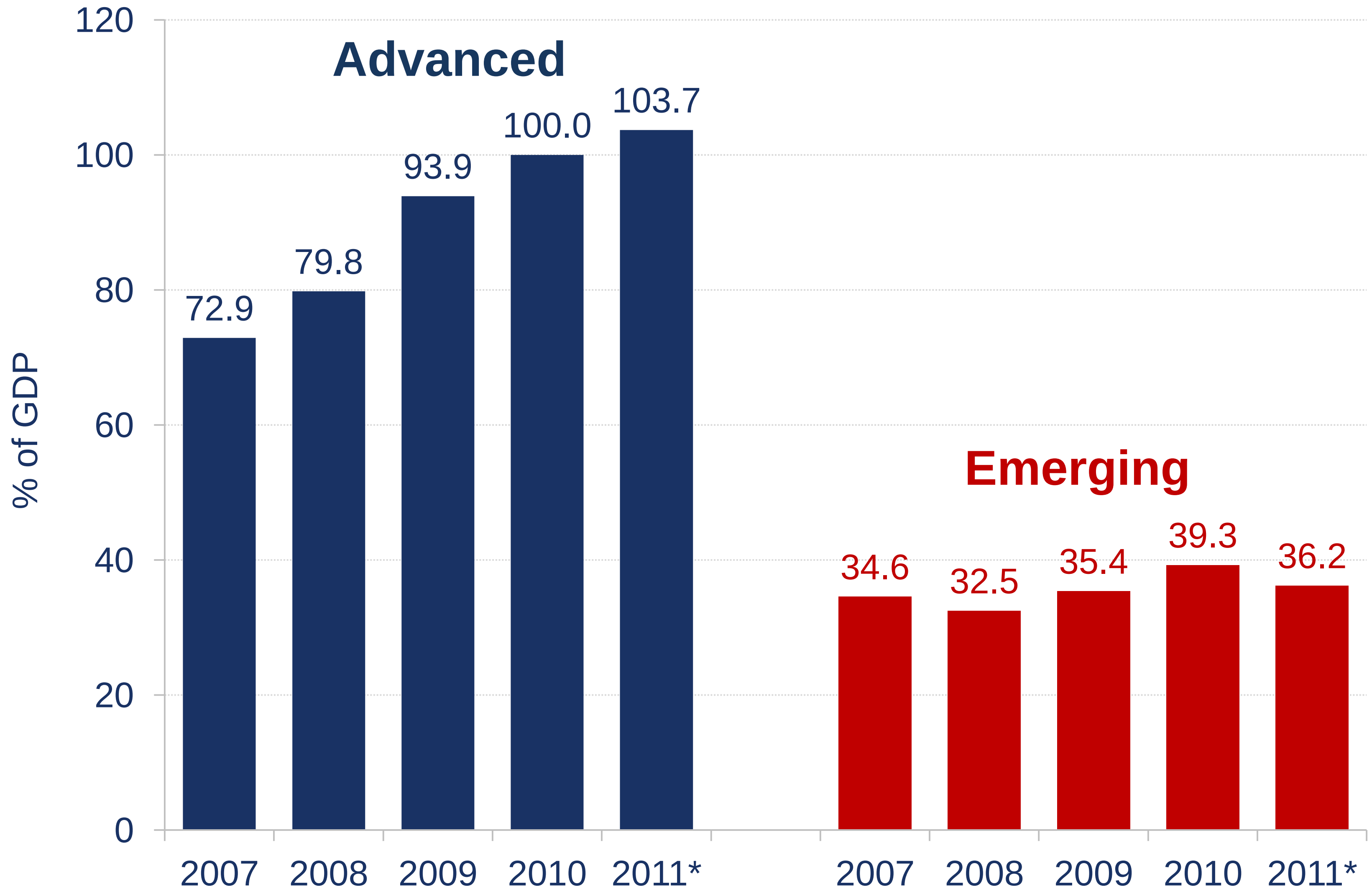
The decrease in market value of firms listed in main global stock exchanges have achieved US$ 8 trillion in the last eight months, aggravating deflationary forces in the global economy.



Source: Bloomberg

BANCO CENTRAL DO BRASIL

Growing Debt in AE – Gross Public Debt

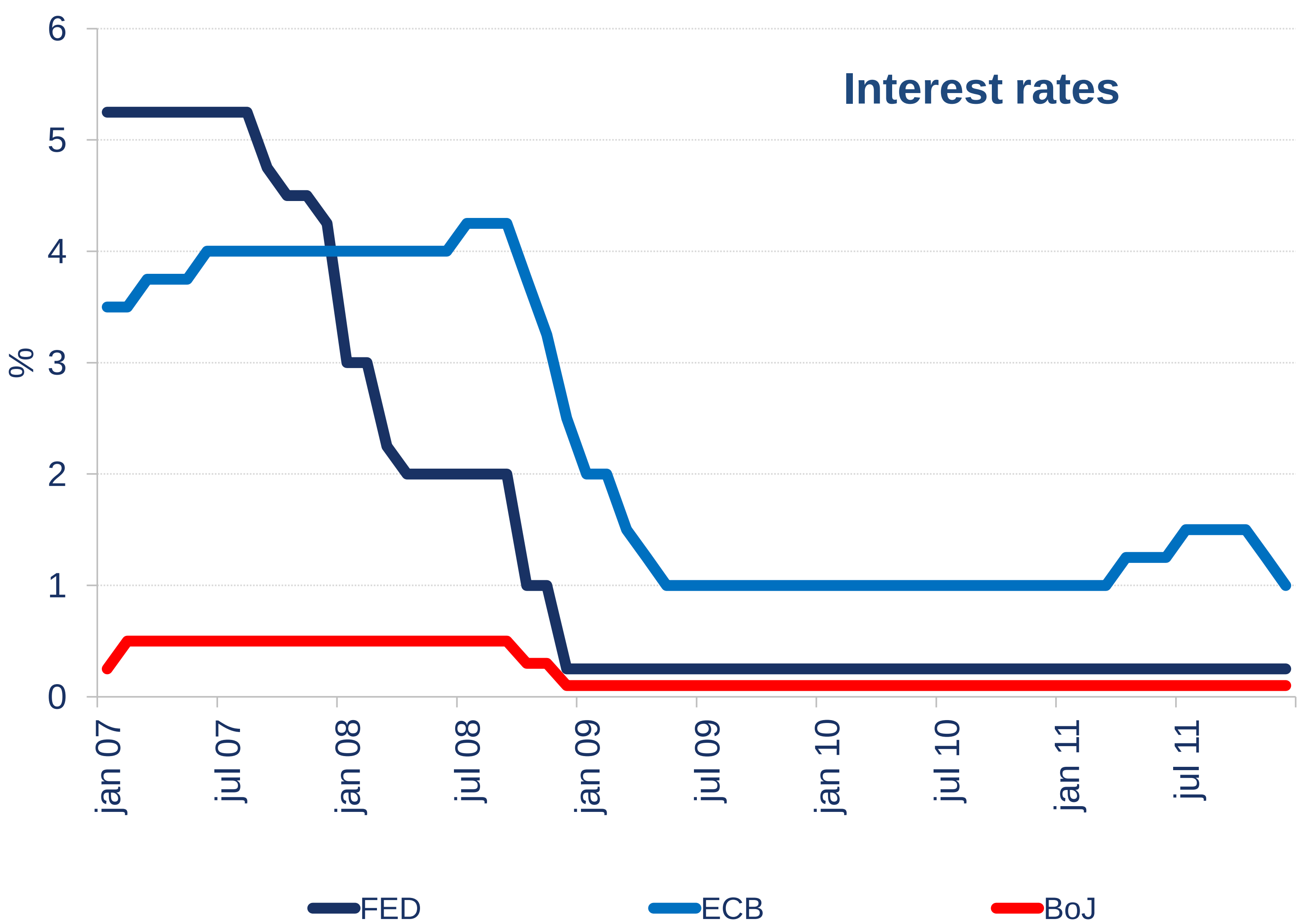


* IMF forecast

Source: IMF

BANCO CENTRAL DO BRASIL

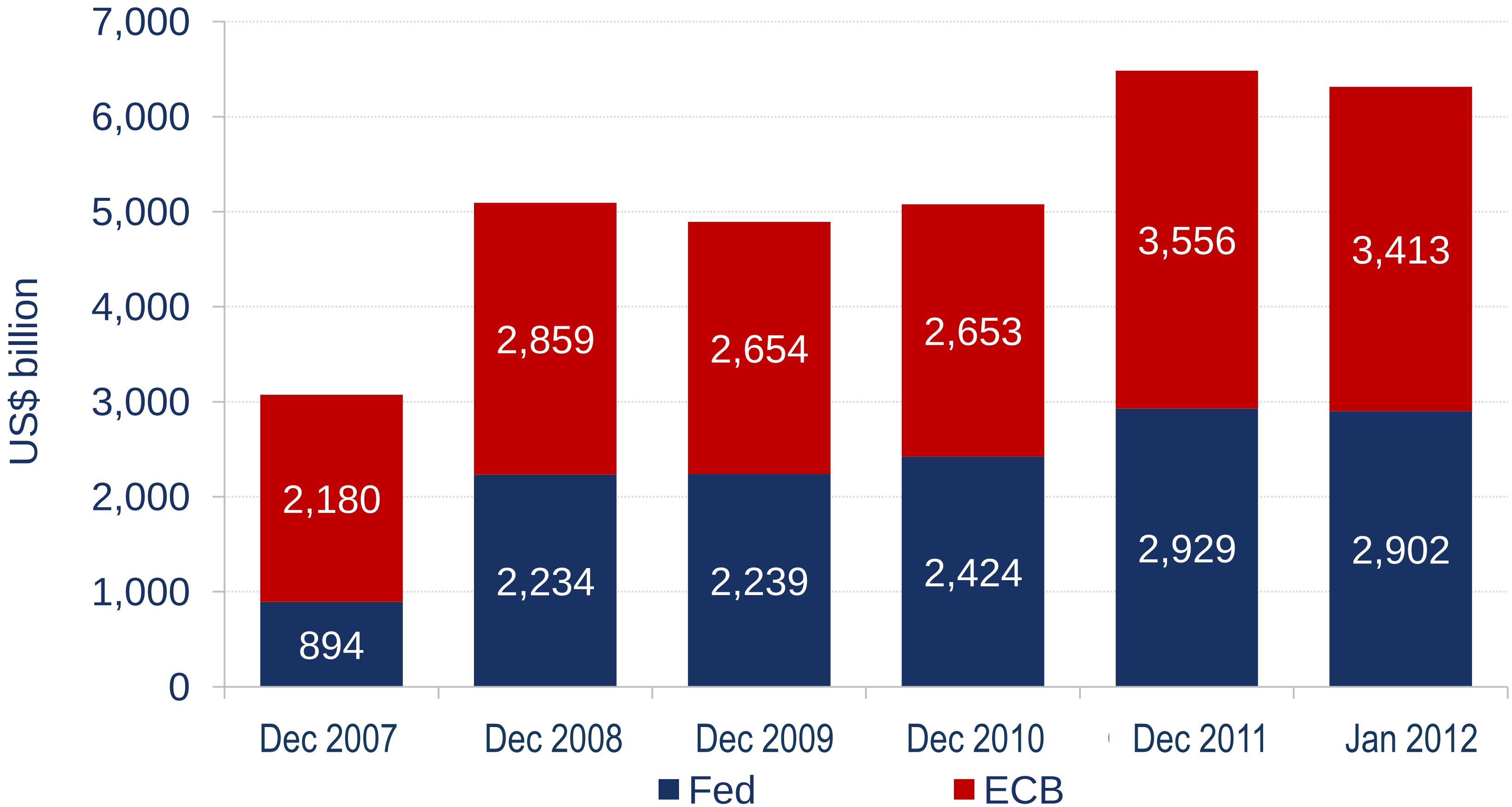
Conventional Monetary Policy Faces Limits



Source: Bloomberg

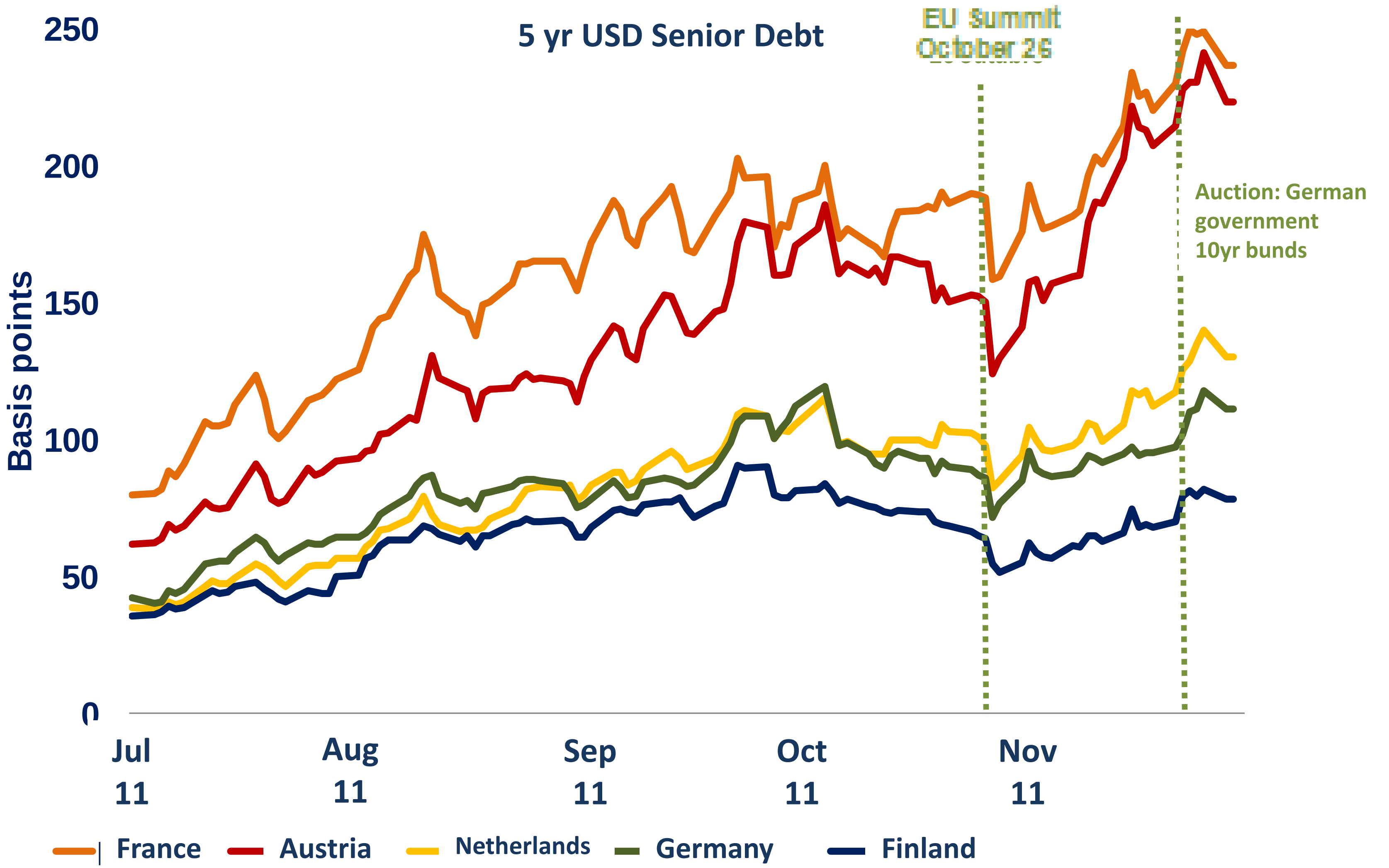
Unconventional Monetary Policy

CBs have improved global liquidity with the acquisition of financial assets, despite the controversy over the effects of QE measures on economic prospects for Europe and the US.



Source: Bloomberg

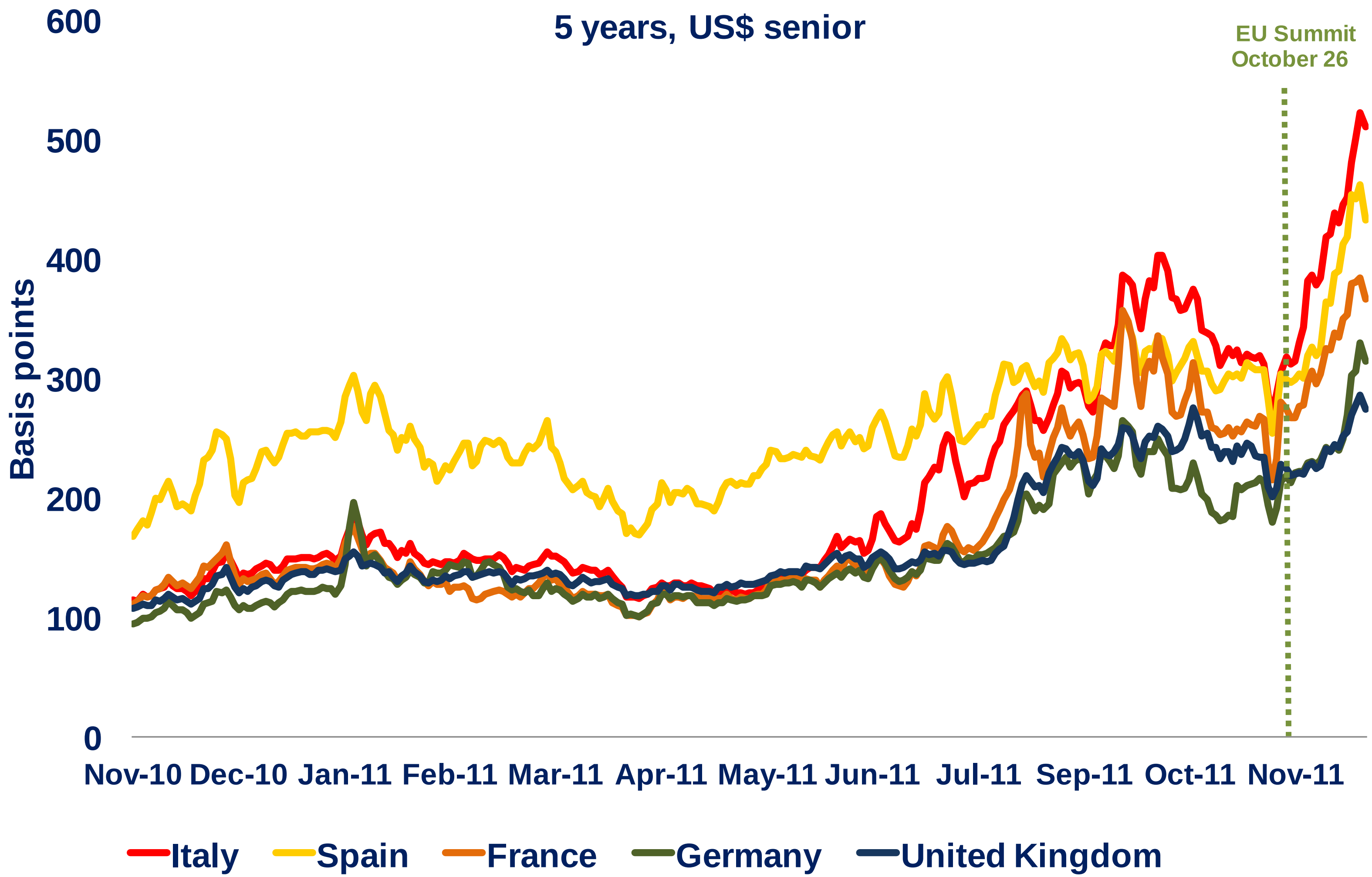
Sovereign CDS - AAA rated countries: Euro Zone & UK



Fonte: Bloomberg

BANCO CENTRAL DO BRASIL

Risk in Euro Zone: Bank CDS (bps)



Private Bank CDS average by country:

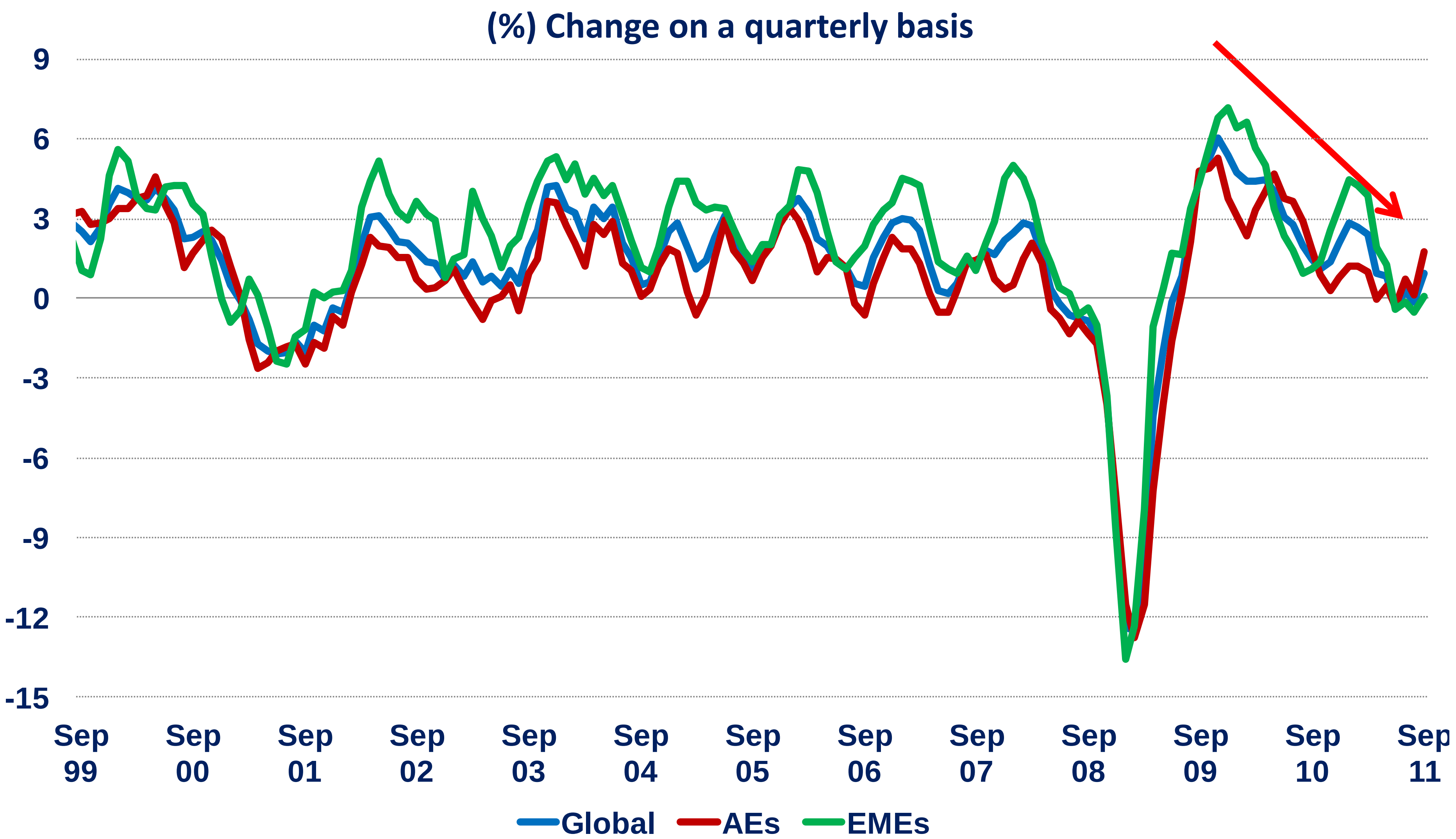
UK: Barclays , HSBC,RBS; **Germany:** Deutsche Bank, Commerzbank; **France:** BNP Paribas, Societé Generale, Credit Agricole; **Italy:**Unicredit, BNL**;** **Spain:** BBVA, Santander**;**

Source: Bloomberg

BANCO CENTRAL DO BRASIL

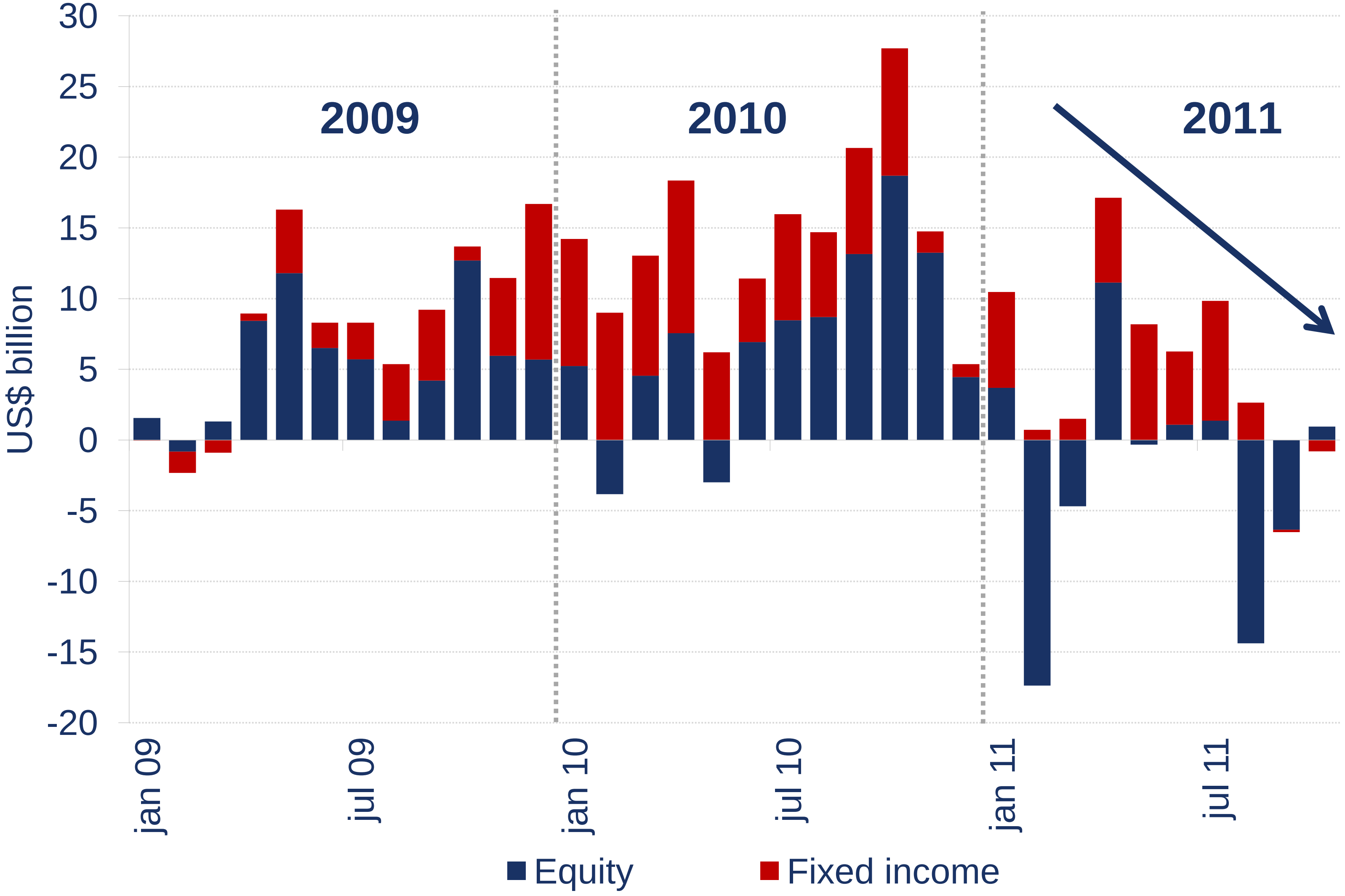
2. Global Scenario Impact on Emerging Economies

World Trade – Overall Volume



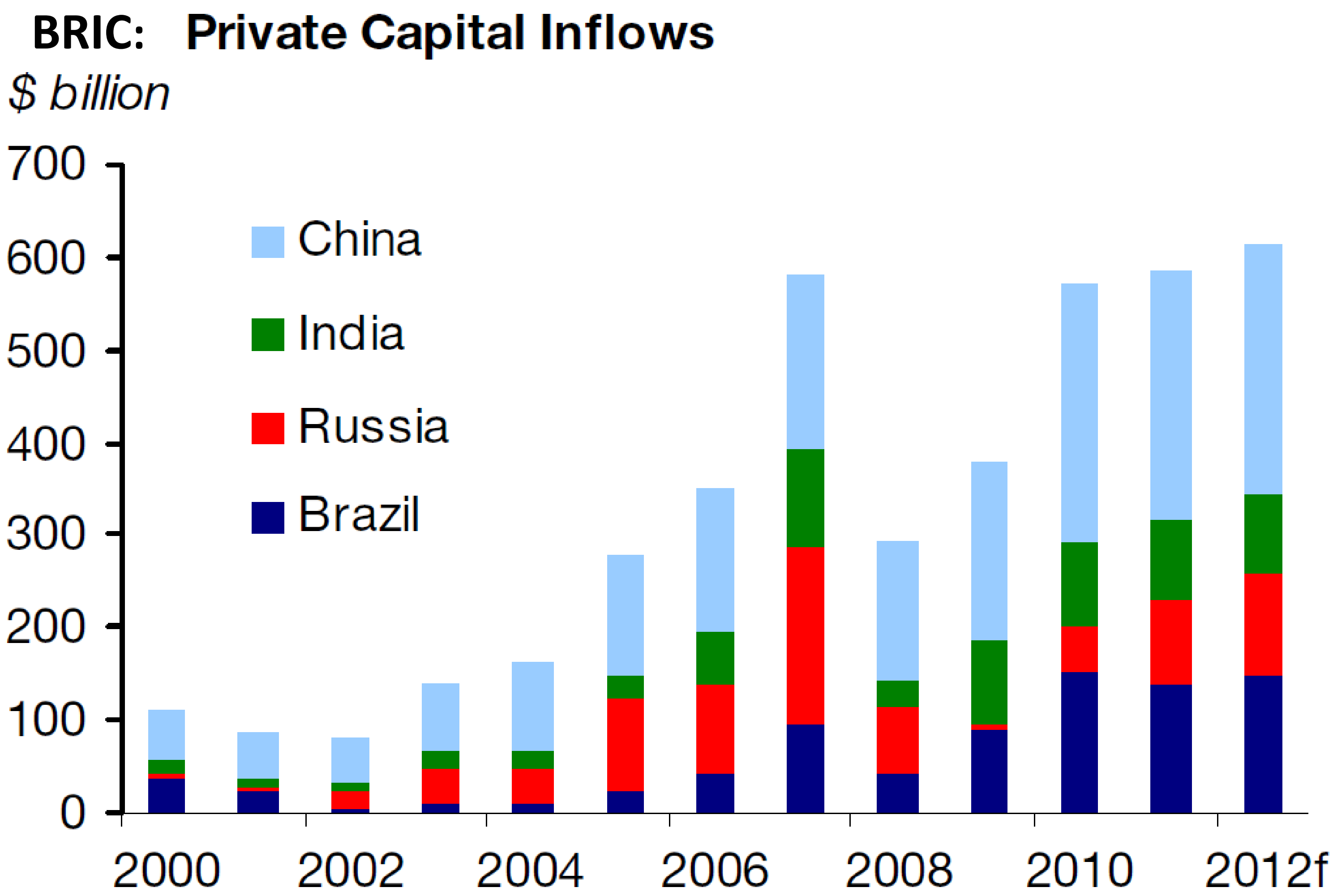
Source: CPB (World Trade Monitor – Nov/2011)

Capital Inflows to Emerging Economies



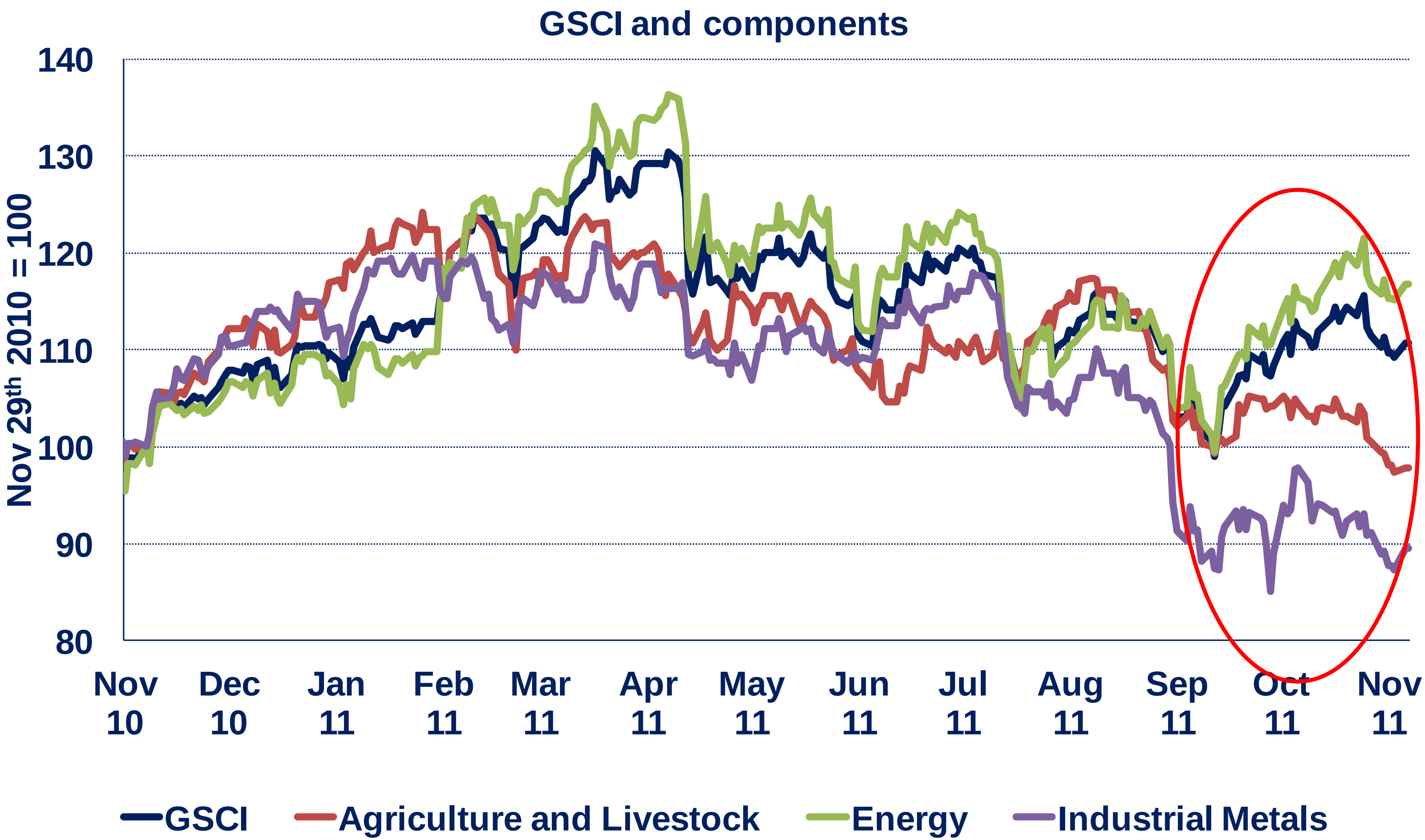
Source: IIF (Capital Markets Monitor – Oct/2011)

BRIC: Total Net Flows (2000-2012f)



Fonte: IIF - CMM outubro 2011

Commodities – Prices



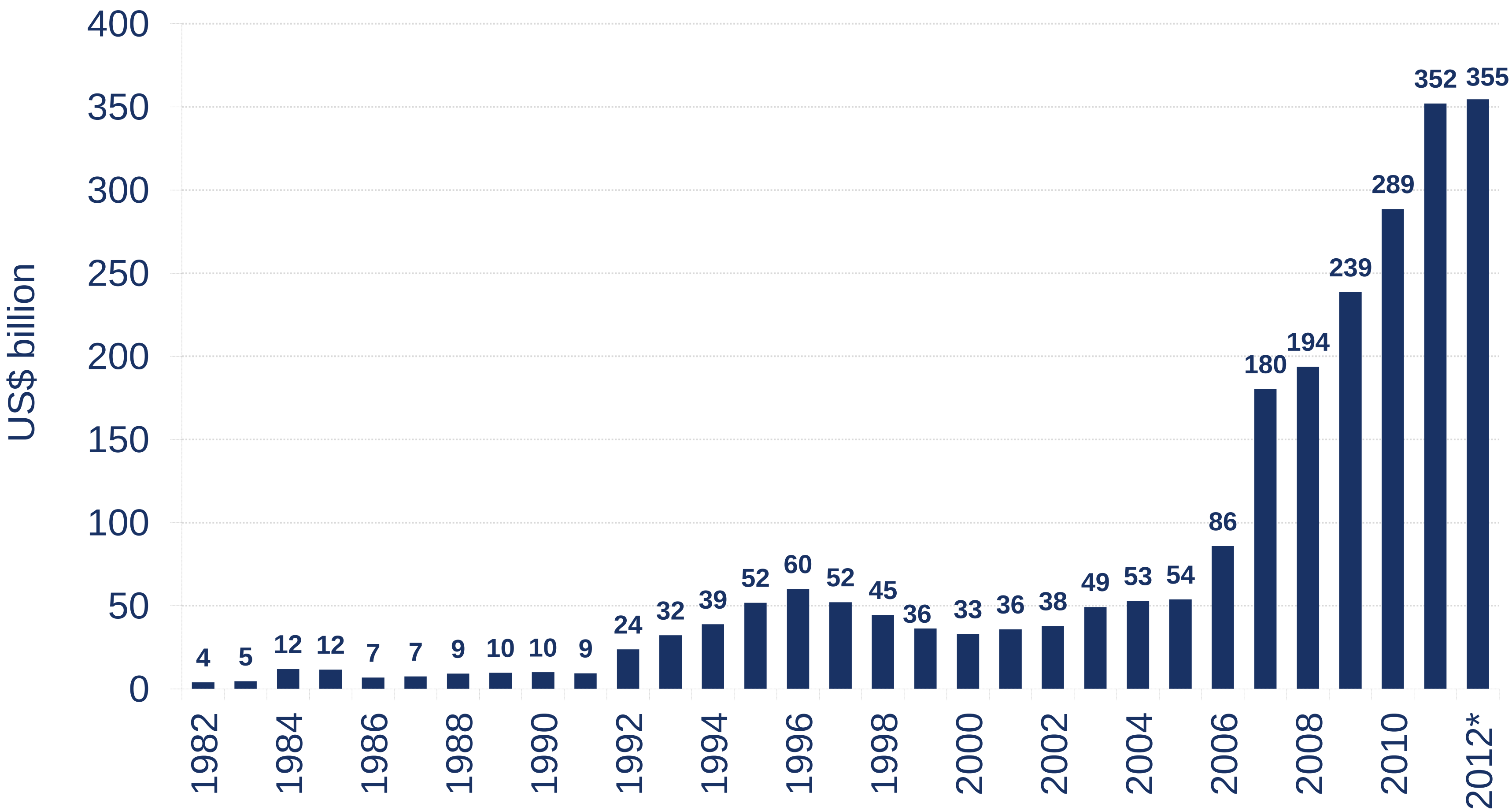
Source: Bloomberg (Nov 29th). Prepared by BCB/Derin.

BANCO CENTRAL DO BRASIL

3. Brazil:

Prepared for Further Deterioration in Global Economic Conditions

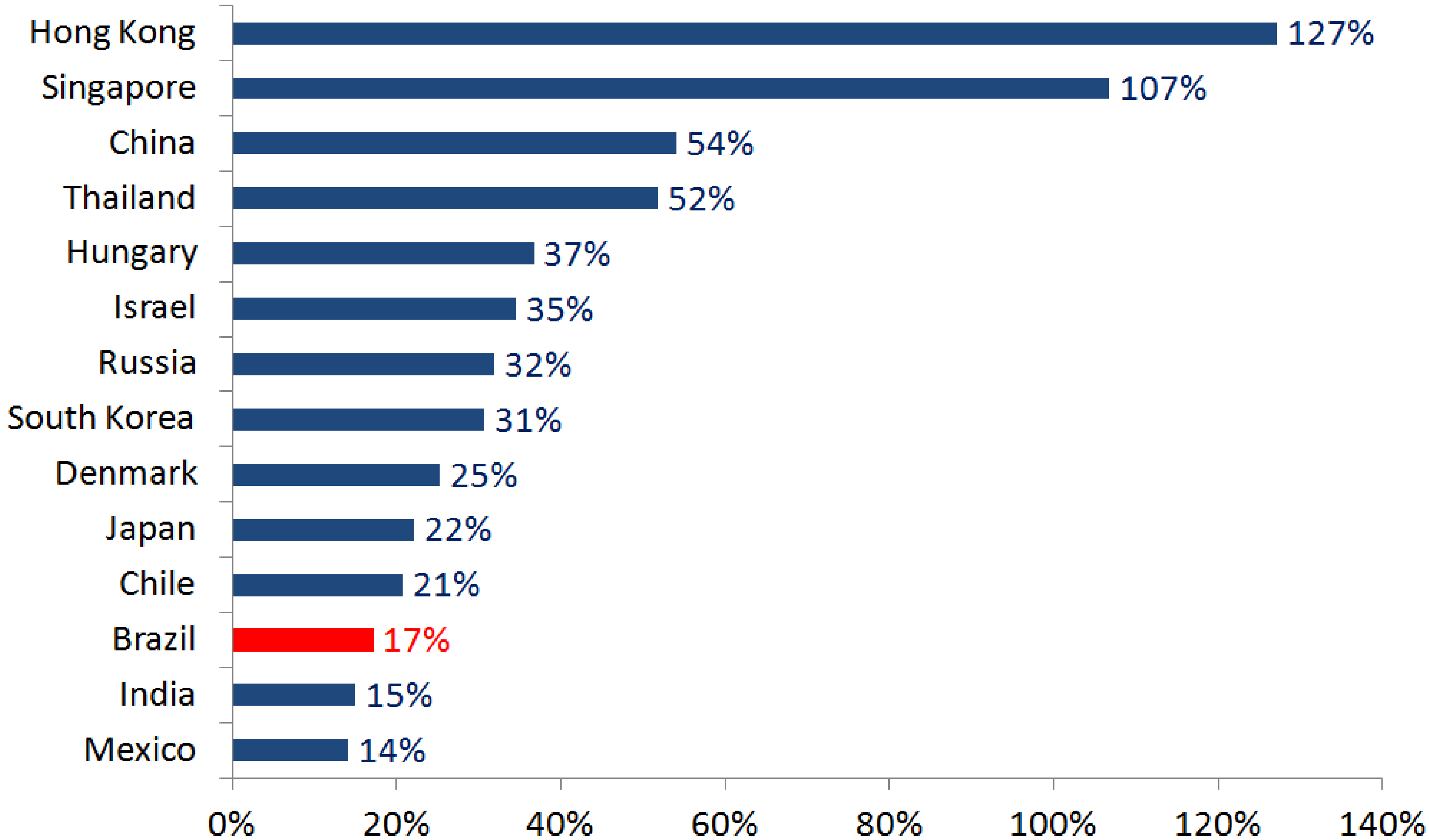
International Reserves



up to Jan 26th

Source: BCB

International Reserves (% of GDP)*

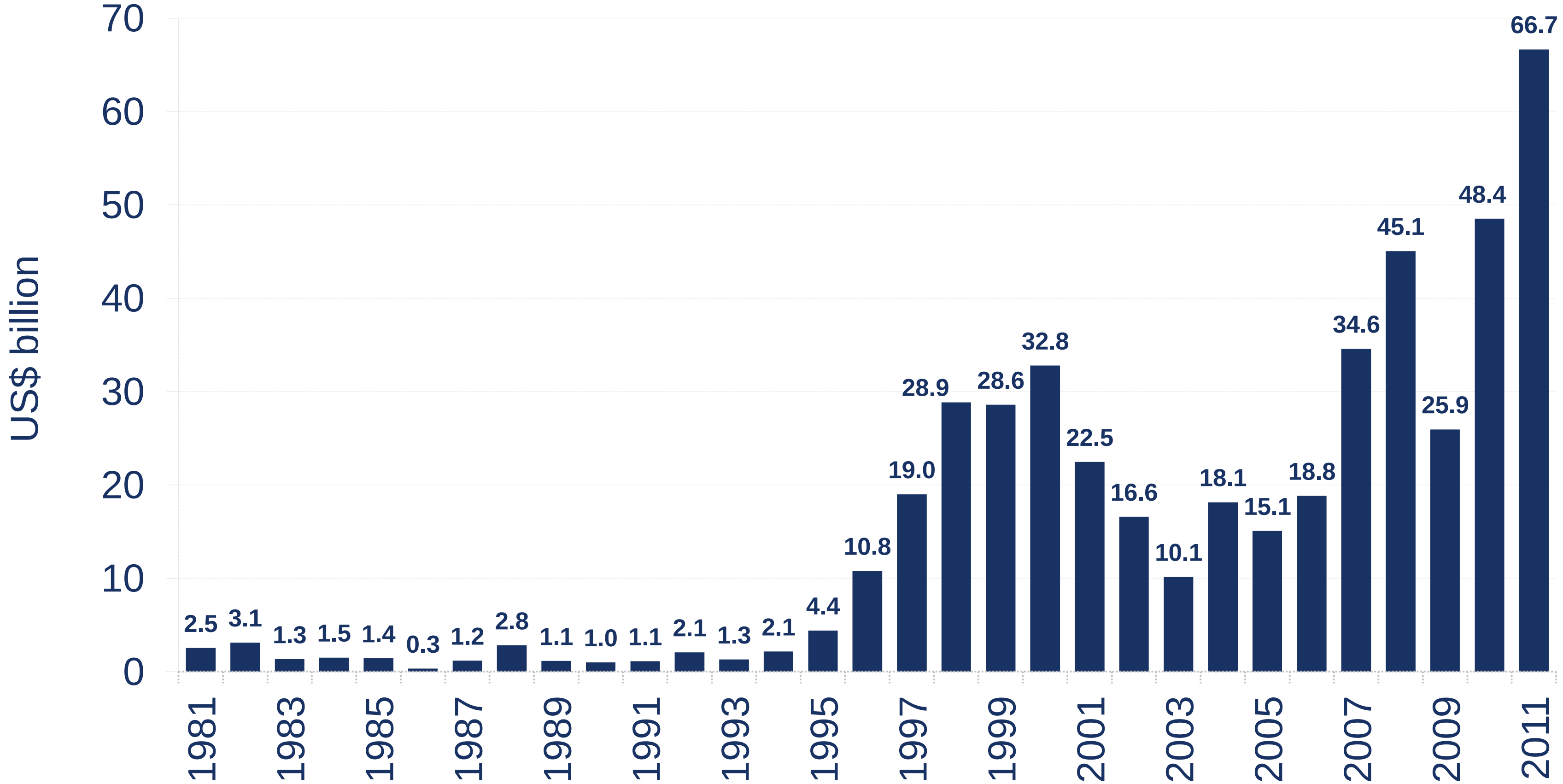


*Dec 11

Sources: IMF / Thomson Datastream

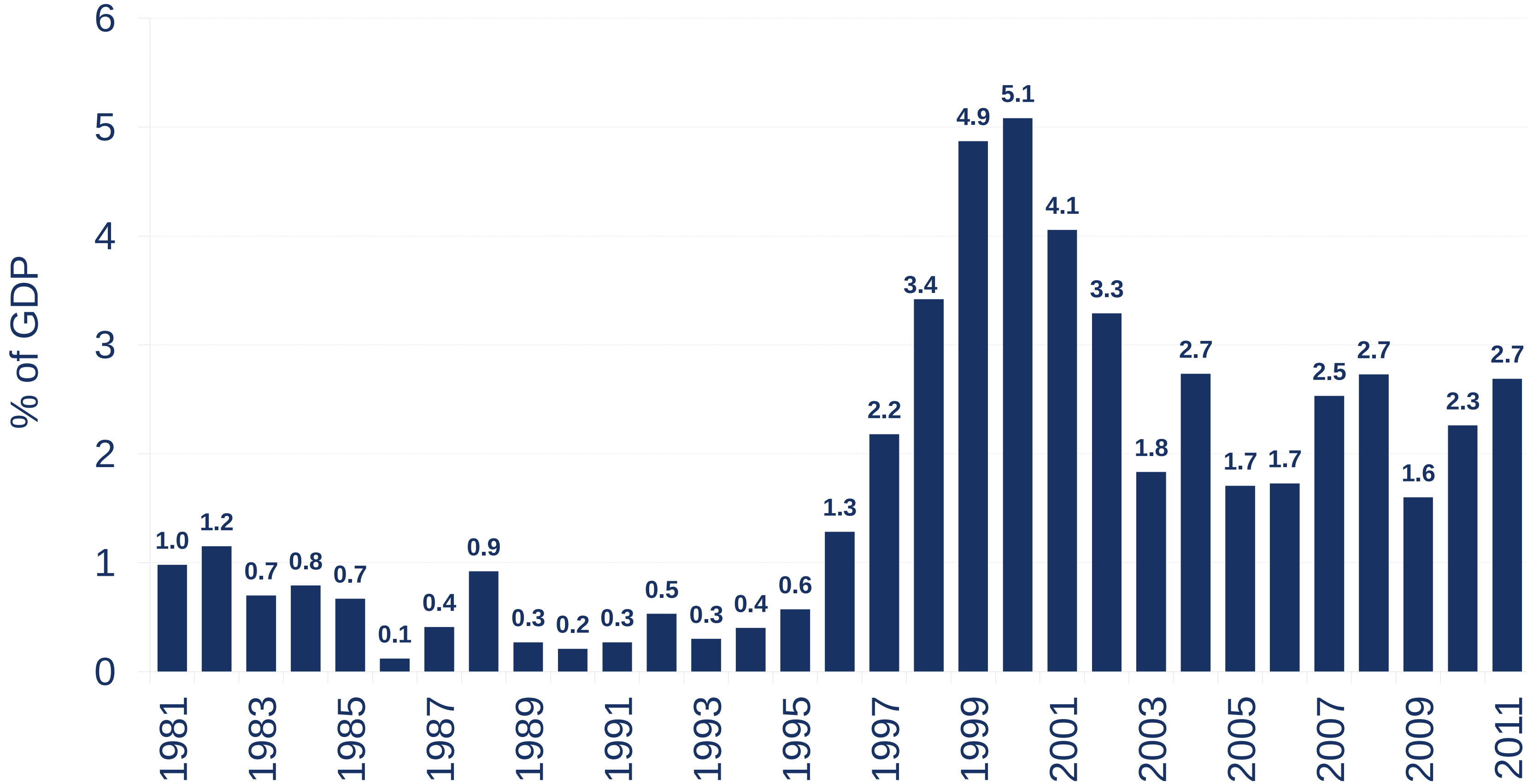
BANCO CENTRAL DO BRASIL

Foreign Direct Investment



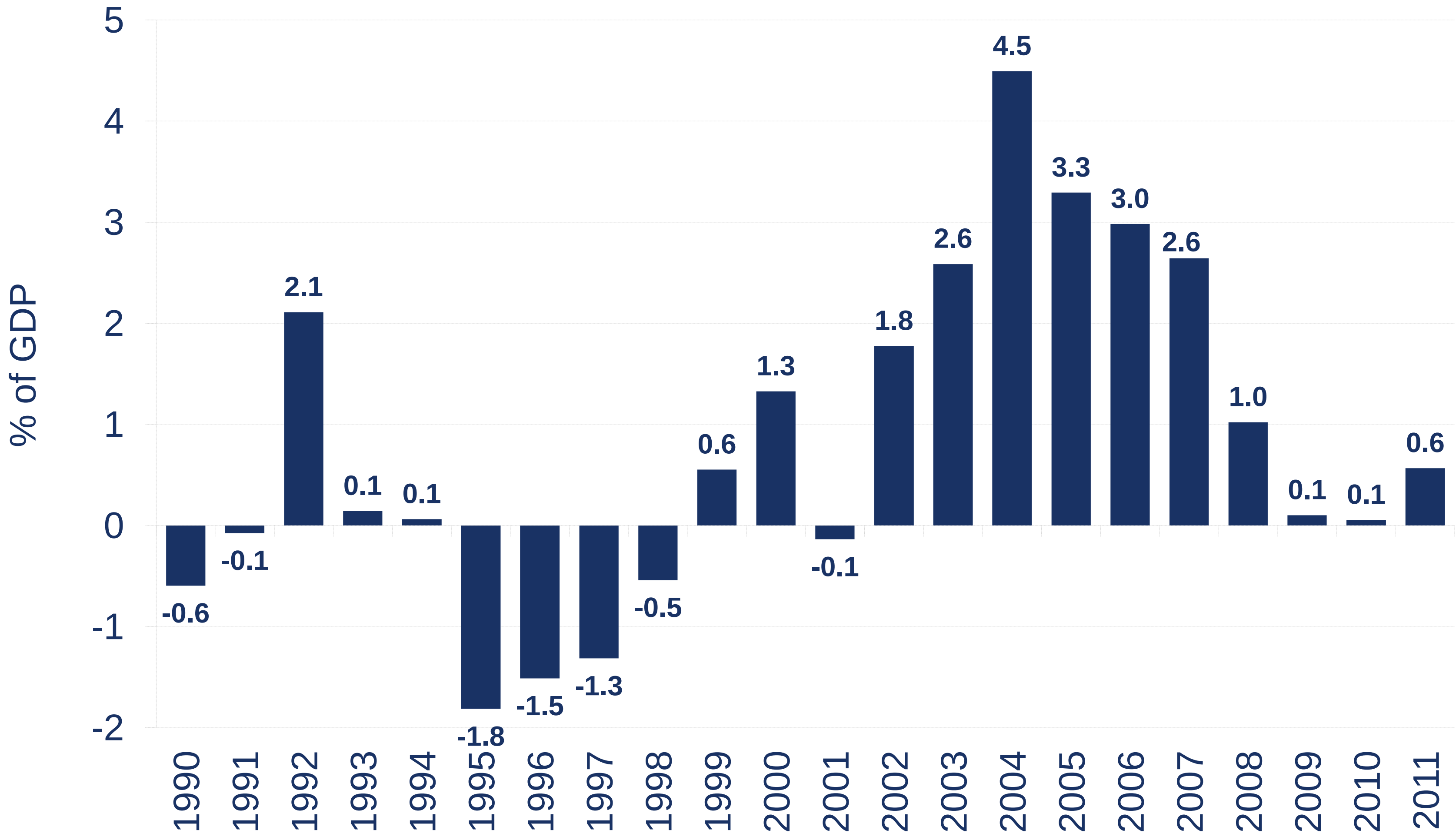
Source: BCB

Foreign Direct Investment / GDP



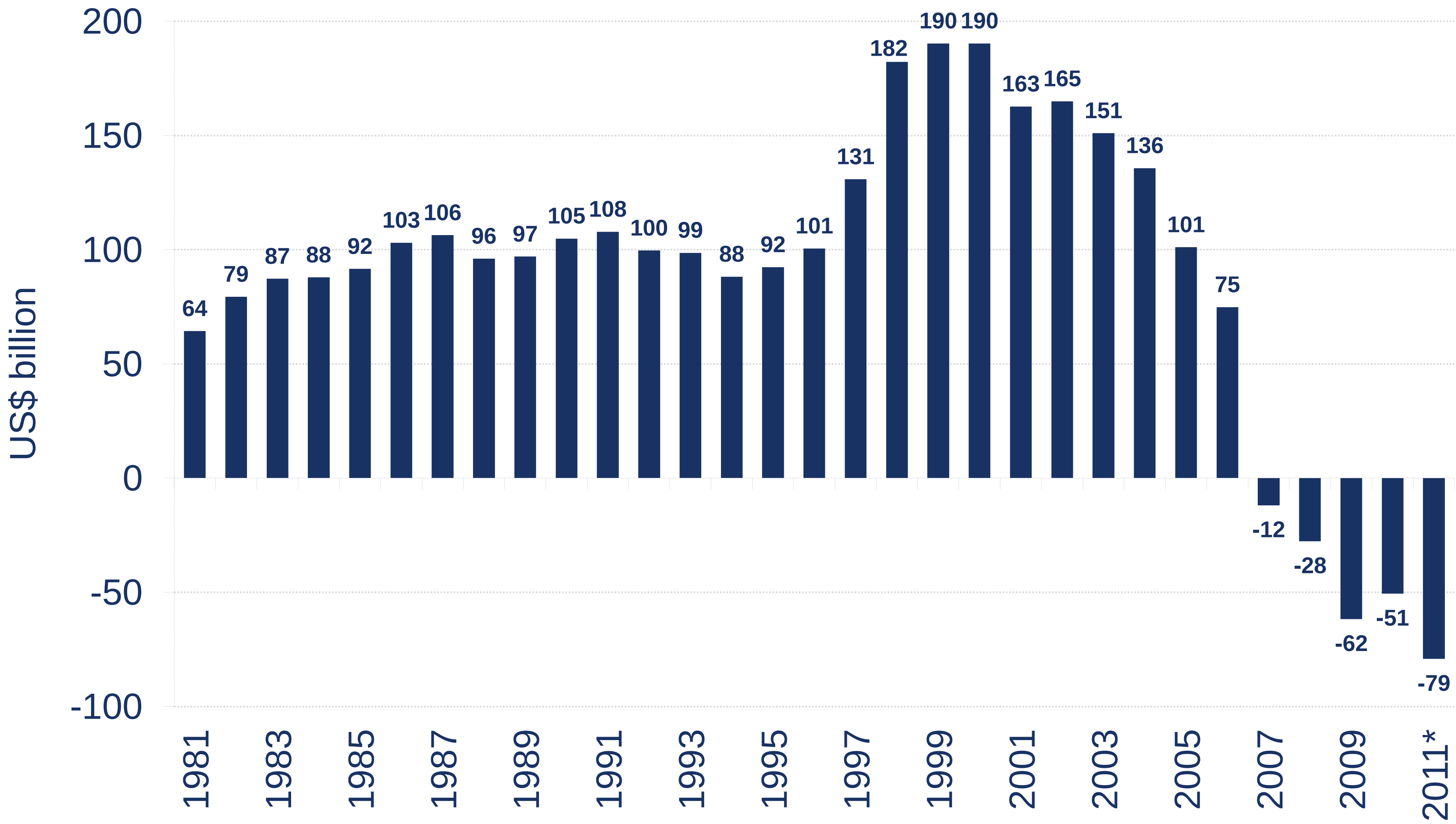
Source: BCB

FDI (-) Current Account Deficit



Source: BCB

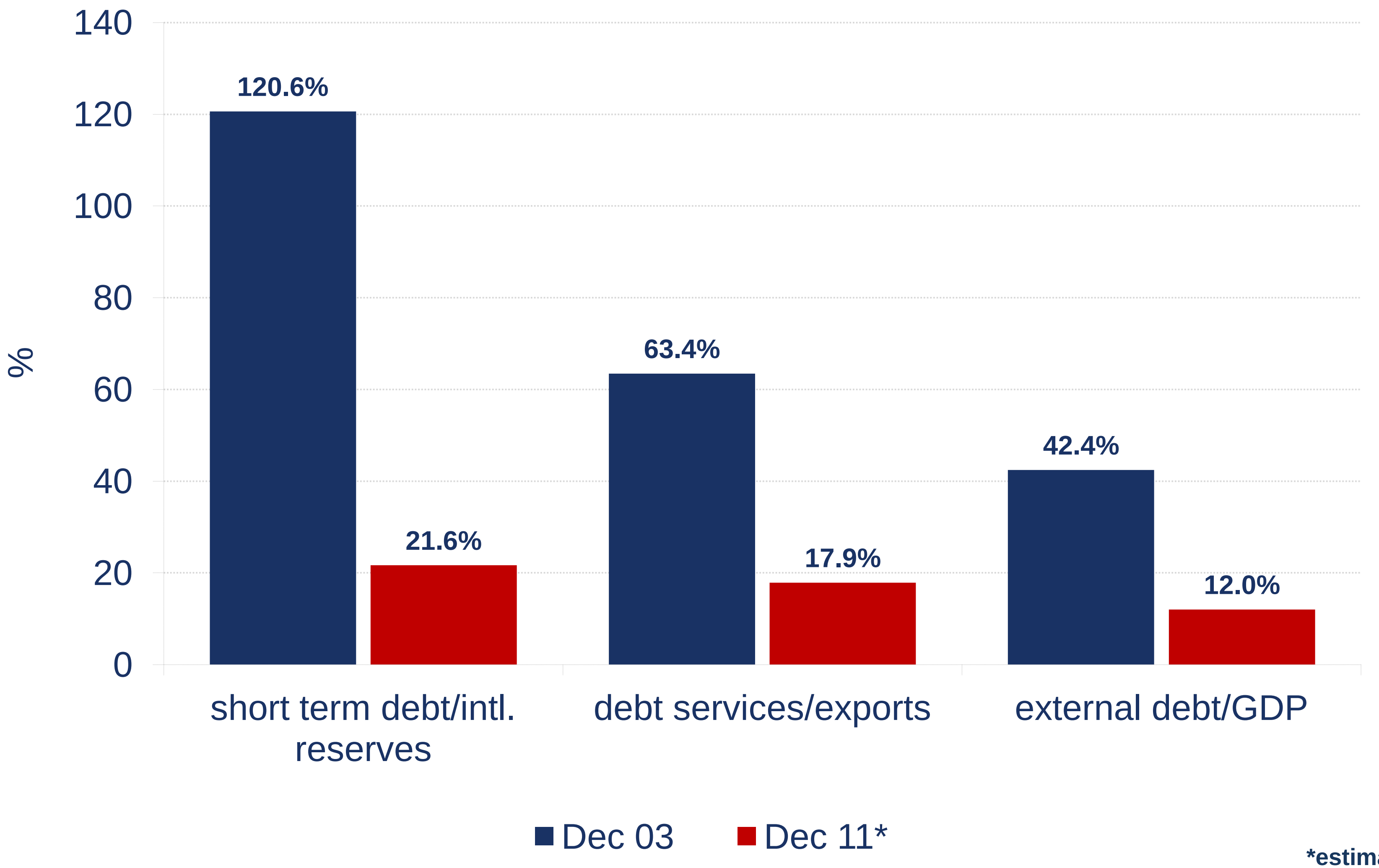
Net External Debt



*estimate Dec 11

Source: BCB

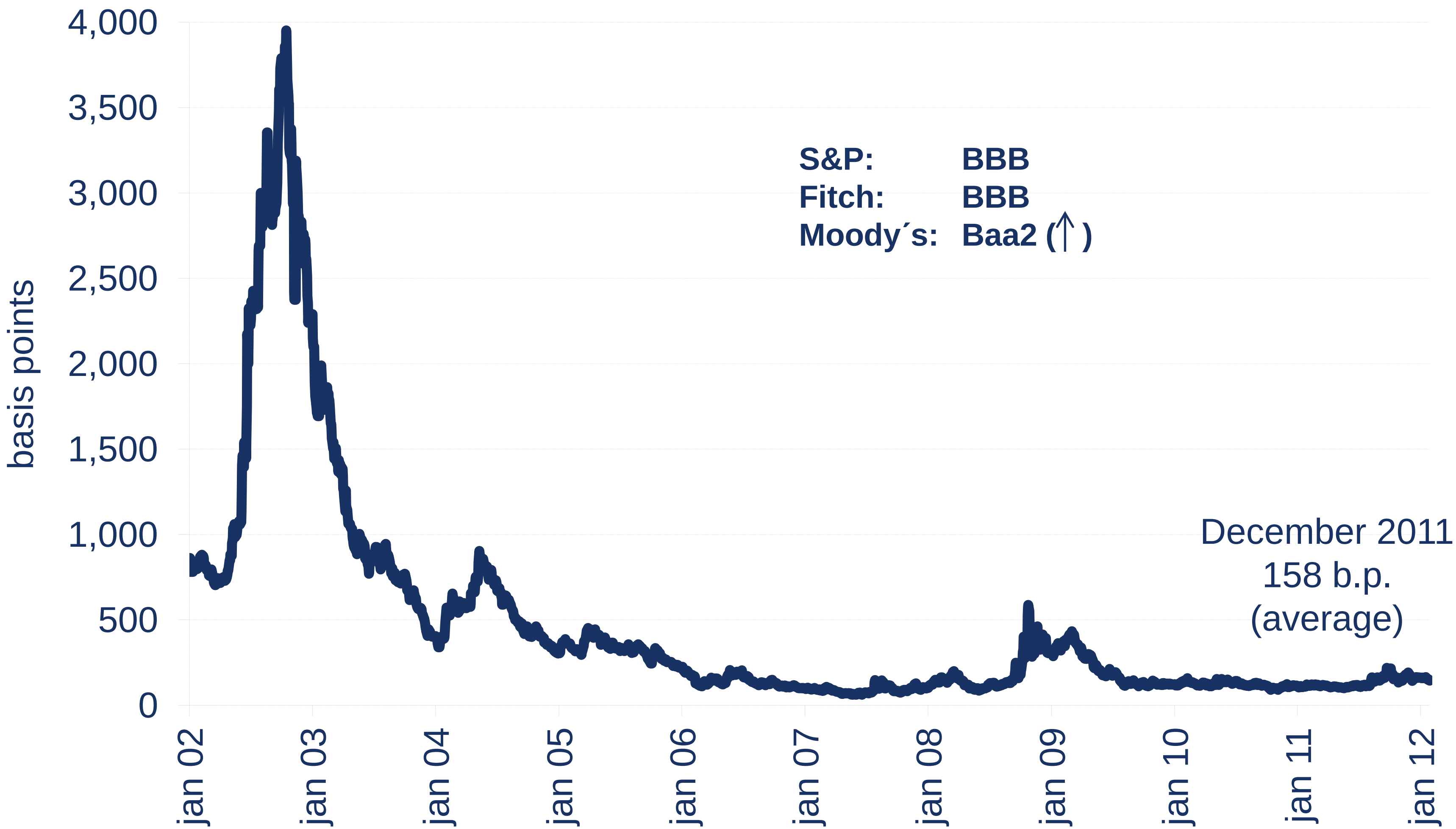
External Debt Ratios



*estimate

Source: BCB

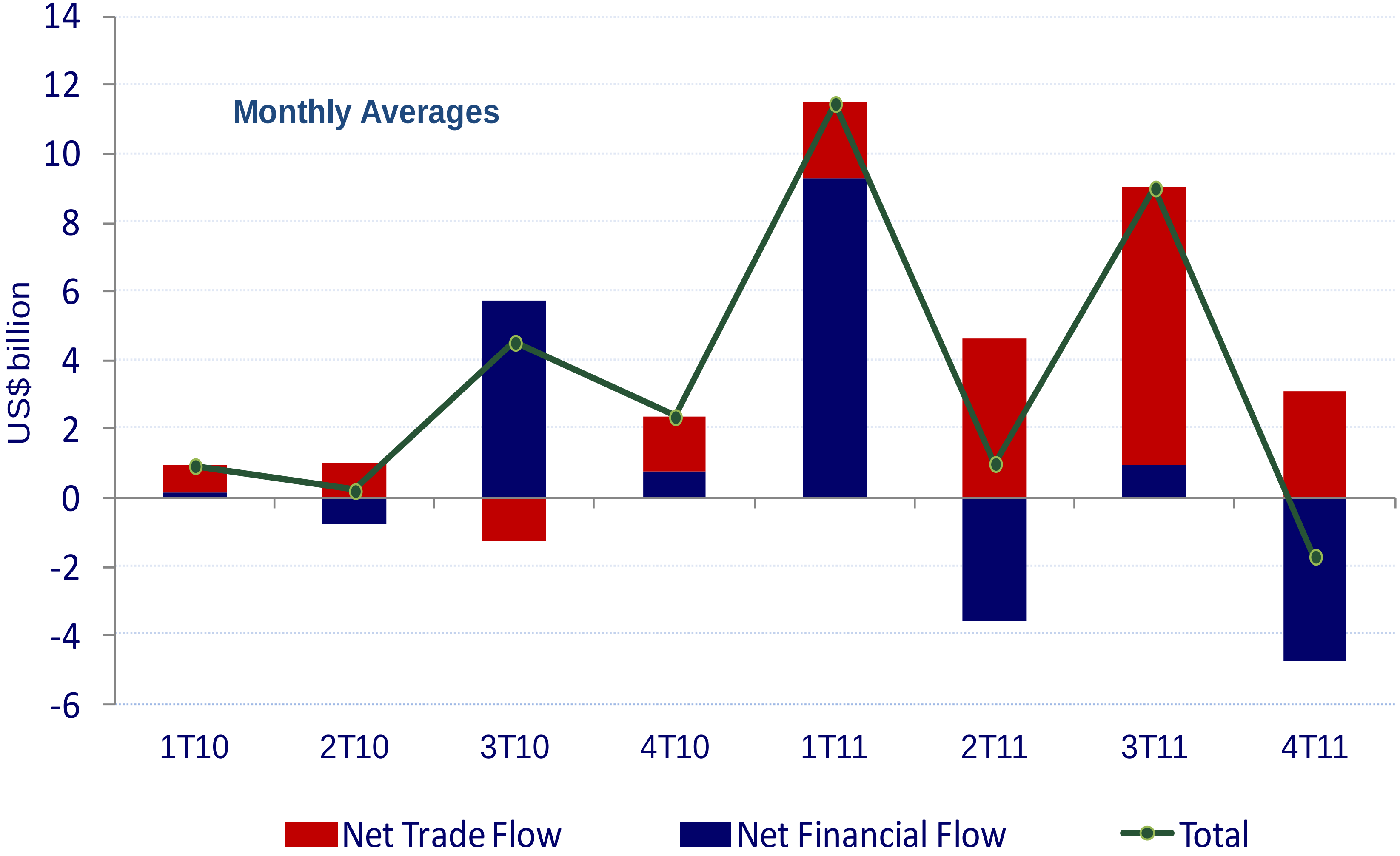
Sovereign Risk (CDS)



up to Jan 27th

Source: Bloomberg

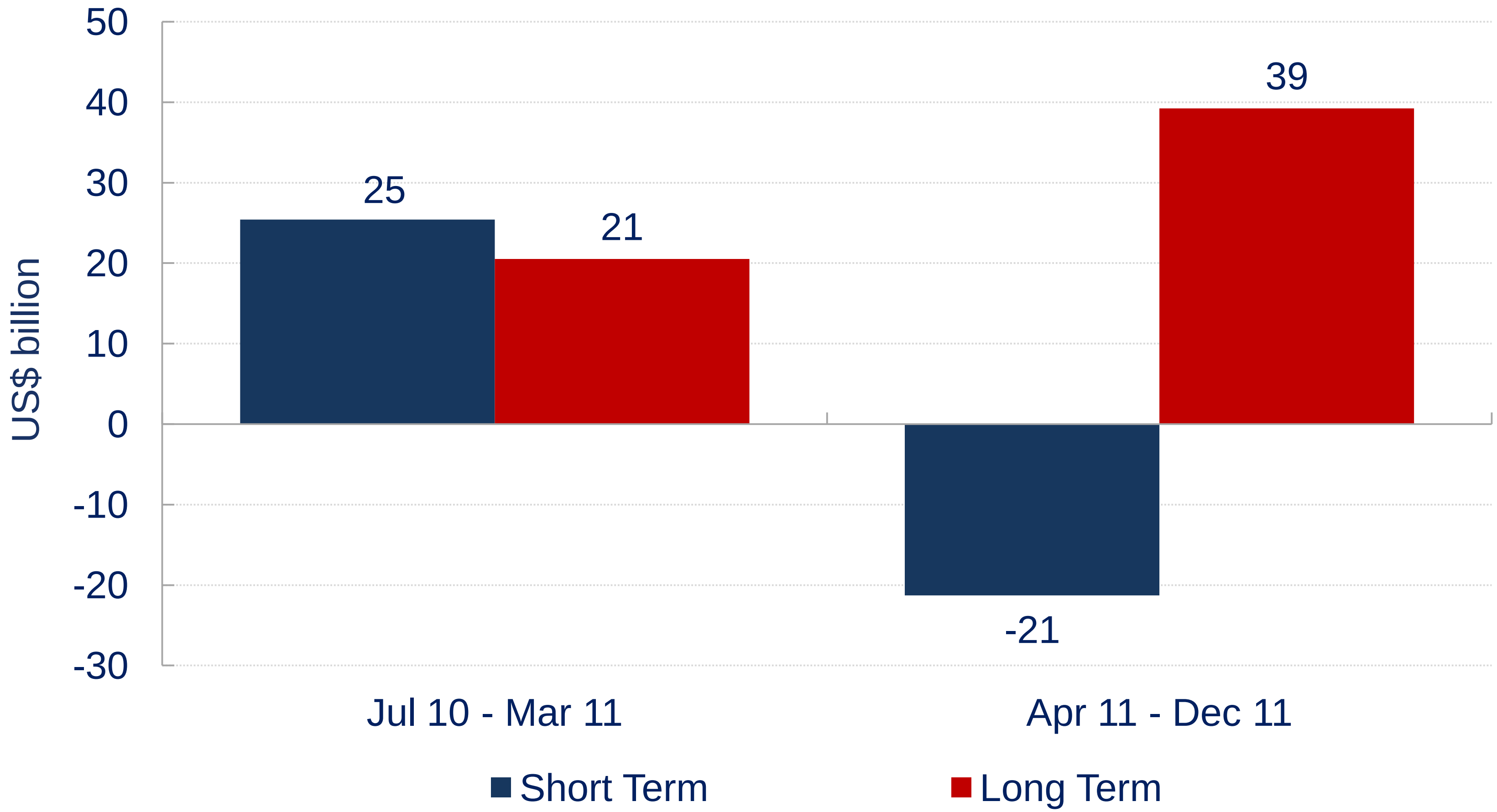
Capital Flows – Inflow Moderation



Source: BCB

Capital Flows – Better Profile/ Composition

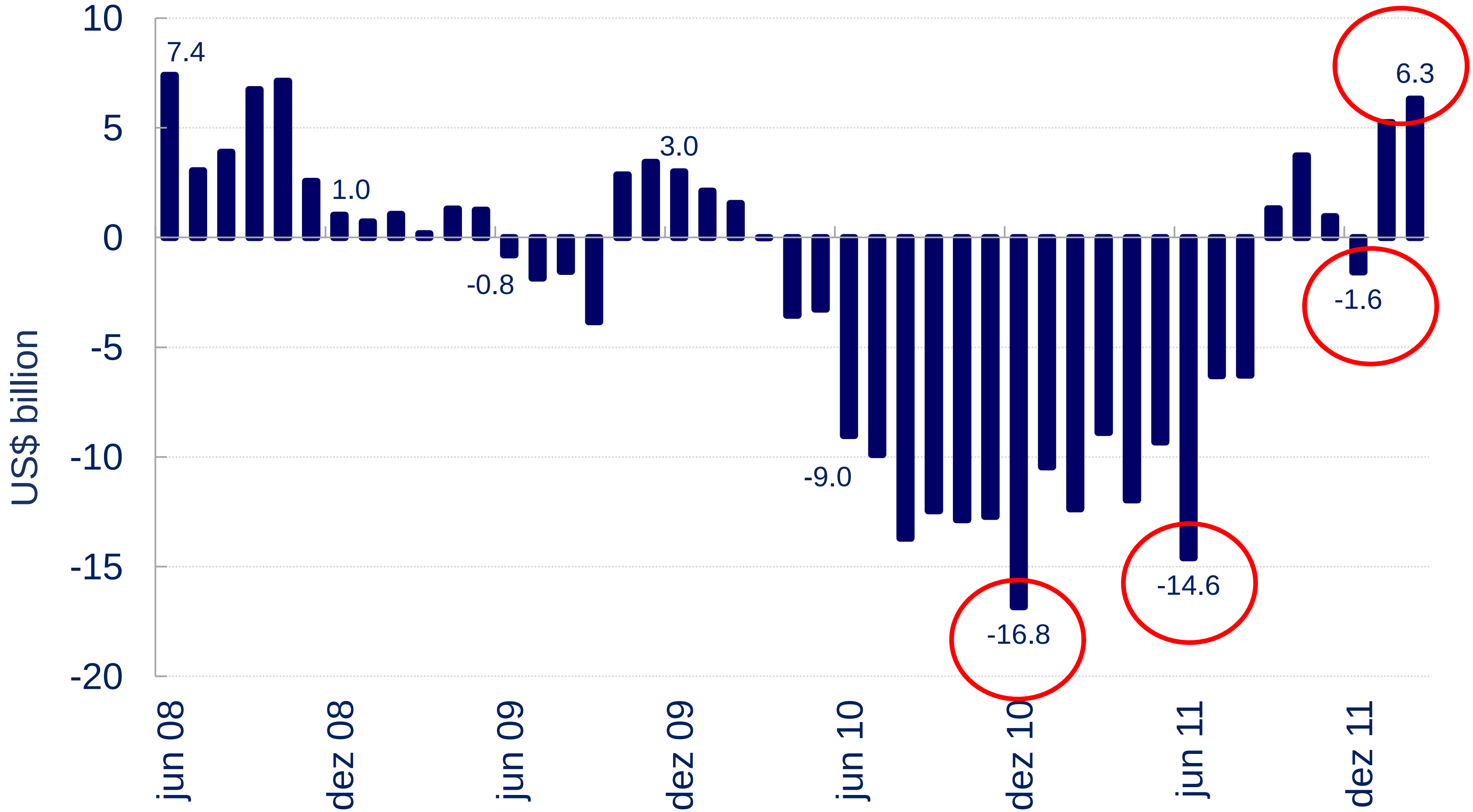
The amount of long term capital inflows to Brazil has recently increased



Source: BCB

Banks Short FX Positions

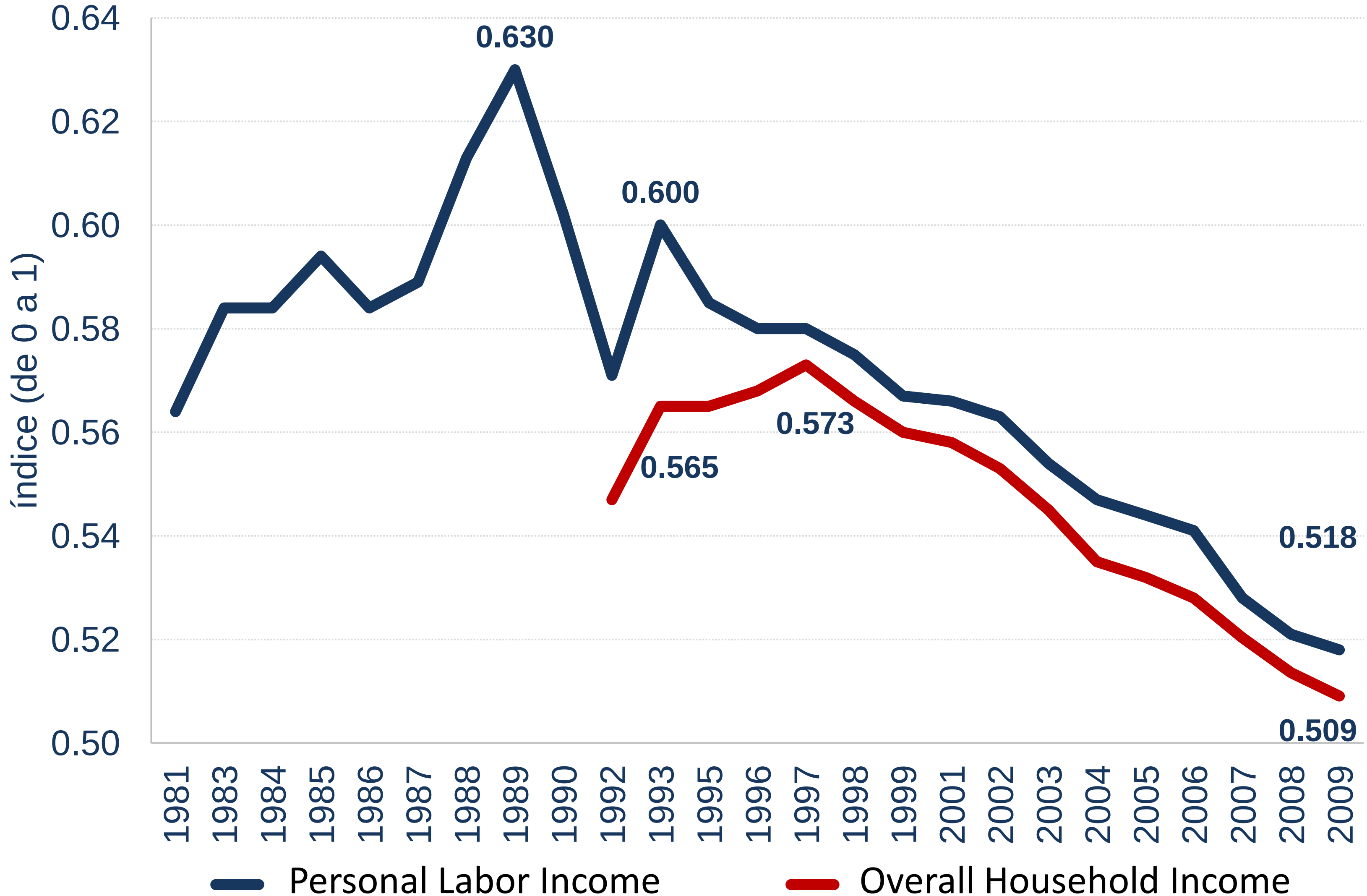
Financial institutions were enticed by the CB measures to reduce their net short FX positions.



up to Feb 2, 2012

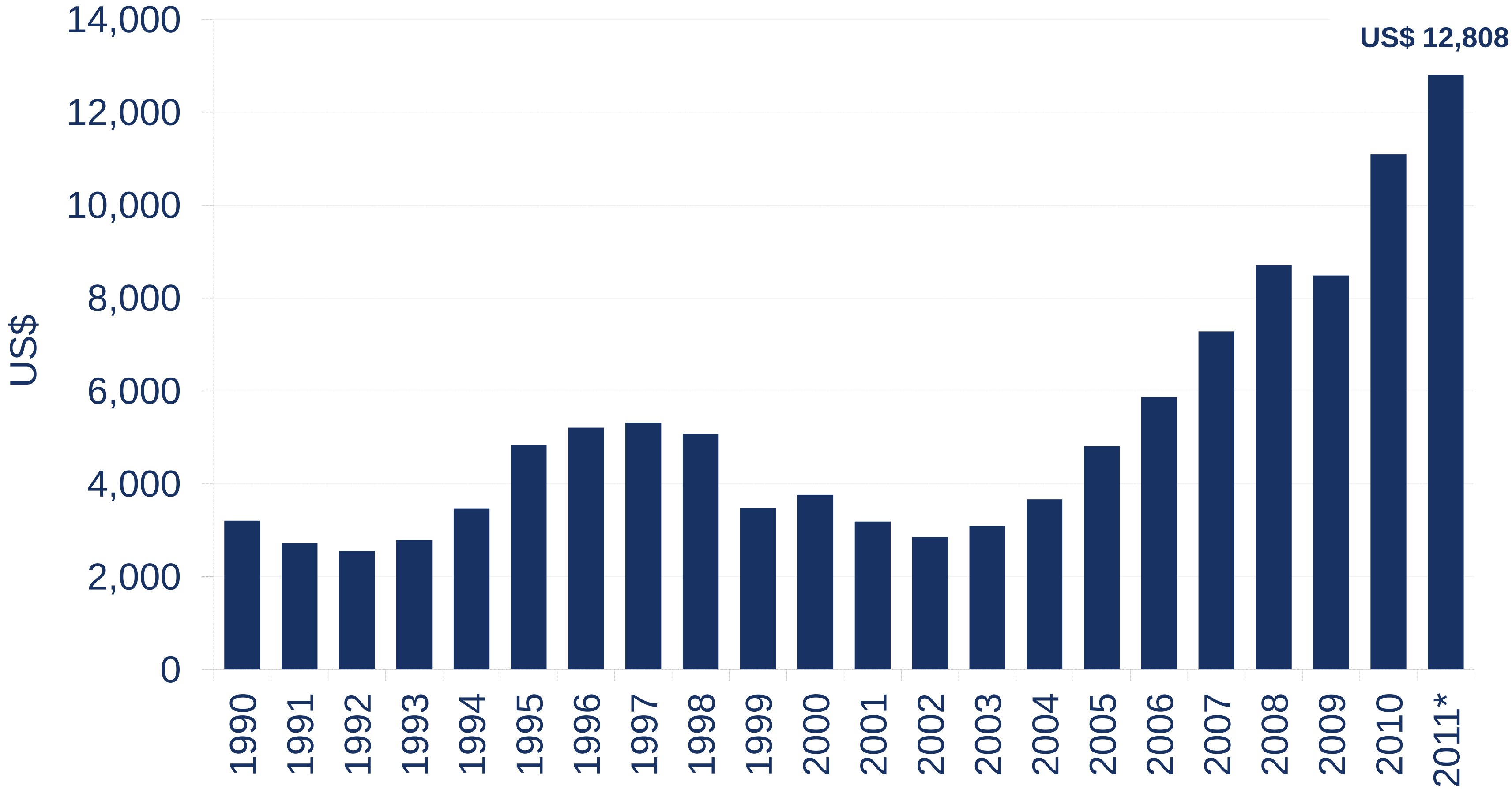
Source: BCB

Better Income Distribution – Gini Coefficient



Source: IBGE

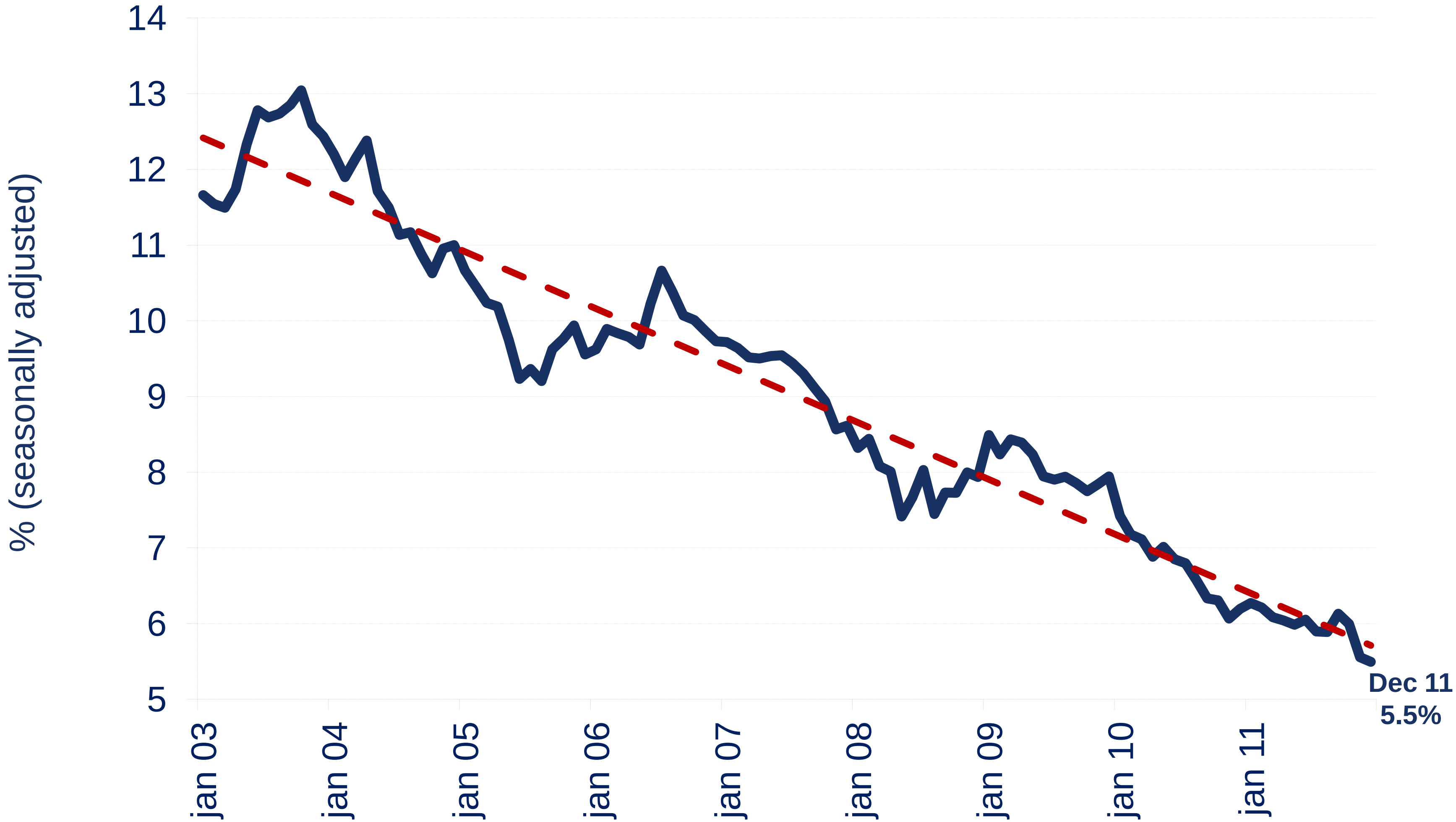
GDP per Capita



***Forecast from Central Bank of Brazil (Inflation Report – Dec 11)**

Sources: BCB / IBGE

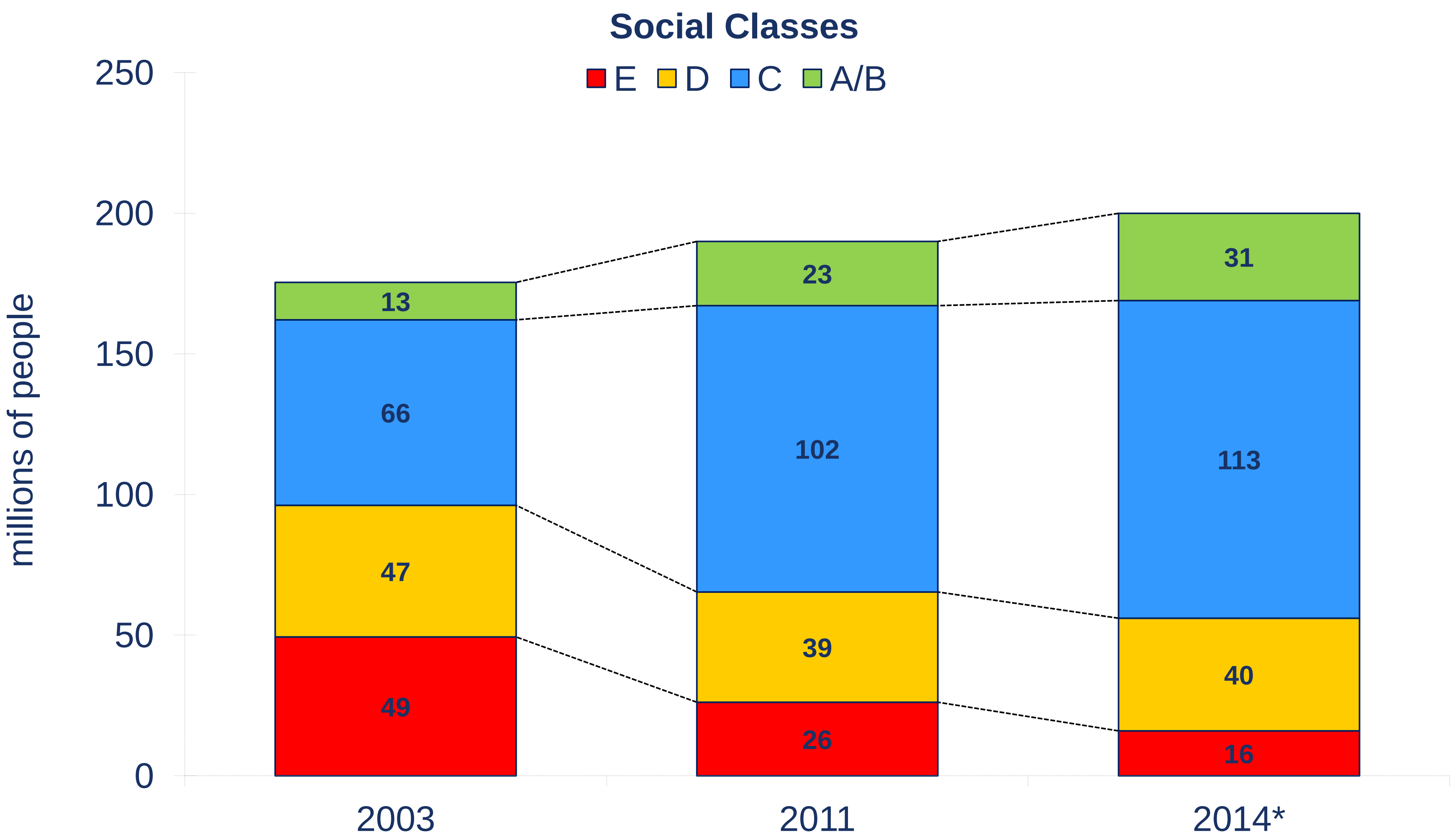
Unemployment Rate



up to Dec 11

Source: IBGE

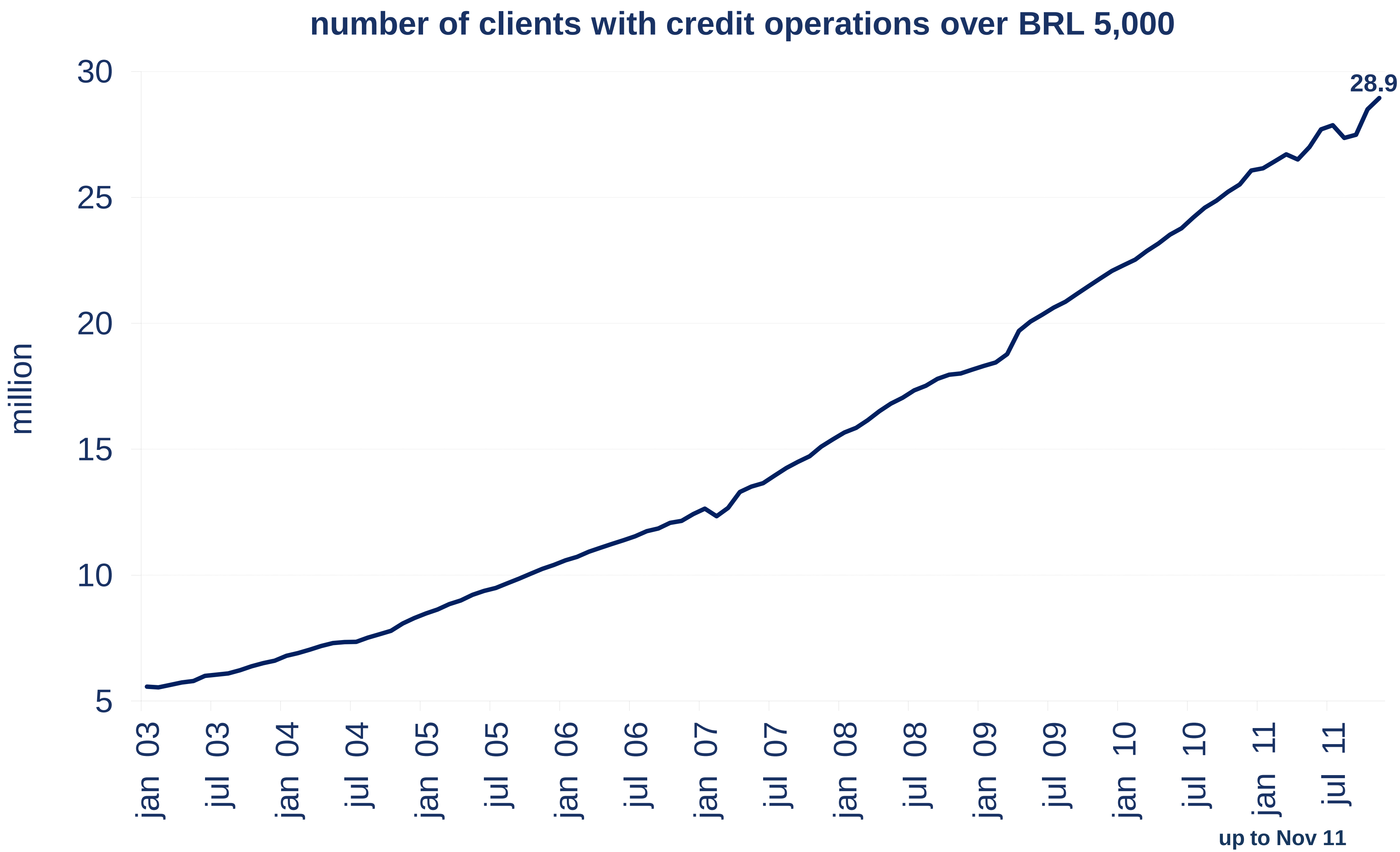
Social Mobility



*FGV forecast

Source: FGV

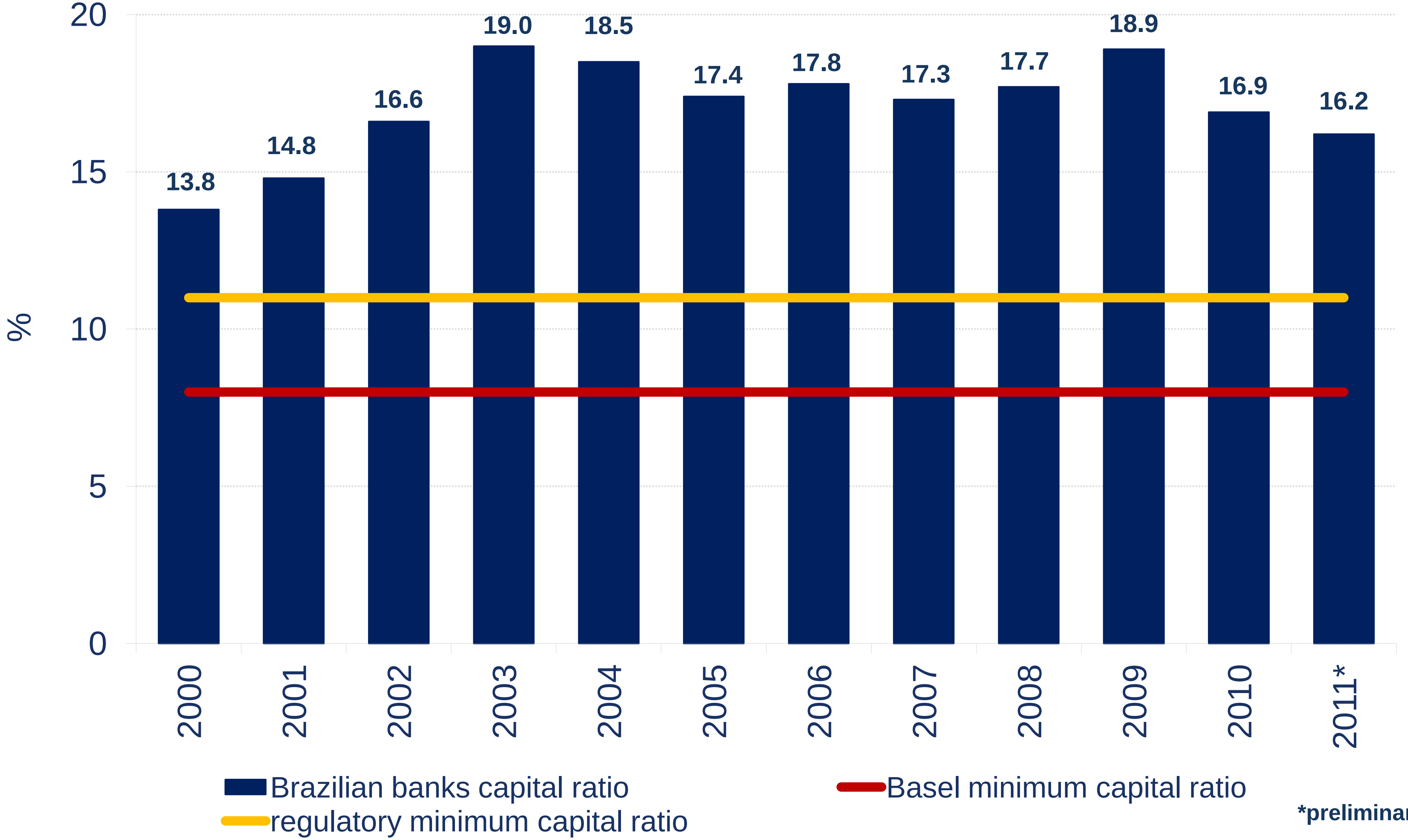
Financial Inclusion



Source: BCB

Brazilian Banks - Capital Adequacy Ratio

leverage ratio: 10.3

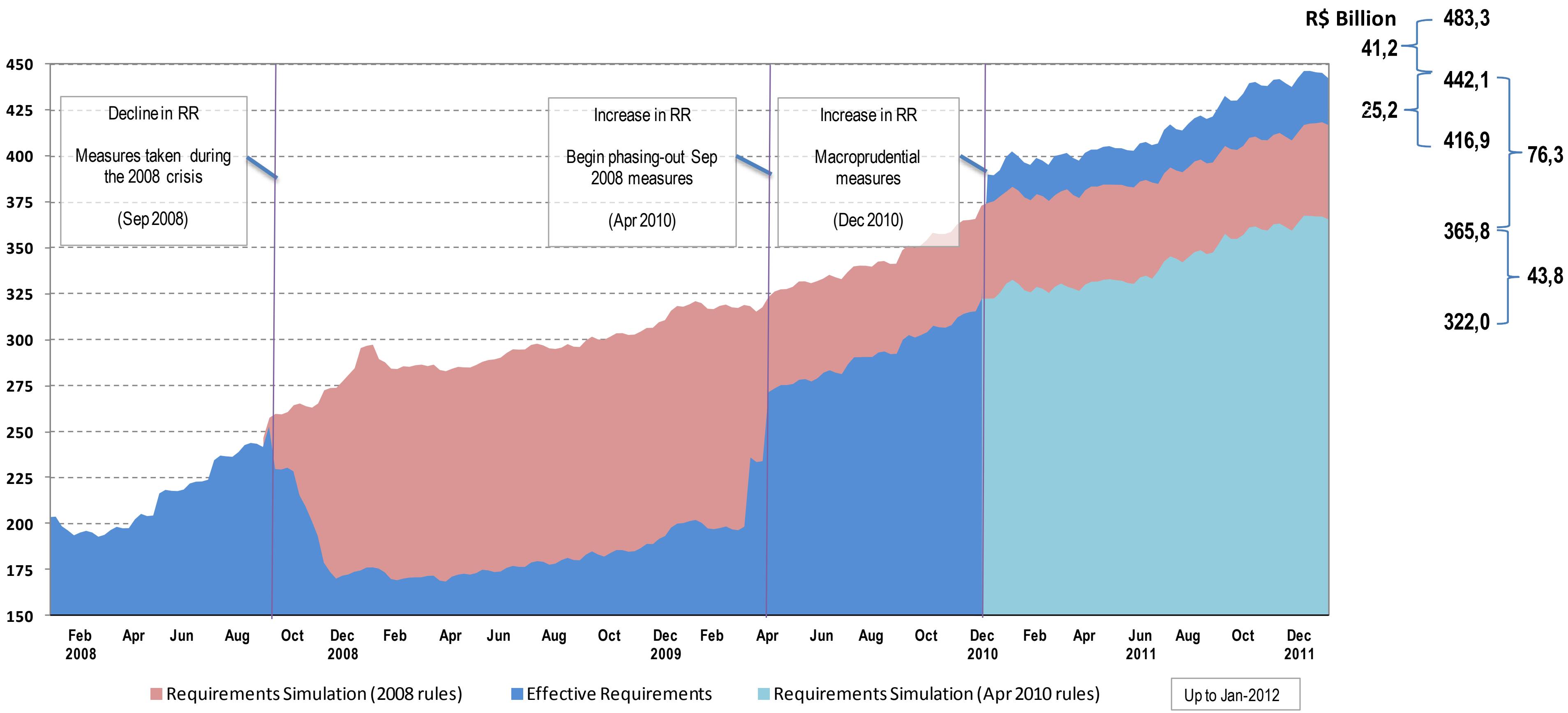


*preliminary

Source: BCB

Bank Reserves on Demand & Time Deposits

Reserve Requirements are R$ 76.3 billion higher because of December 2010 measures. The total amount is R$ 205.6 billion greater than July 2008 level.



Source: Central Bank of Brazil

BANCO CENTRAL DO BRASIL

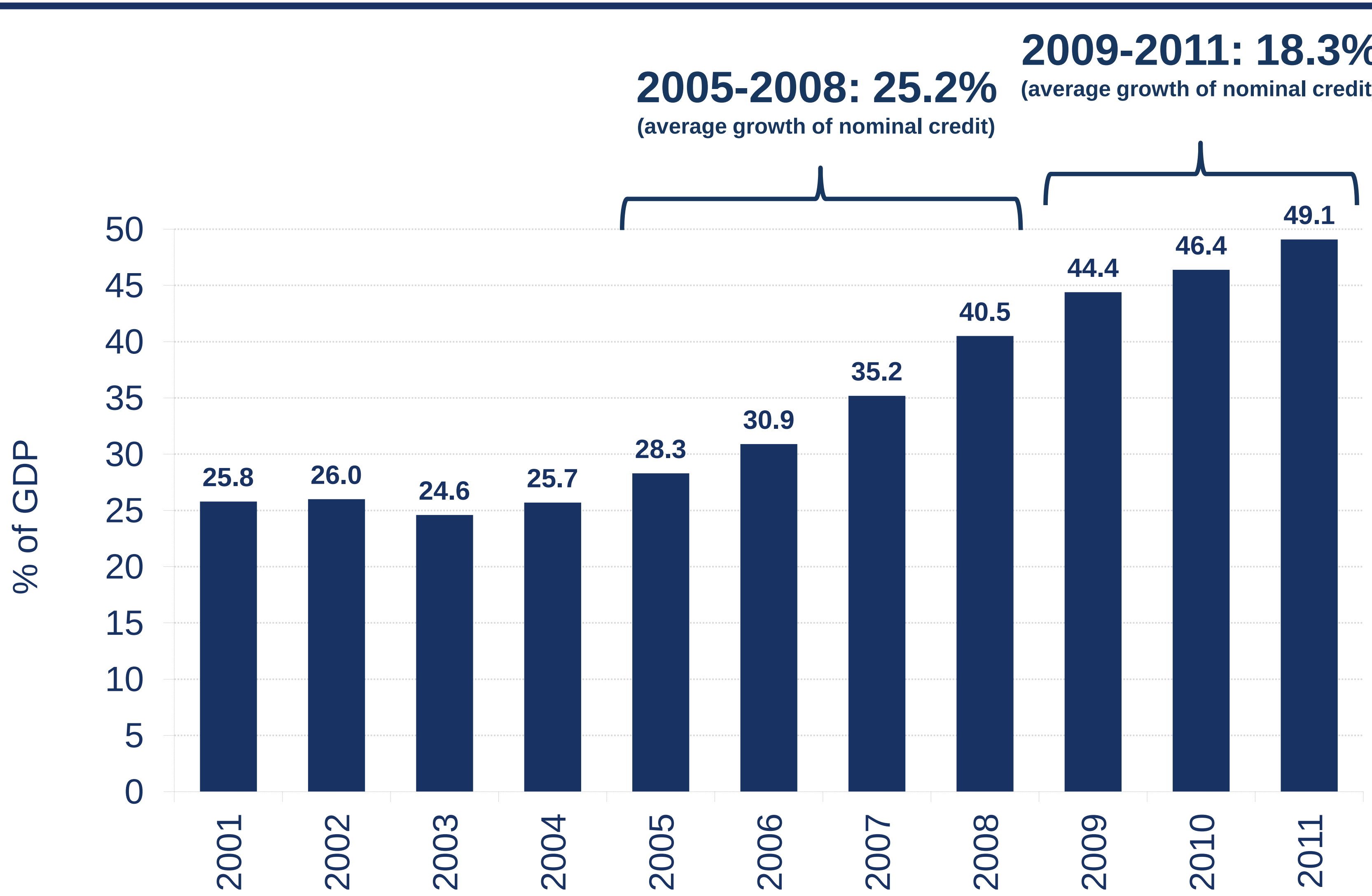
High Provisions / NPLs

Country	Provisions / NPLs (%)	
Mexico	163.8	September 2010
Brazil	159.0	September 2011
France	131.0	December 2009
Korea	125.2	September 2010
Russia	94.8	December 2010
Turkey	81.9	November 2010
Australia	68.0	September 2010
South Africa	61.3	December 2005
Canada	59.1	September 2010
United States	58.1	December 2010
Germany	51.3	December 2008
Italy	46.1	December 2009
United Kingdom	30.1	June 2010

Source: Central Bank of Brazil, Financial Stability Report 2011

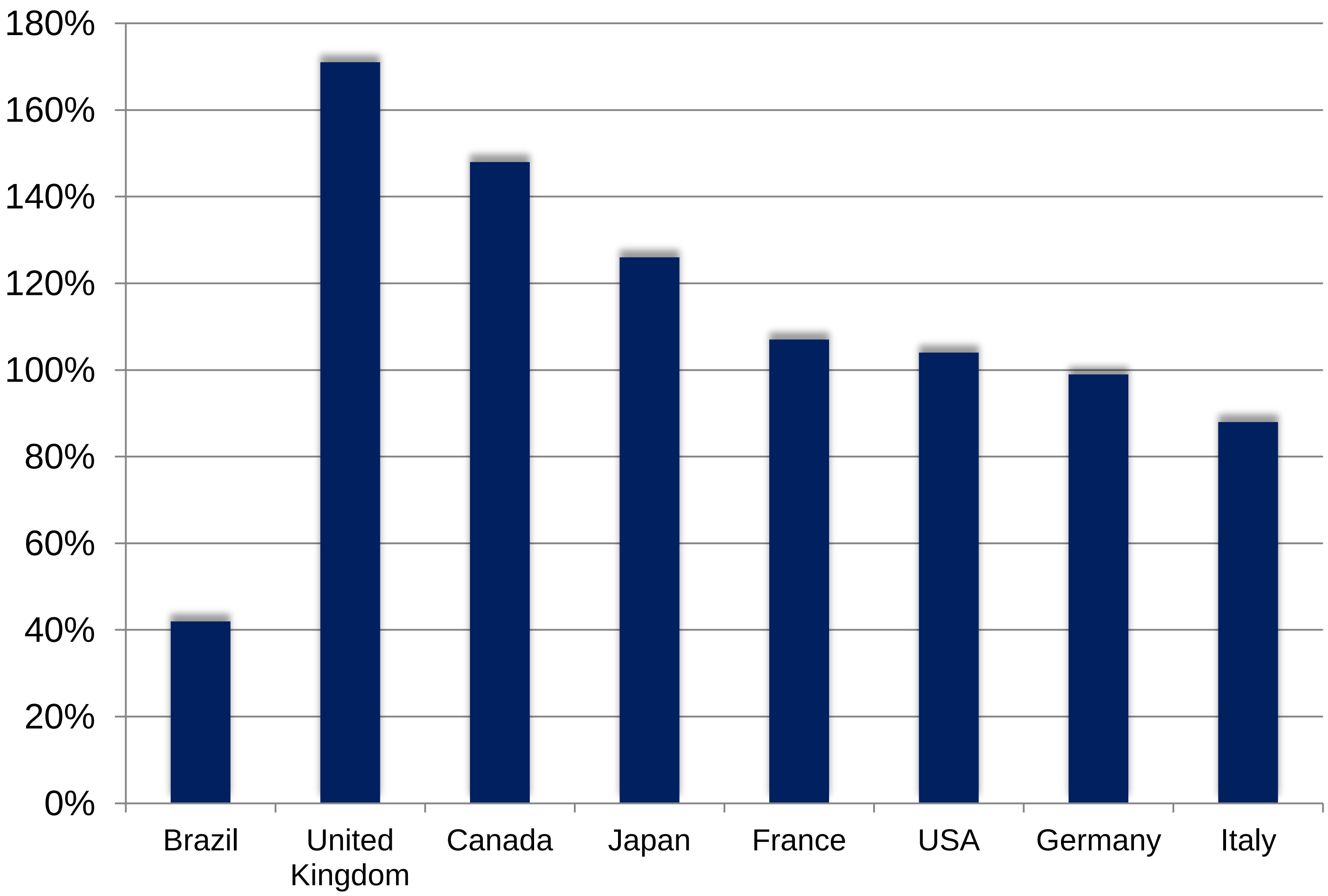
BANCO CENTRAL DO BRASIL

Credit / GDP



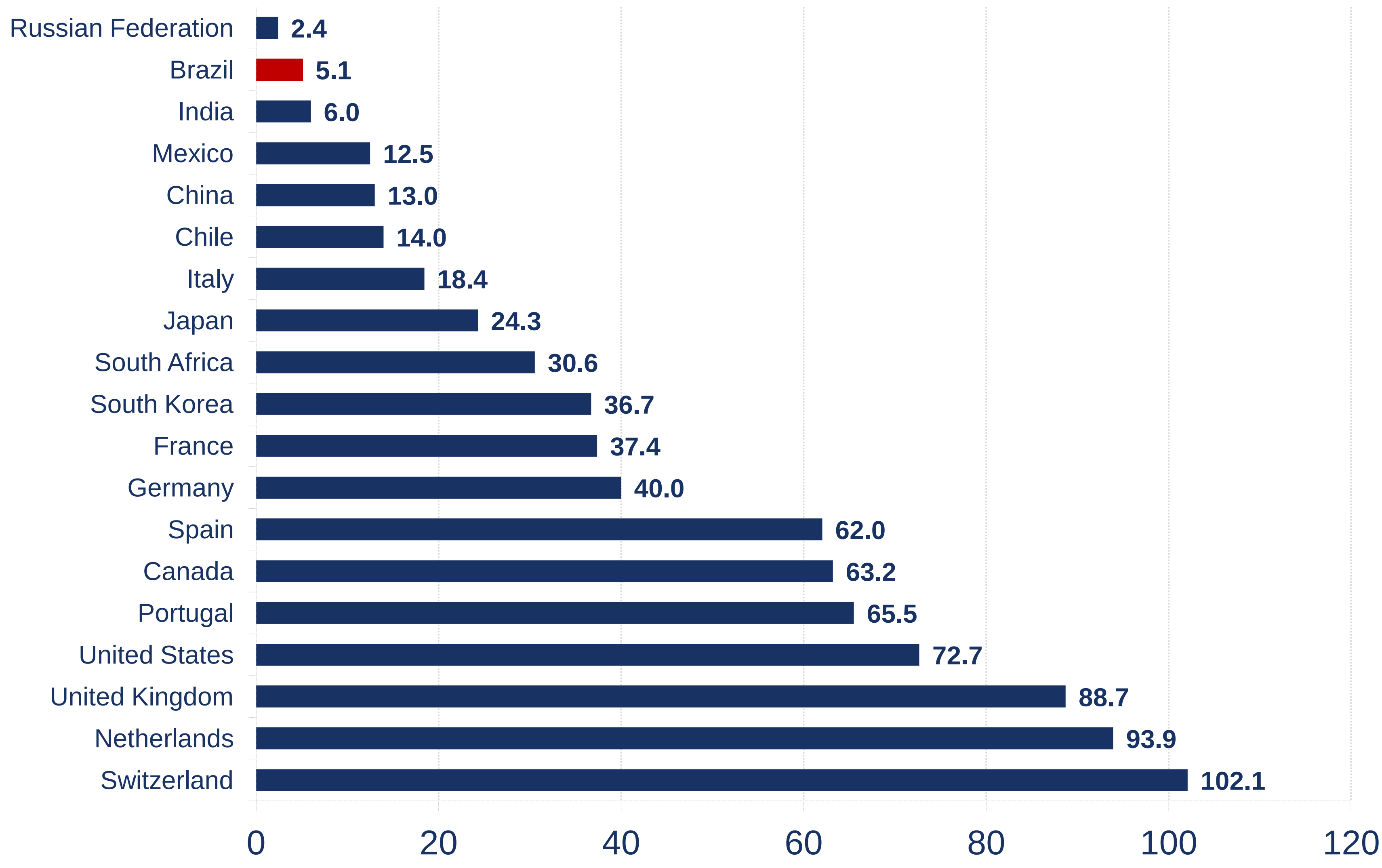
Source: BCB

Household Debt-to-Income Ratio



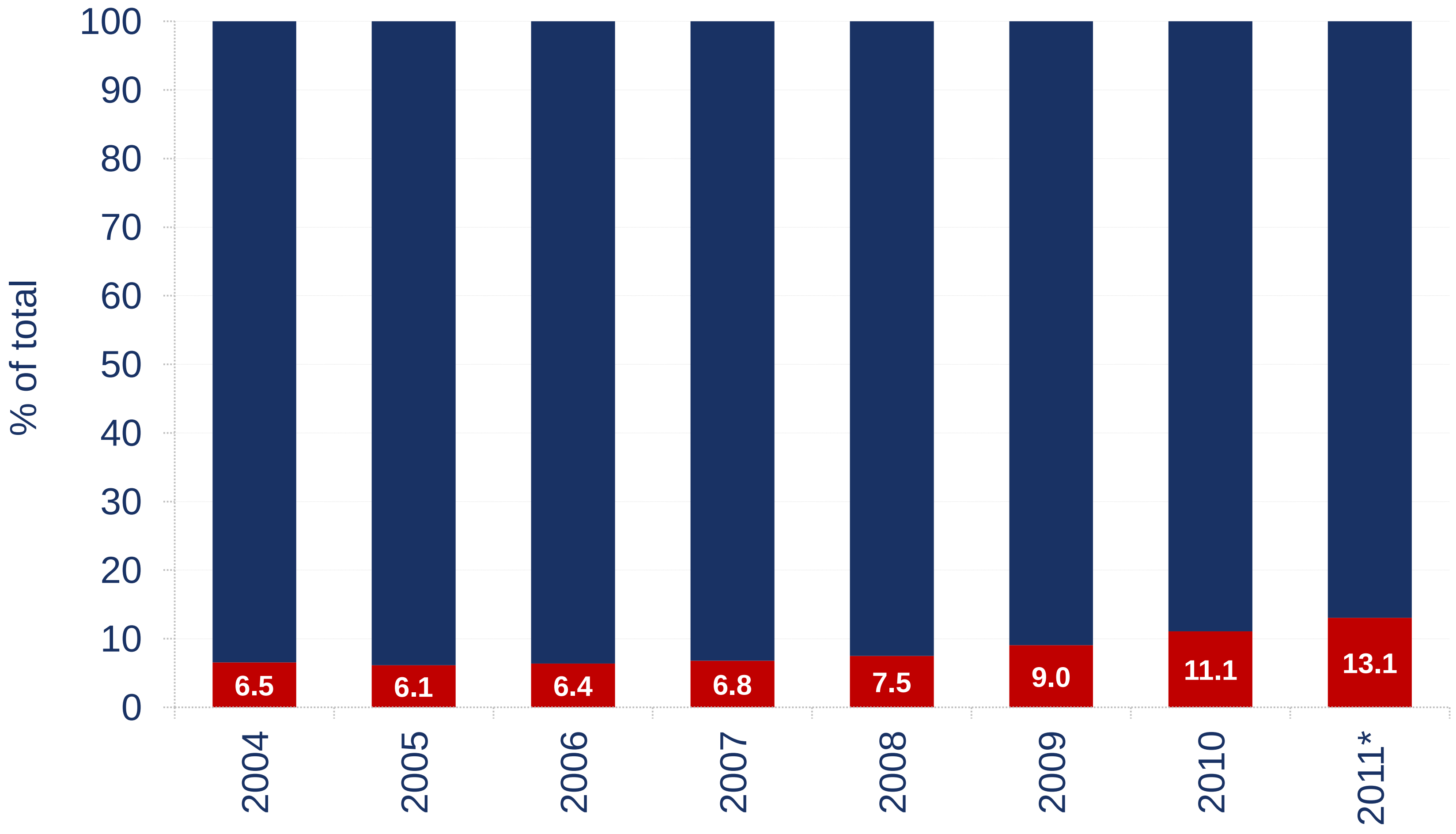
Source: OECD

Housing Credit / GDP



Sources: BCB / World Bank

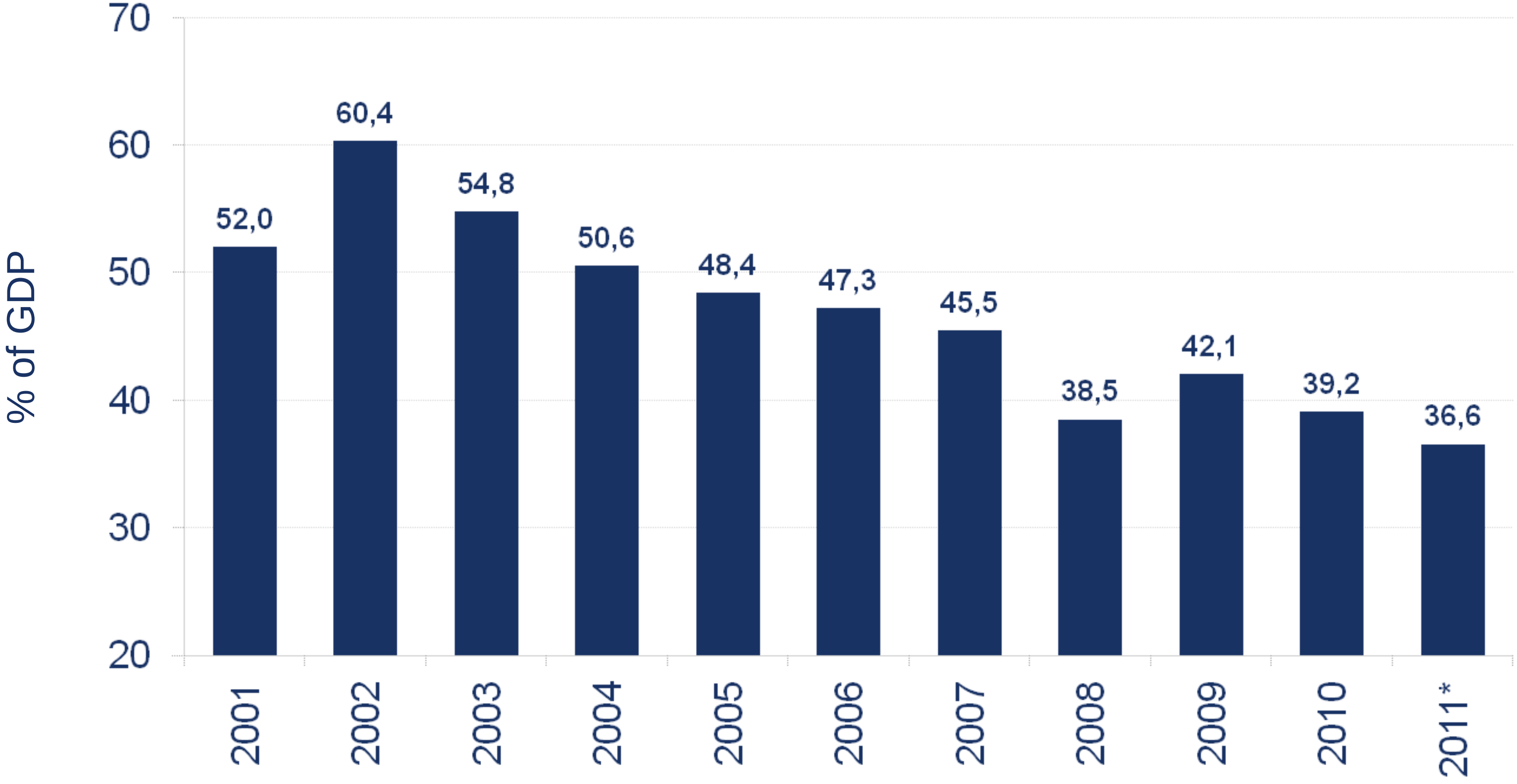
Housing Credit / Total Credit



*Nov 11

Source: BCB

Net Public Debt



*Nov 11

Source: BCB

4. Brazil: A World-Class Financial Infrastructure

The Brazilian Financial Infrastructure

- **A safe and reliable environment to the universe of 2,470 institutions in the country:**

135	Commercial Banks	19	Investment Banks
16	Development Banks	4	Payment Systems
320	Brokers	6	Settlement Systems
485	Others	1,488	Credit Unions

Banco Central do Brasil (BCB) – Mission

- **To ensure:**
  - **Stability of Brazil´s currency purchasing power**
  - **Soundness of the country´s financial system**
- **To regulate and supervise the financial system**
- **To oversee payments, securities and derivatives settlement systems**

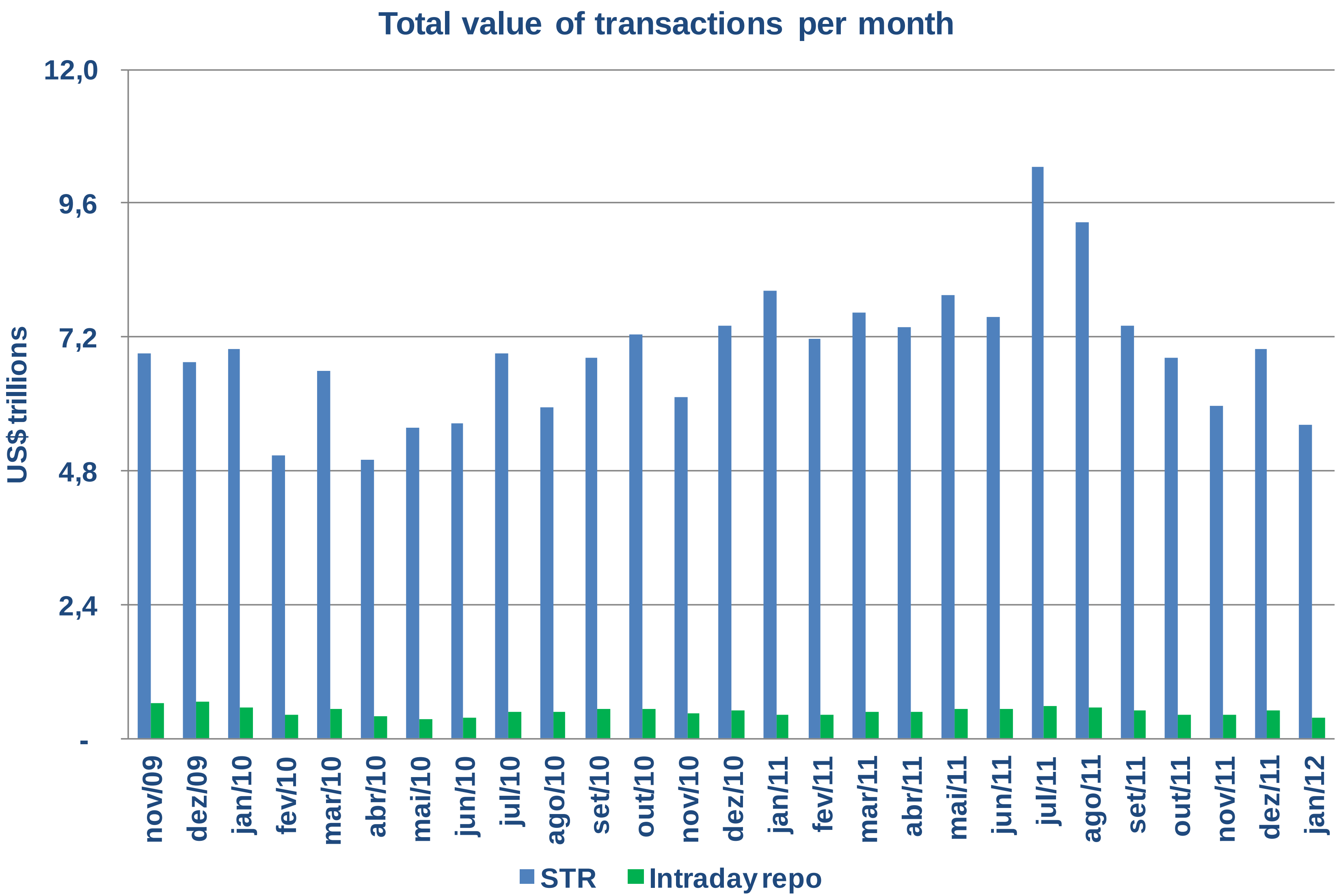
The Brazilian Payment System – main features

- **A real time gross settlement (RTGS) system for funds transfers – operated by the CB - settlement in central bank money**
- **Central counterparty (CCP) for securities, derivatives, foreign exchange (USD) and government bonds**
- **Full automation with *straight through processing* (STP), supported by a high-performance and open architecture network**

BCB as The Payments System Overseer

- **Risk management and compliance with regulations**
  - **Assessment against international standards (BIRD and IMF)**
  - **Periodic assessment of clearinghouses' management mechanisms (backtesting)**
  - **Periodic tests of payment system participants' contingency plans**
  - **Real time liquidity monitoring (preventing gridlock events)**
  - **DVP is observed in all systems**

Brazilian RTGS – STR



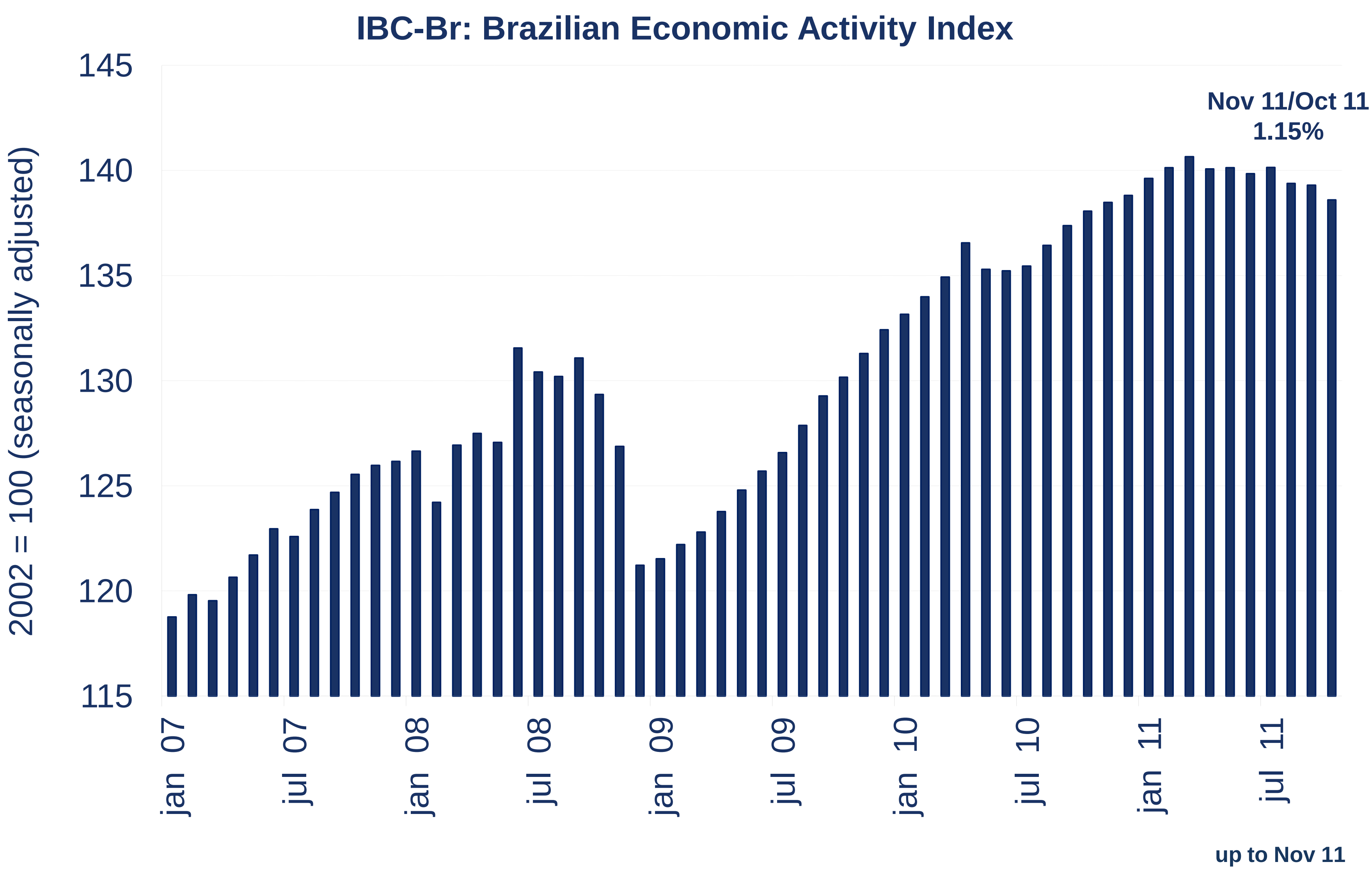
BANCO CENTRAL DO BRASIL

Additional Information

- No restrictions to capital flows
- Inflows require electronic registration (not an authorization) with the BCB
- FX registration must be carried out by a local representative
- No minimum period requirements for remittances
- The law protects final investor's equities - not deemed to be owned by the intermediary (broker/custodian) even in case of bankruptcy
- Compliant with global anti-money laundering efforts (largely compliant with the FATF 40 recommendations)

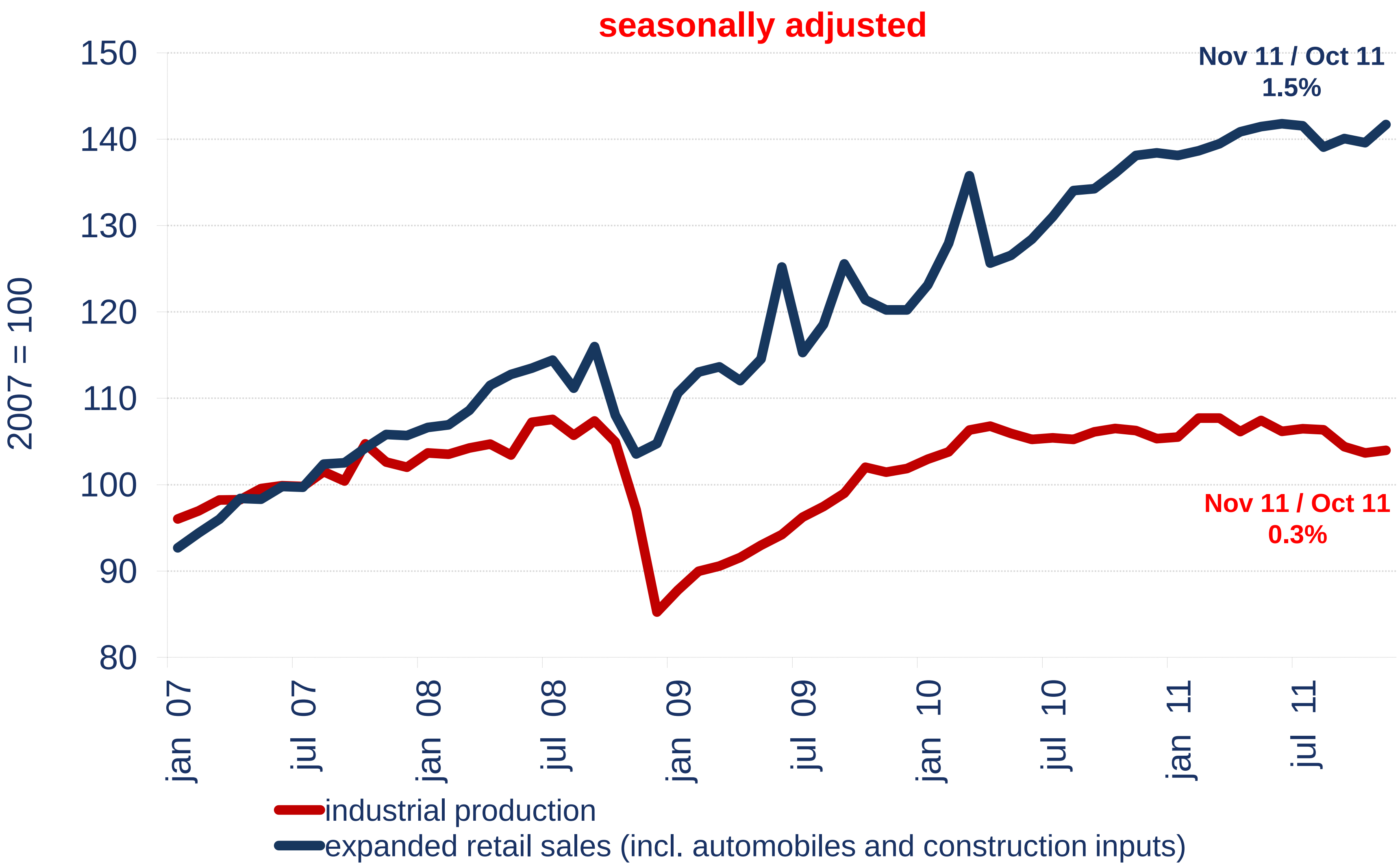
5. Short Term Developments and Current Economic Indicators

Leading Indicator



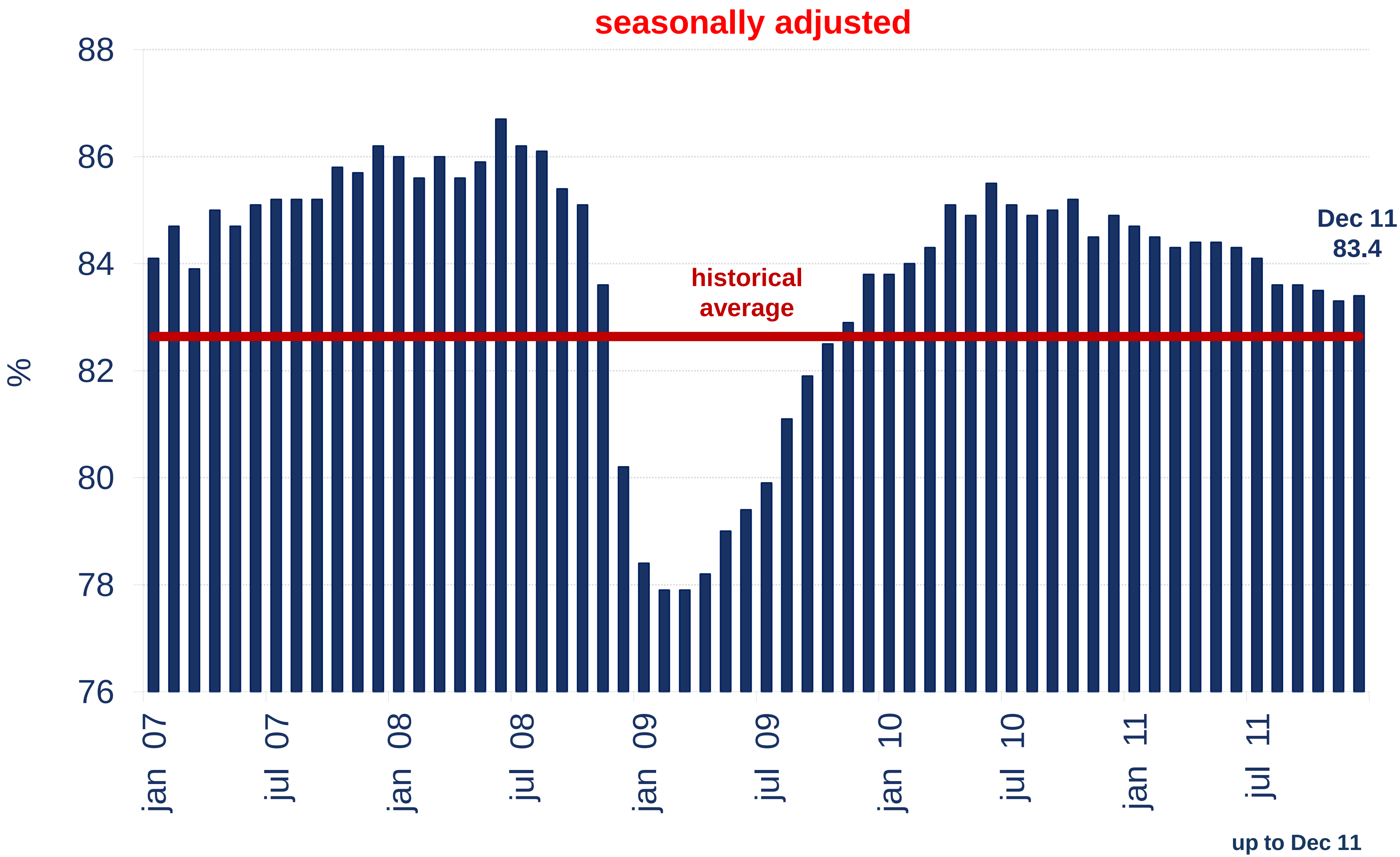
Source: BCB

Industrial Production vs. Retail Sales



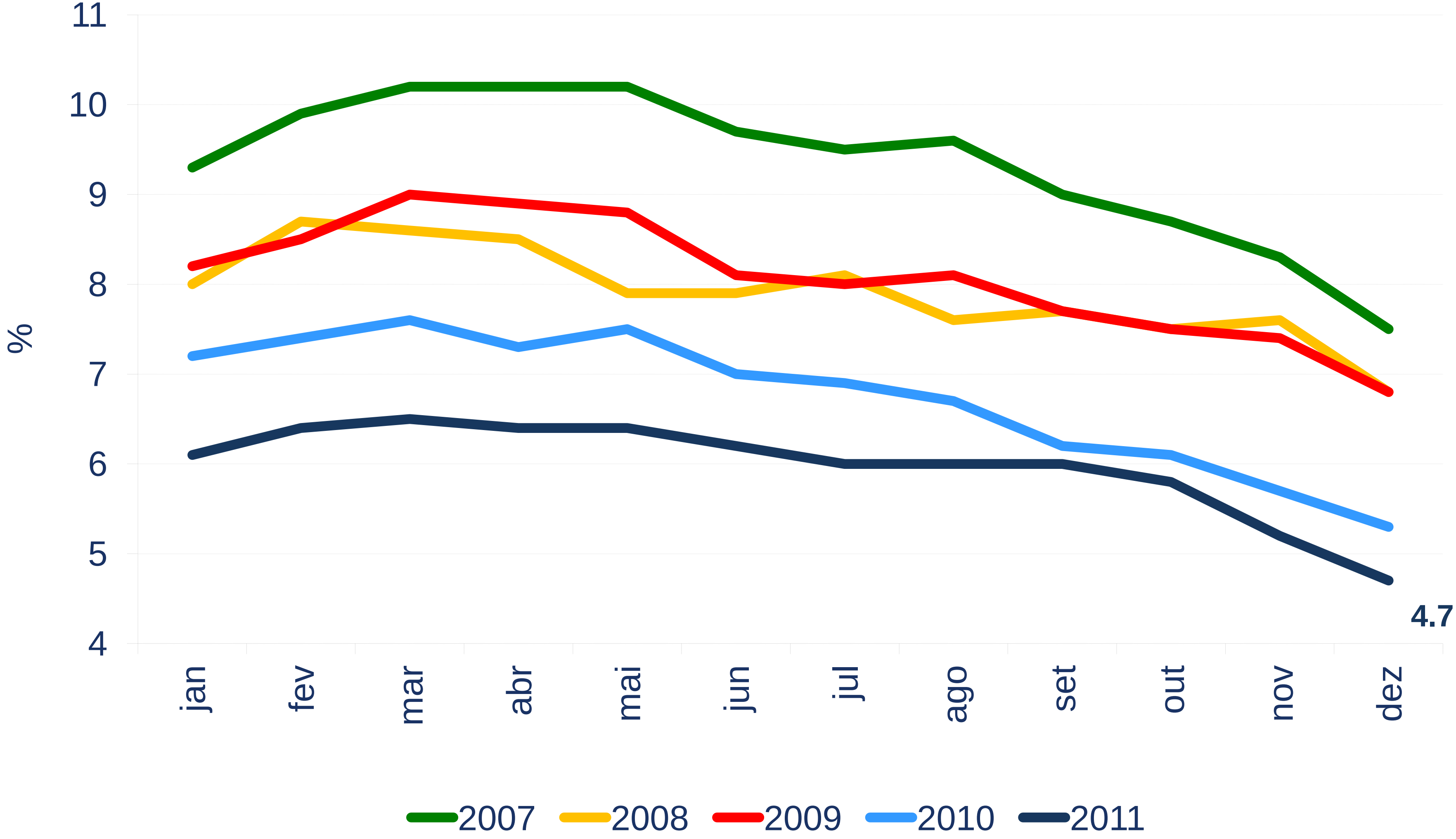
up to Nov 11

Industrial Capacity Utilization



Source: FGV

Unemployment Rate

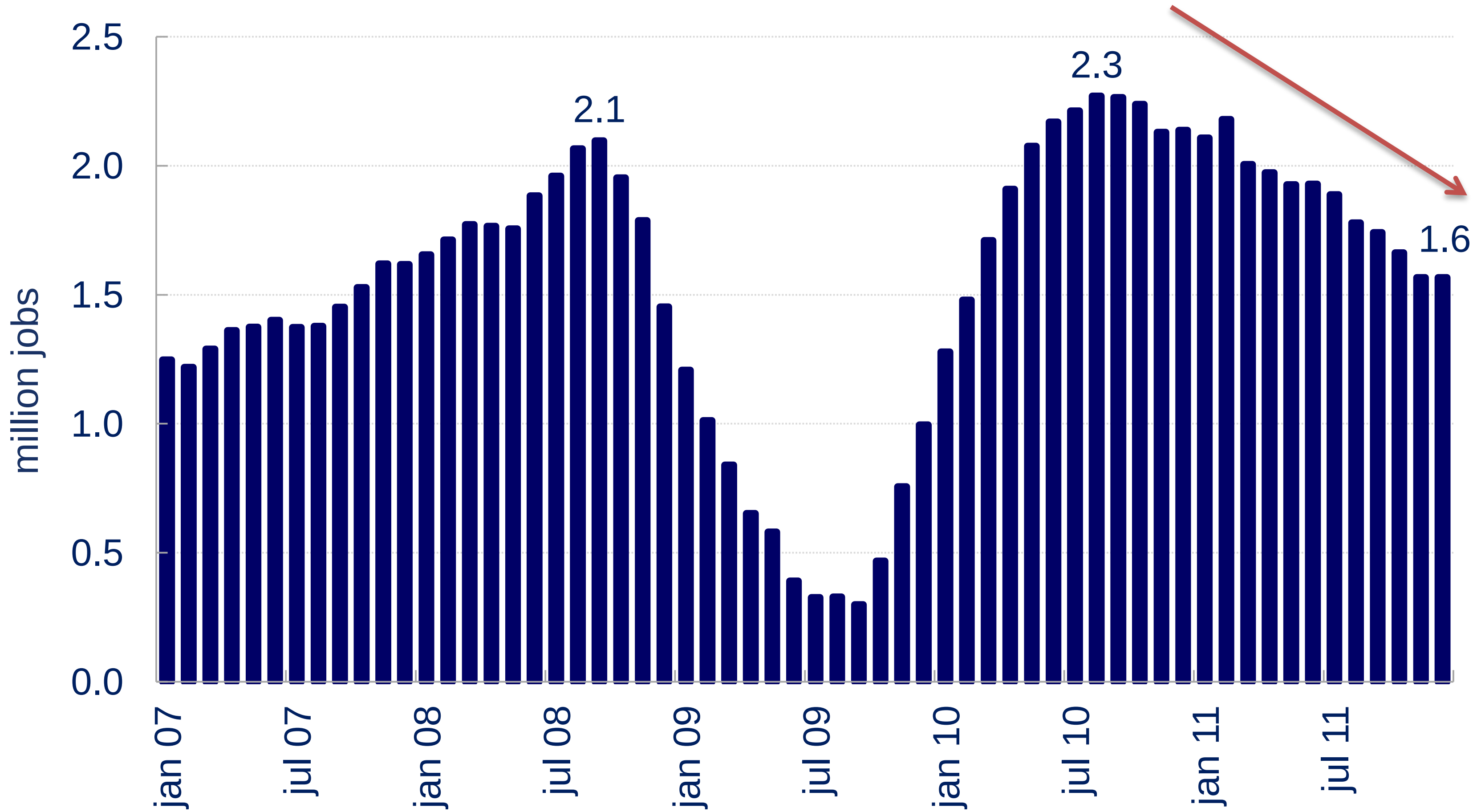


Source: IBGE

Formal Job Creation

Formal job creation endures but in a bit more moderate pace than in previous months.

12 months accrual rate

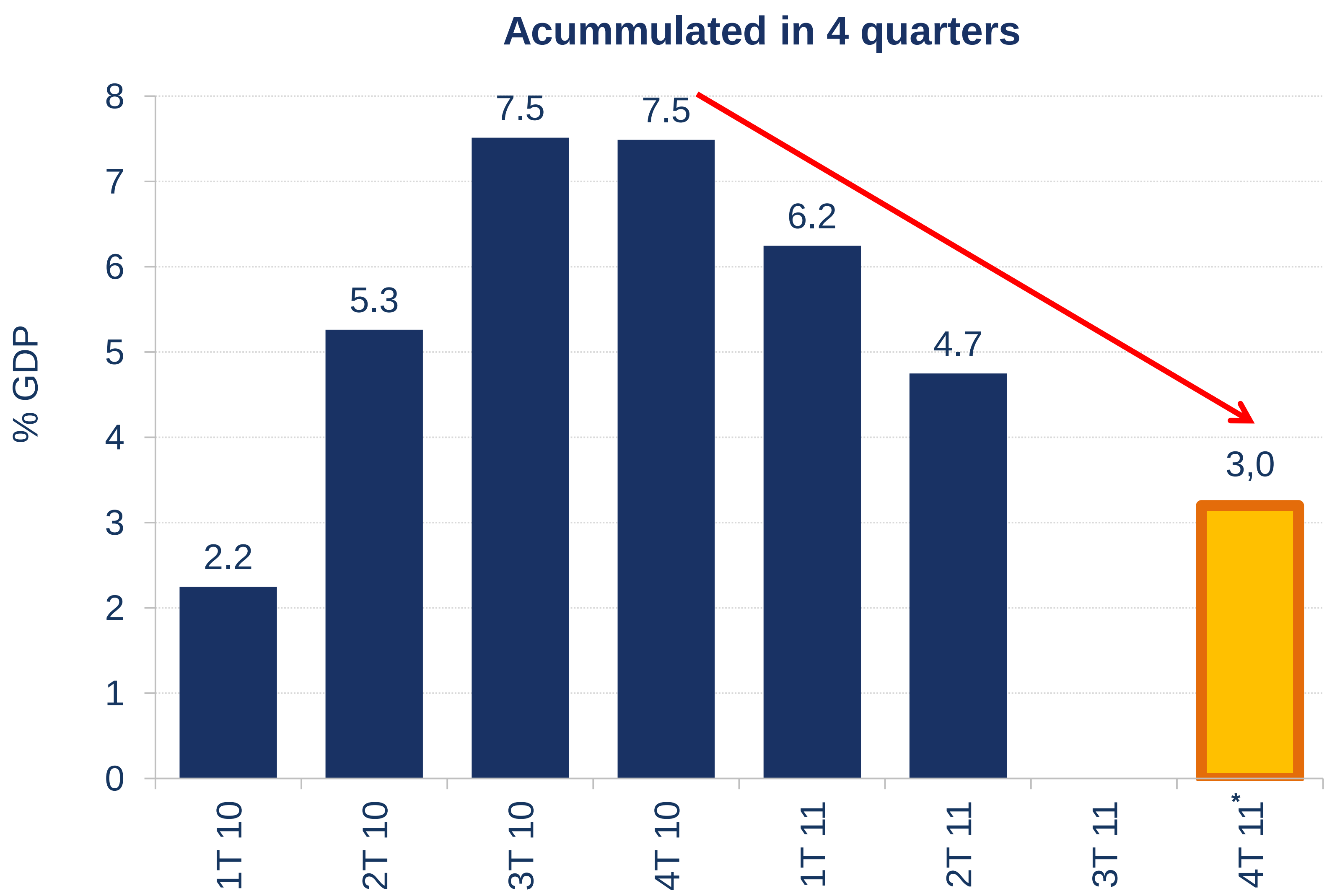


up to Dec 11, without adjustments

Source: Ministry of Labor (MTE)

BANCO CENTRAL DO BRASIL

Economic Growth is moderating



*Focus forecast by Nov. 18, 2011

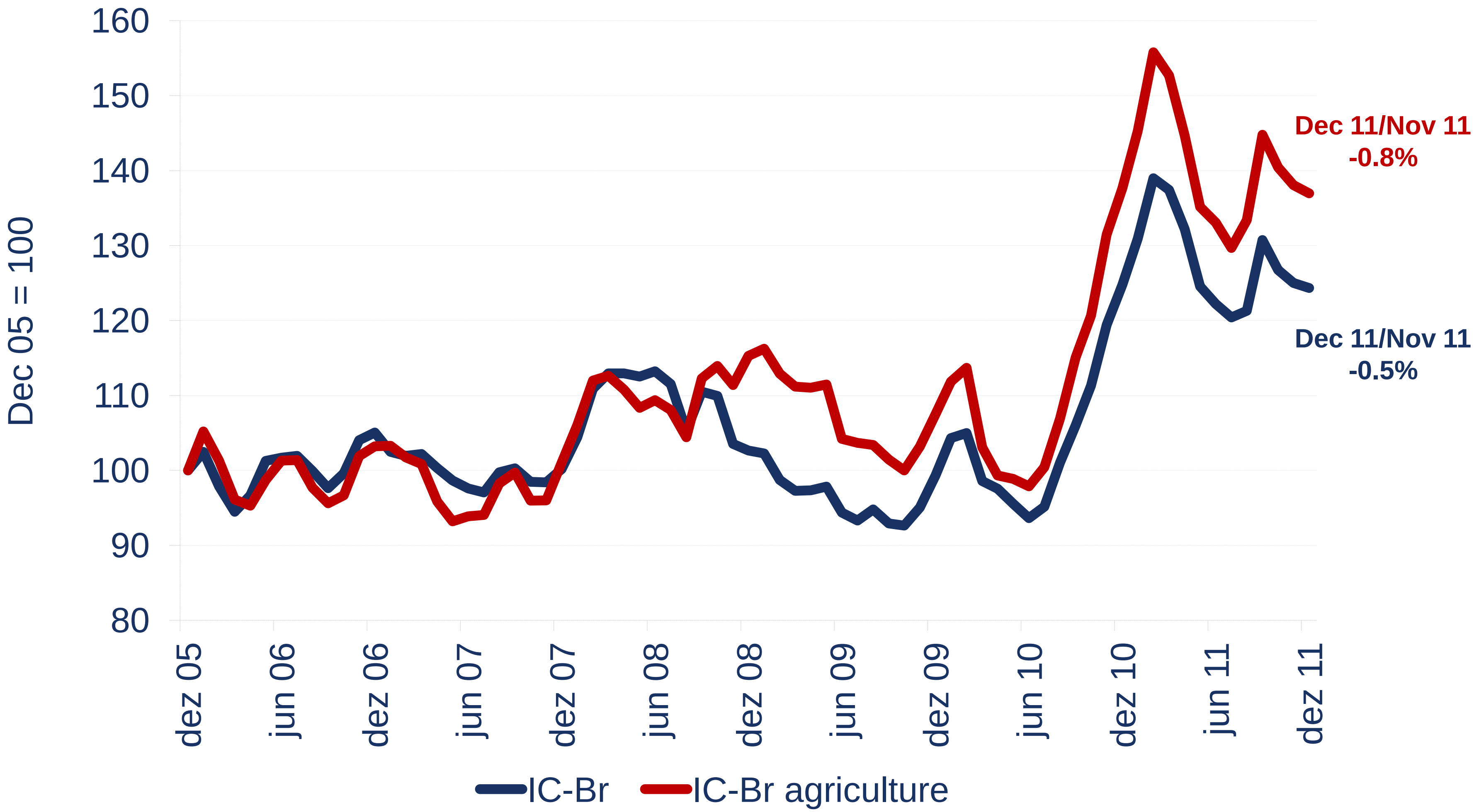
Source: IBGE / BCB

Consumer Price Index (IPCA)

up to Dec 11

Source: IBGE

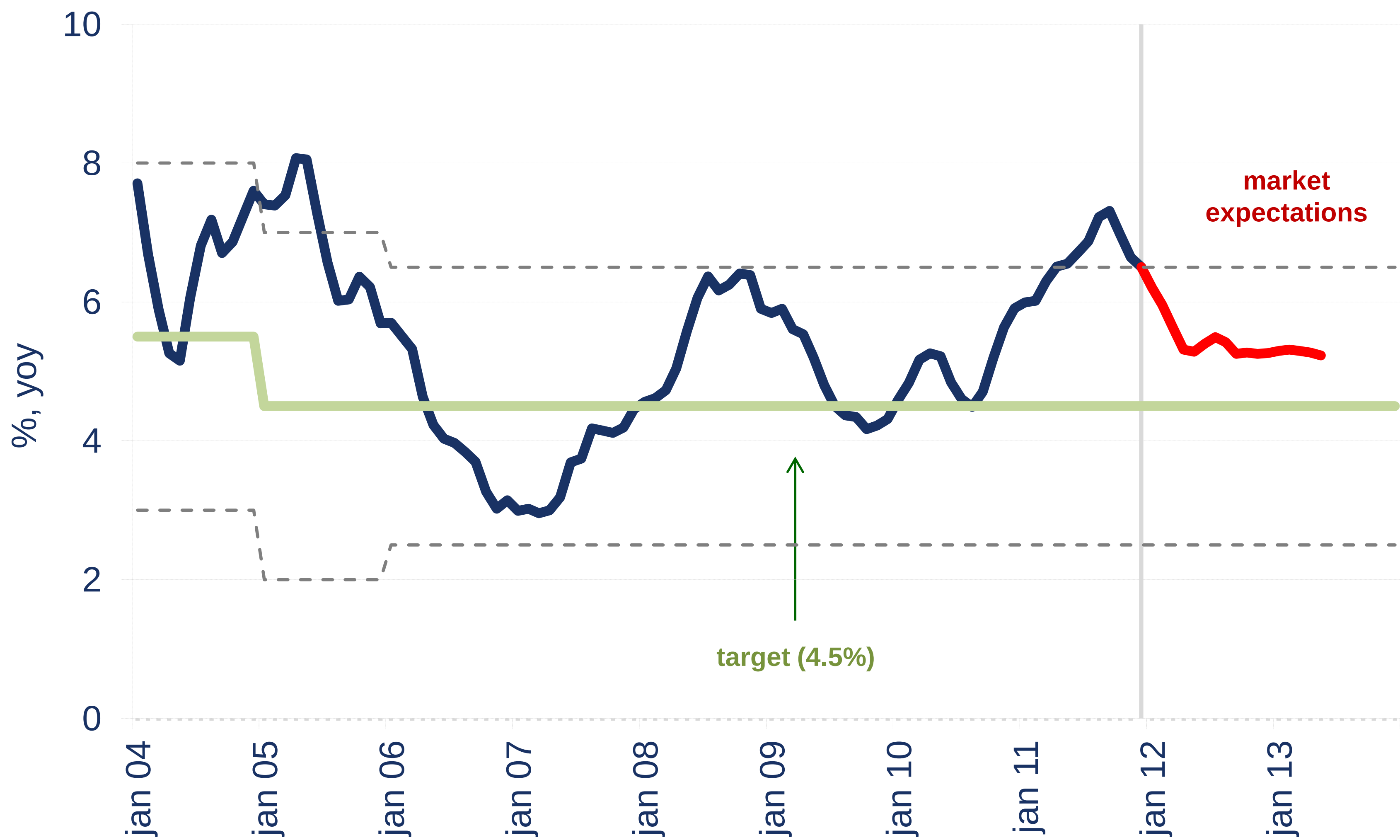
Commodity Price Index



IC-Br: Brazilian Commodity Price Index in BRL; up to Dec 11

Source: BCB

Inflation – Convergence to Target



market expectations: as of Jan 27th, up to Jun 13; target up to Dec 13

Sources: BCB / IBGE

6. Concluding Remarks

Brazil is Well Positioned to Face Global Economic Deterioration

1. A sizeable international reserves as well as large reserves requirement (both higher than in 2008).
2. A proven set of measures/policies that were applied in 2008-09, which can be used.
3. A sound financial system, enjoying a modern market infrastructure that can easily withstand external shocks (rating agencies upgrades in 2011); and
4. Brazil economic activity is presently experiencing a sustainable growth and inflation shows a gradual convergence to target (resulting from enacting global forces and proper policy adjustment).

Thank You