



**BANCO CENTRAL DO BRASIL**

**Apresentação do Diretor de Assuntos Internacionais e Gestão de Riscos Corporativos do Banco Central do Brasil, Tiago Couto Berriel, em evento organizado pela *Brazilian American Chamber of Commerce*, na cidade de Nova Iorque, Estados Unidos.**

**Nova Iorque, 9 de novembro de 2016.**



# ***Outlook for the Brazilian Economy***

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**Tiago Berriel**

Deputy Governor for International Affairs  
and Corporate Risk Management

***Brazilian American Chamber of Commerce***  
New York City

November 9<sup>th</sup> 2016

# Overview

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- 1. Current Context:** Sustained recovery in confidence
- 2. Structural Reform Agenda:** Origin and Progress
- 3. Productivity and growth Agenda:** Logistics and Infrastructure
- 4. Monetary Policy:** Inflation Convergence and its Risks
- 5. Resilience Factors** to withstand transitional risks

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**Current Context:**

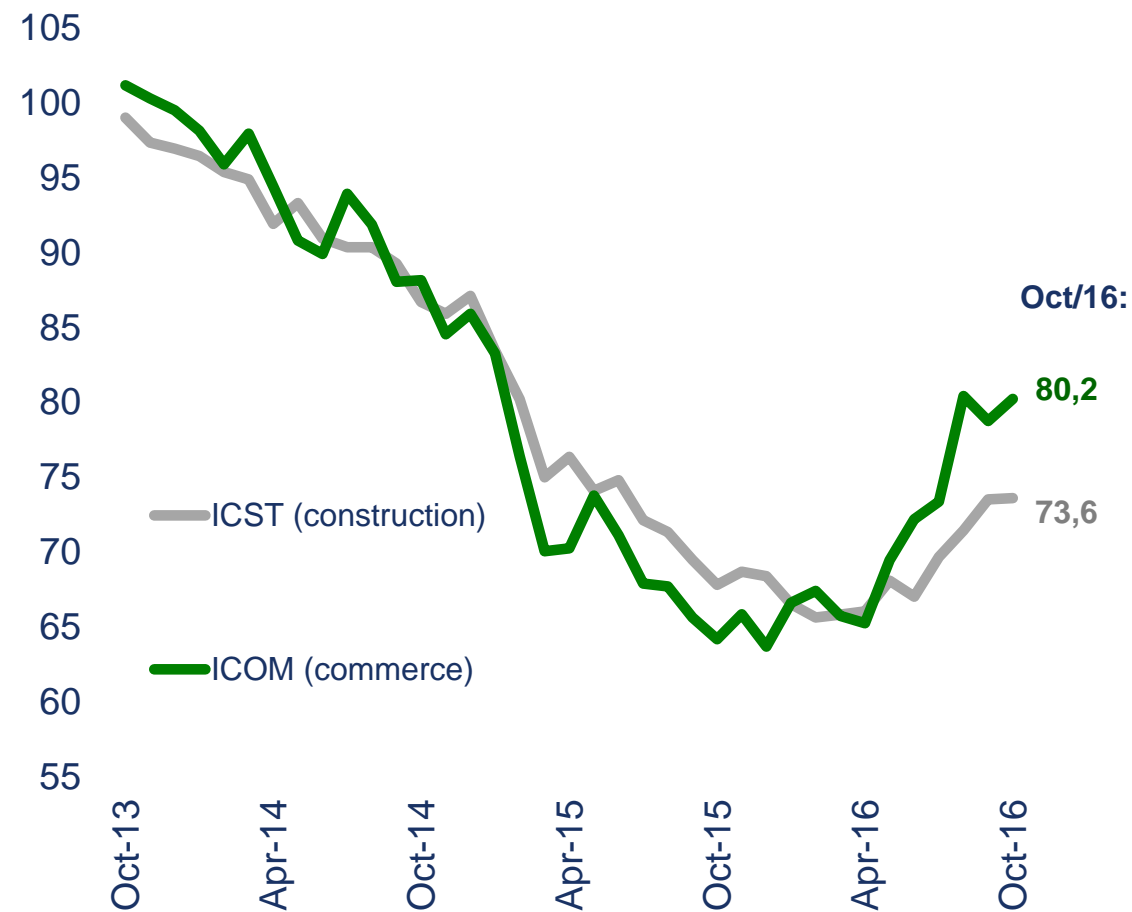
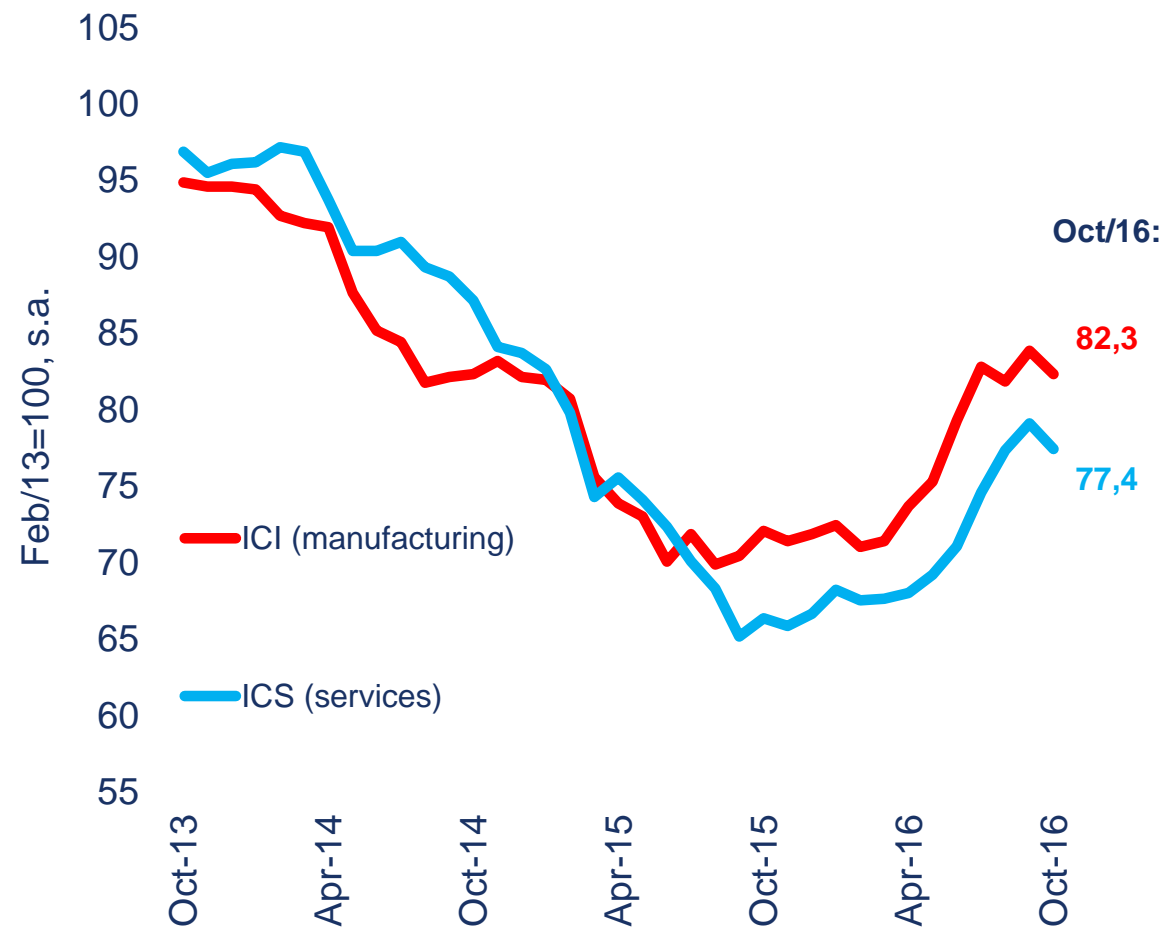
**Sustained recovery in confidence**

# Sustained Recovery in Confidence as Economic Policy Agenda advances

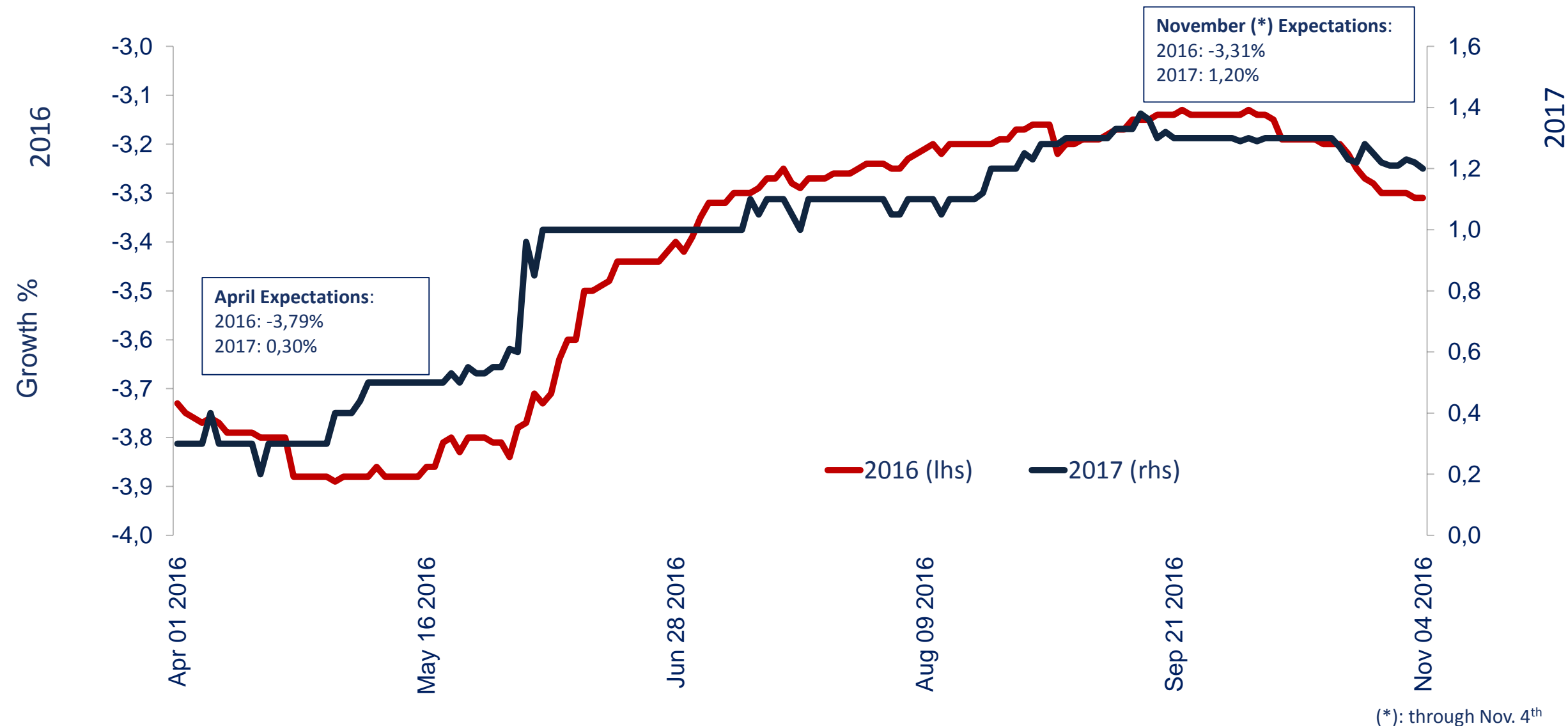
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- Economic activity stabilized and the horizon for recovery is more clear with the reduction of uncertainty and positive expectations for 2016 and 2017.
- Inflation in convergence path and inflation expectations have been re-anchored.
- Advance in fiscal measures' approval in Congress fed back into confidence pick-up, market interest rates have fallen, as risk measures decreased and asset prices rebounded.
- External adjustment is consolidated and the financial system does not present systemic risks, opening room for later support to the recovery.

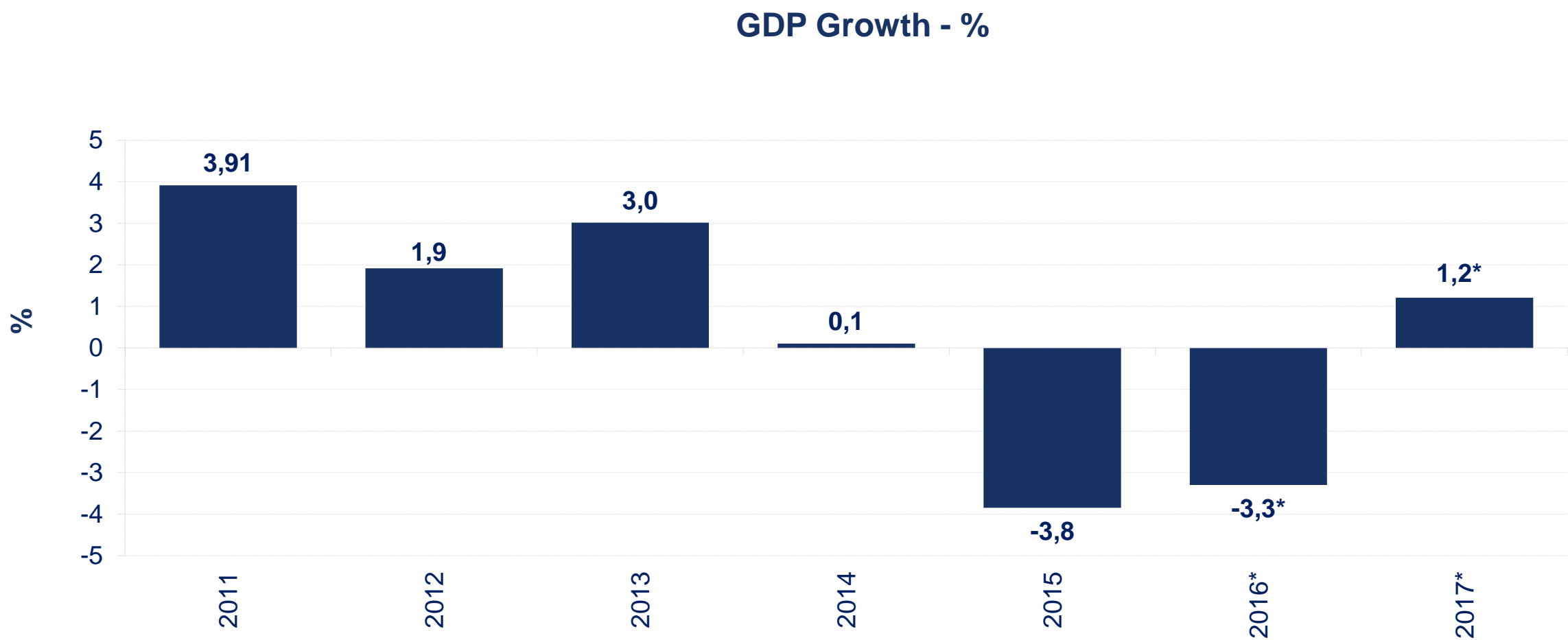
# Regaining Confidence: Businessmen Expectations



# Expectations for 2016/17 Real GDP Growth



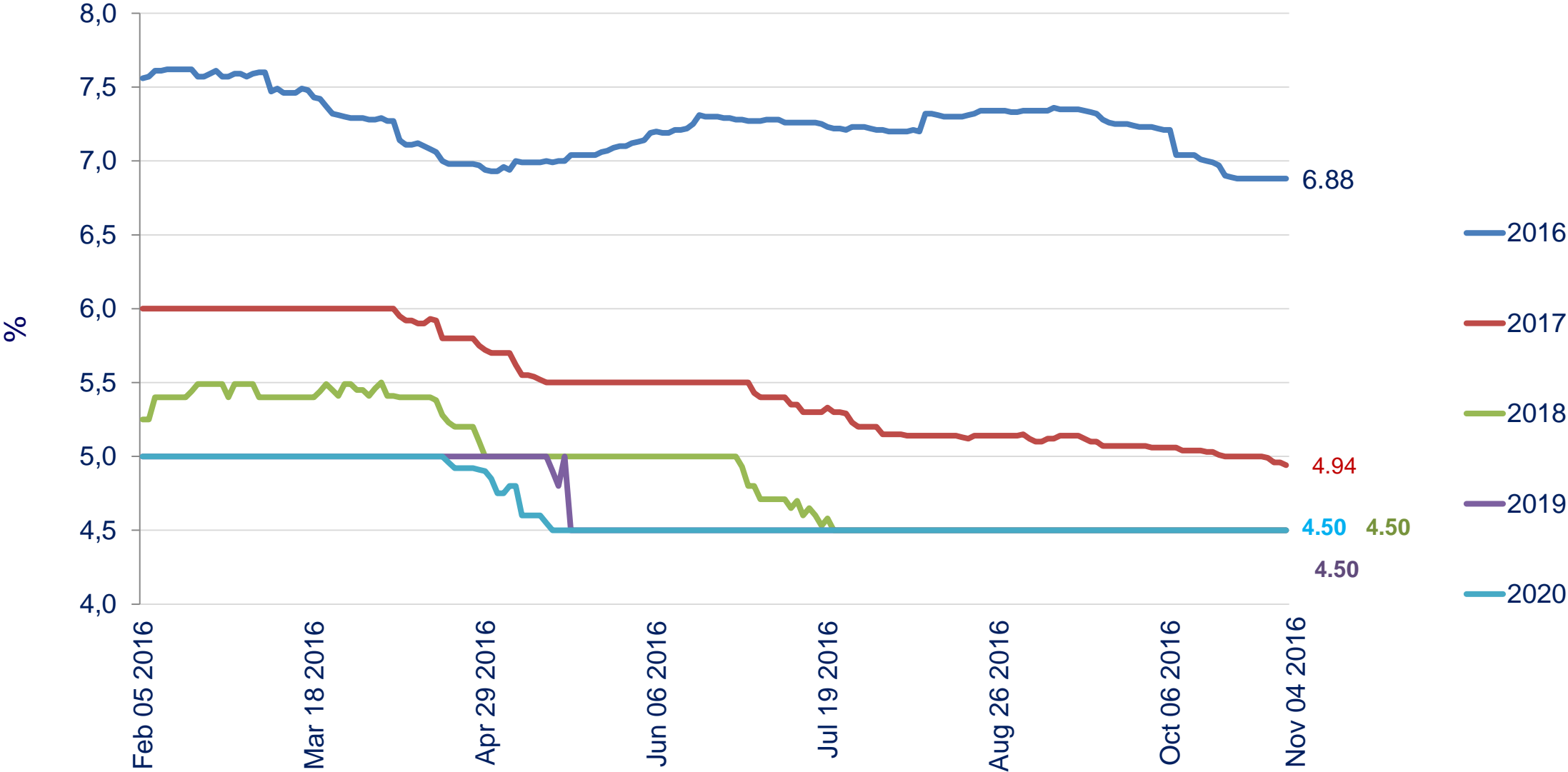
# Economic Activity: stabilization and expected to normalize



\* through Nov. 4th 2016 (Focus Report)

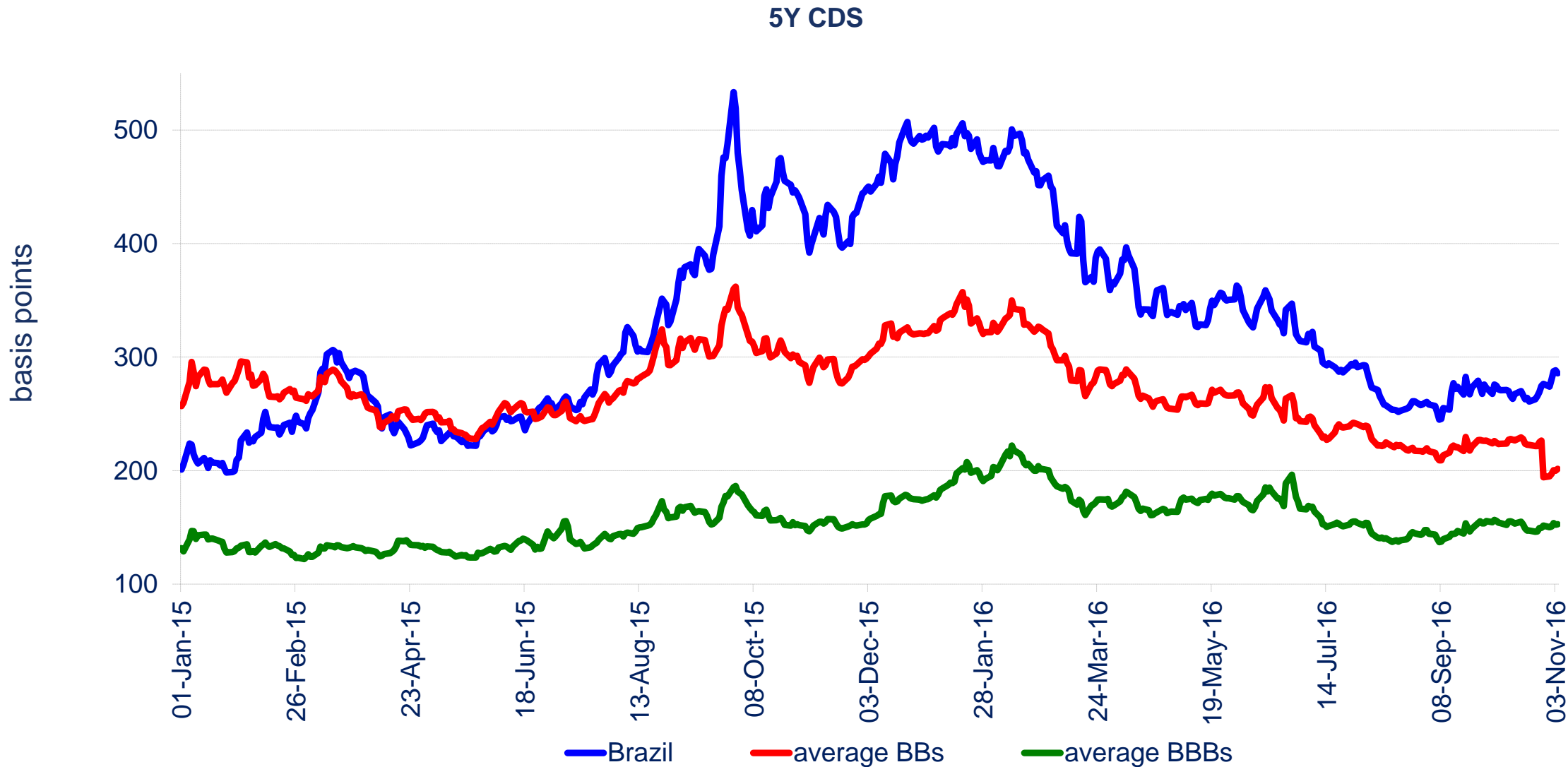


# IPCA Market Expectations are Re-Anchored



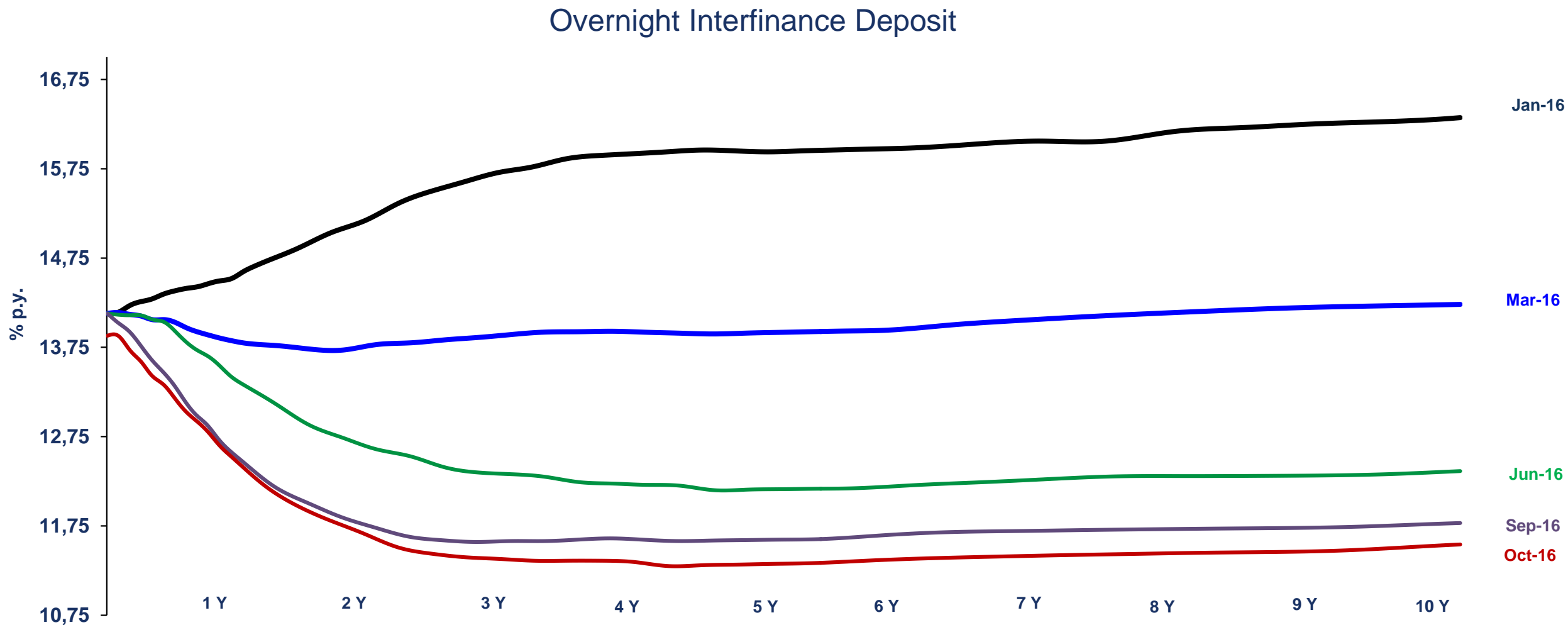
Source: BCB / Focus (through Nov. 4th)

# Regaining Confidence: Risk Premmia: Brazil, BBBs and BBs



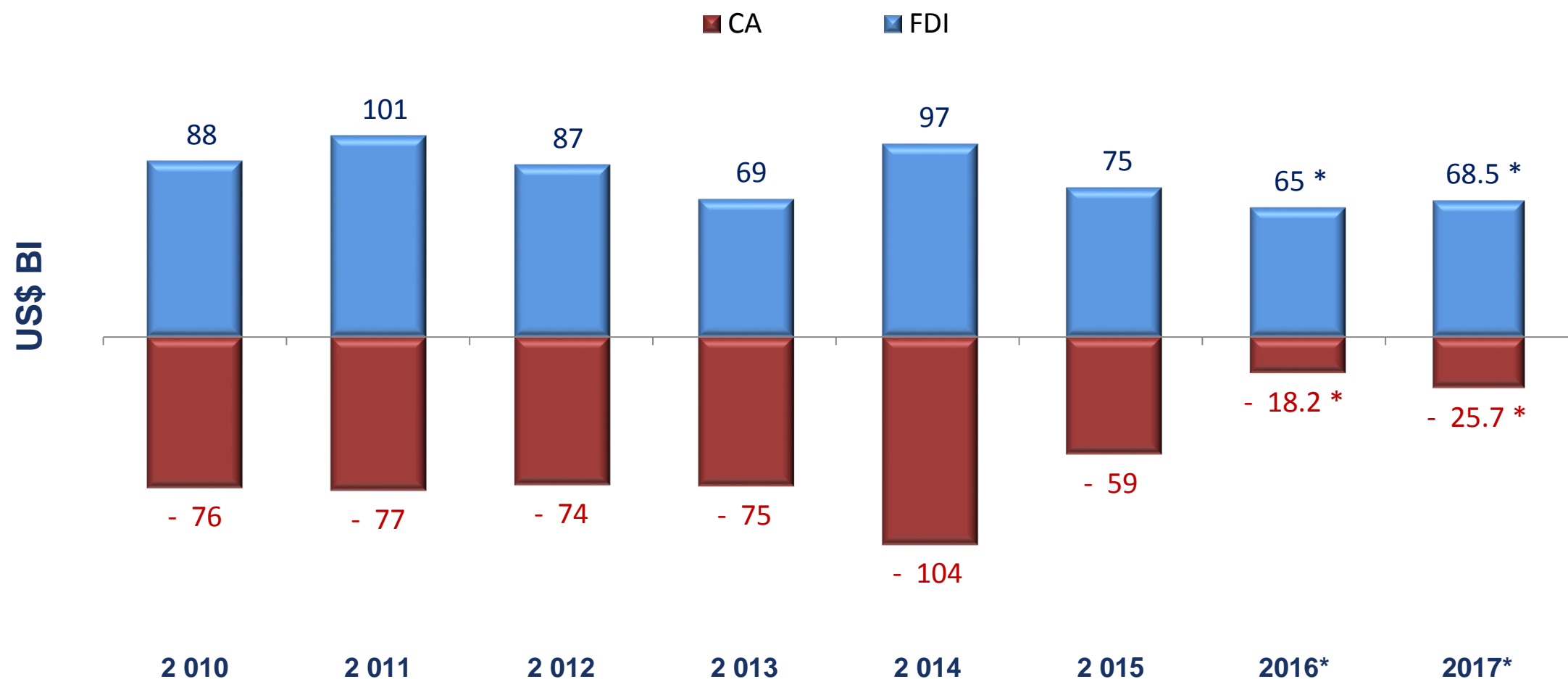
Source: Bloomberg

# Regaining Confidence: Nominal Interest Rating Have Been Falling



Source: BM&FBovespa; BCB.

# External Adjustment: Comfortable Current Account Situation



\* Focus (median of expectations) as of Nov. 4<sup>th</sup>

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# **Structural Reform Agenda:**

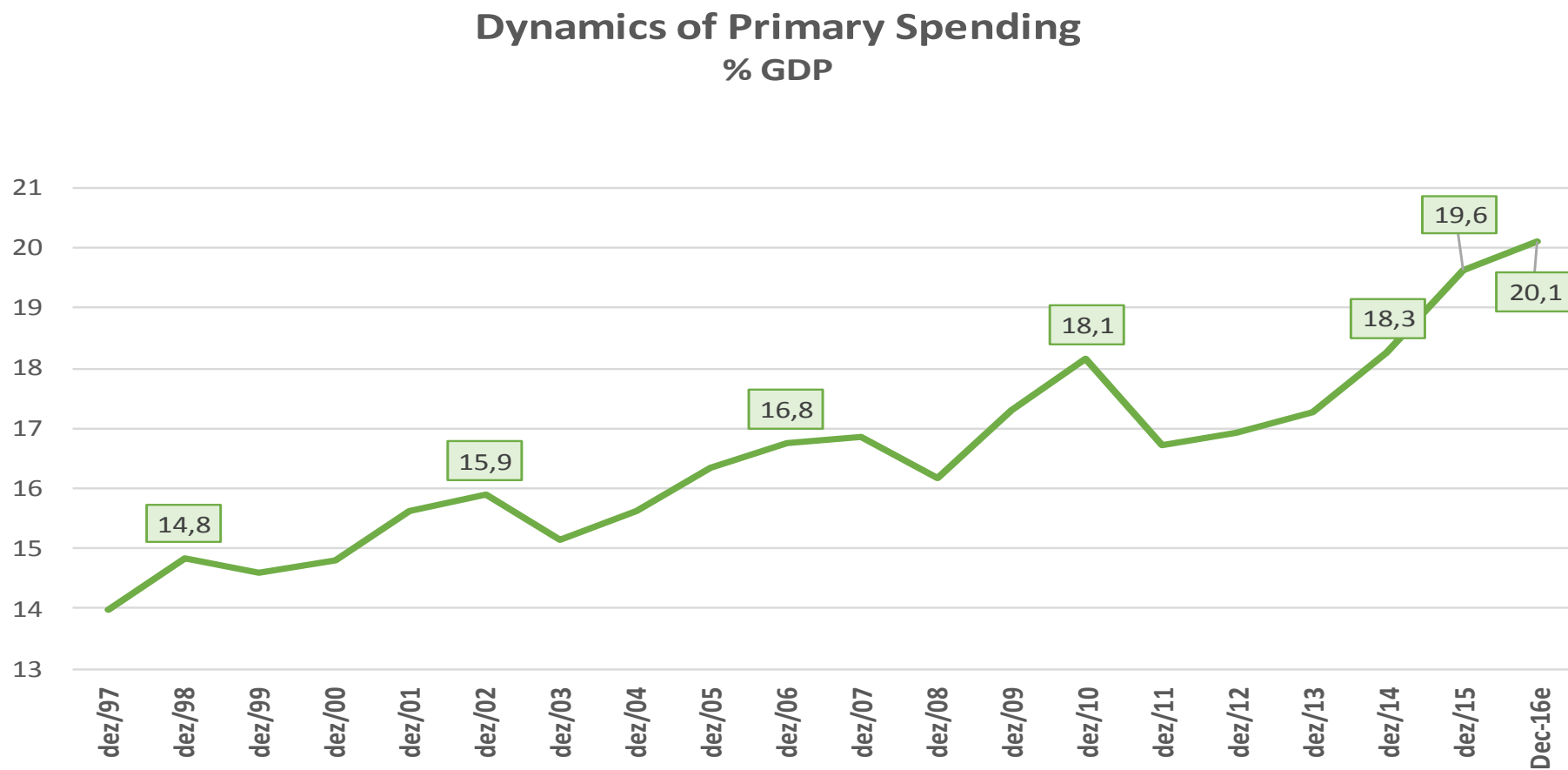
## **Origin and Progress**

# Structural Fiscal Reform Agenda: Origin and Progress

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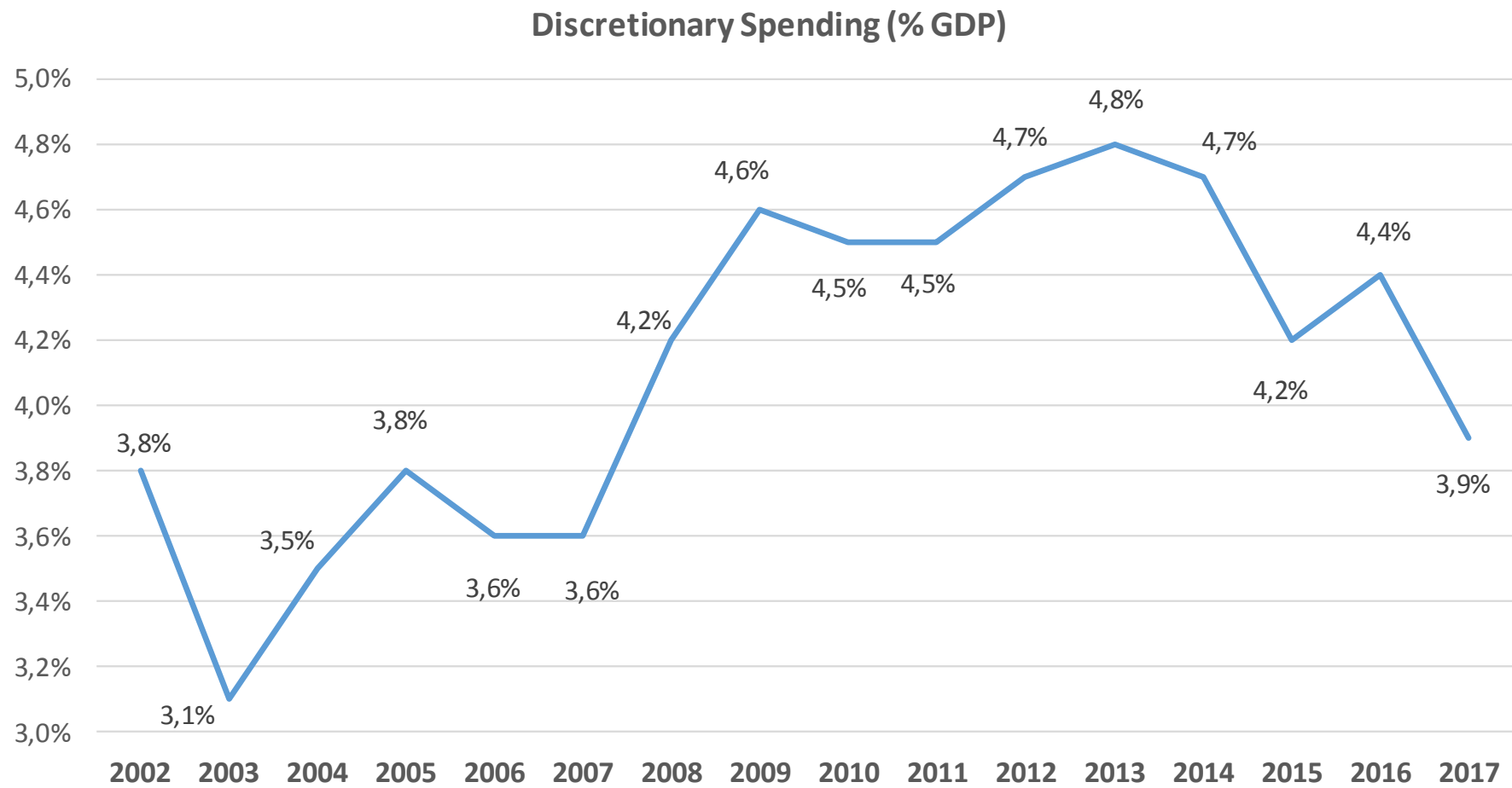
- Persistent growth in expenditures amid structural and cyclical deceleration caused a **fiscal crisis that triggered a confidence crisis**.
- **Structural Fiscal Reform Agenda is critical** to bring fiscal equilibrium back, assuring public debt sustainability and definitively **removing uncertainty for longer horizons**.
- **Spending Ceiling** - *Constitutional Amendment was approved in the Lower House (in 2 rounds) and is expected to be approved in the Senate this year.*
- **Social Security Reform** is on the way.

# Historical Expenditure Dynamics: Persistent Real Growth



**Expenditures have increased significantly in the last 20 years:** The primary spending has a persistent upward trend, while main expenditures have shown a real increase (above inflation) – **overall growth was 12.9% vs 6.6% of annual average inflation**

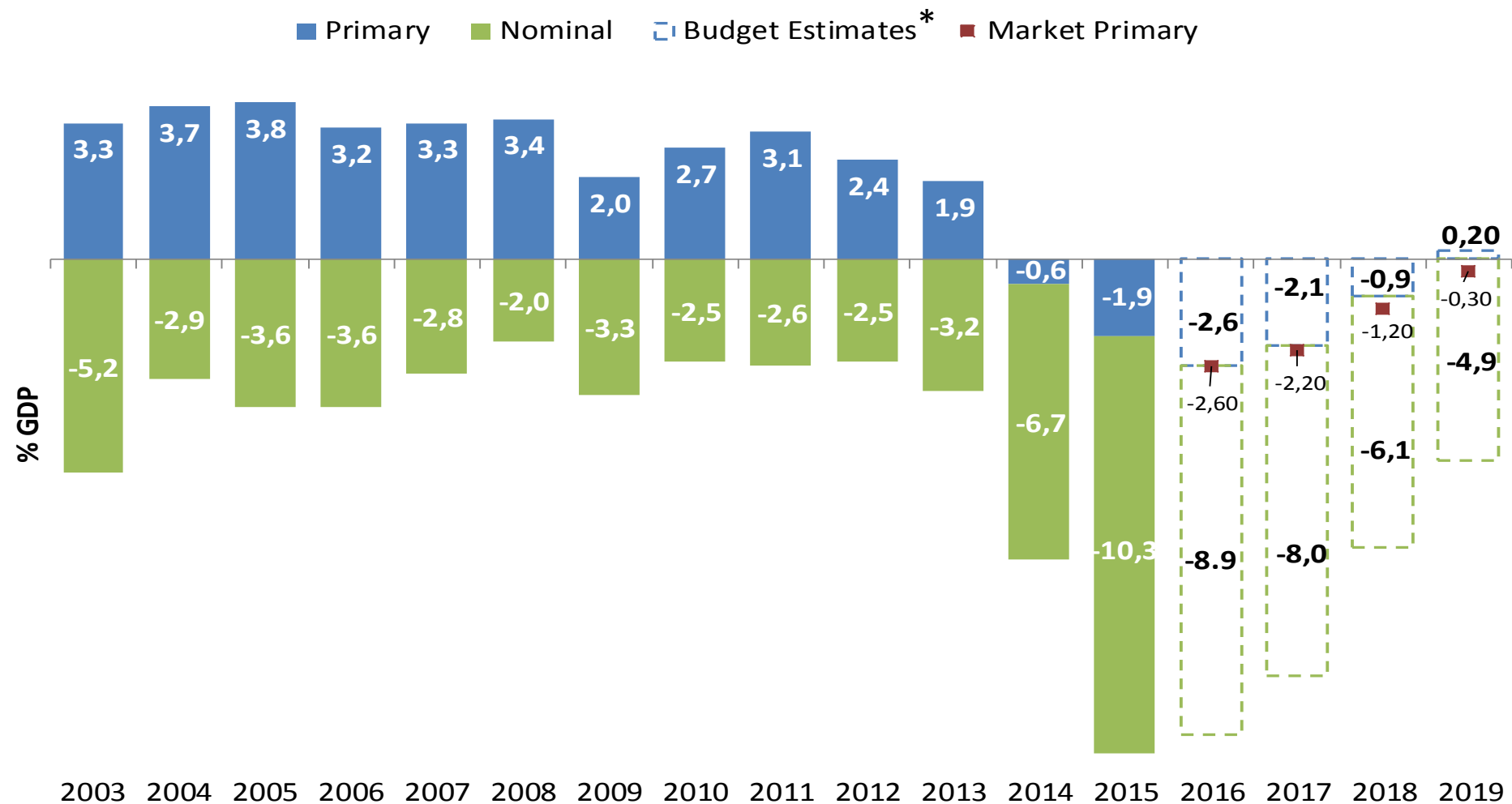
# Structural Reforms are essential: curbing spending is insufficient



**Fiscal Adjustment** cannot rely on cutting discretionary spending it **requires structural reforms** on mandatory spending



# Fiscal Results and Targets: Recovery favors rebuild of Primary Equilibrium



\* The projections are made based in a real GDP growth of -3,0%, 1.2%, 2.5% and 2.5% in 2016, 2017, 2018 and 2019 respectively.

# Structural Fiscal Reforms: Main Initiatives

## 1. Spending Ceiling – Constitutional Amendment approved in Lower House (now submitted to Senate)

- 2007-2015: net revenues decreased from 19.0% to 17.7% GDP, while primary spending increased from 16,9% to 19.6 % GDP (in the Federal Gov't level)
- 2008-2015: revenues decreased 7.8%, while spending grew 51% in real terms
- Curbing discretionary spending is insufficient

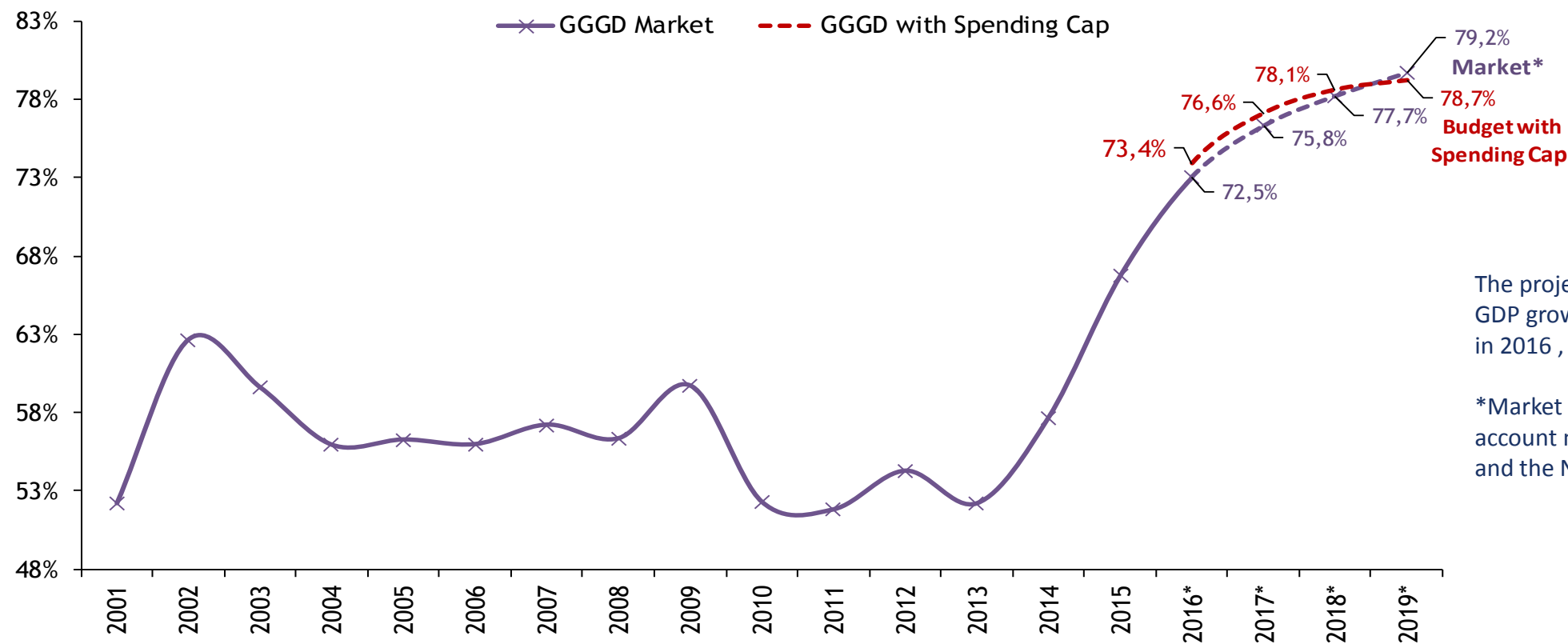
## 2. Social Security Reform is a Priority

- Increase minimum retirement age
- Shrink the gap between gender and public vs private sector workers

## 3. Broad Review in Government Expenditure

# Debt Dynamics: Stabilization after Spending Cap

## General Government Gross Debt



The projections are made based in a real GDP growth of -3.1%, 1.2%, 2.5% and 2.5% in 2016 , 2017, 2018 and 2019, respectively.

\*Market projection (FOCUS) takes into account market macroeconomic parameters and the National Treasury’s model.

- » A significant part of the GG Gross Debt responds to:
- 1. Loans to Public Banks → This policy has been reversed as of Jan-2015 → which represents 9.6% GDP
  - 2. REPO Operations → Collateral for sterilization → Increase in FX-reserves → which represents 20.8% GDP

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# **Productivity and growth Agenda:**

## **Logistics and Infrastructure**

# Growth Oriented Agenda

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- Asset Sales and Privatization Agenda
- Improving Business Environment
- Concessions to the Private Sector: Logistics Investment Program (PIL) and Infrastructure Works with regulatory stability

# Focus on Addressing Constraints to Productivity and Growth

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## Asset Sales and Privatization Agenda

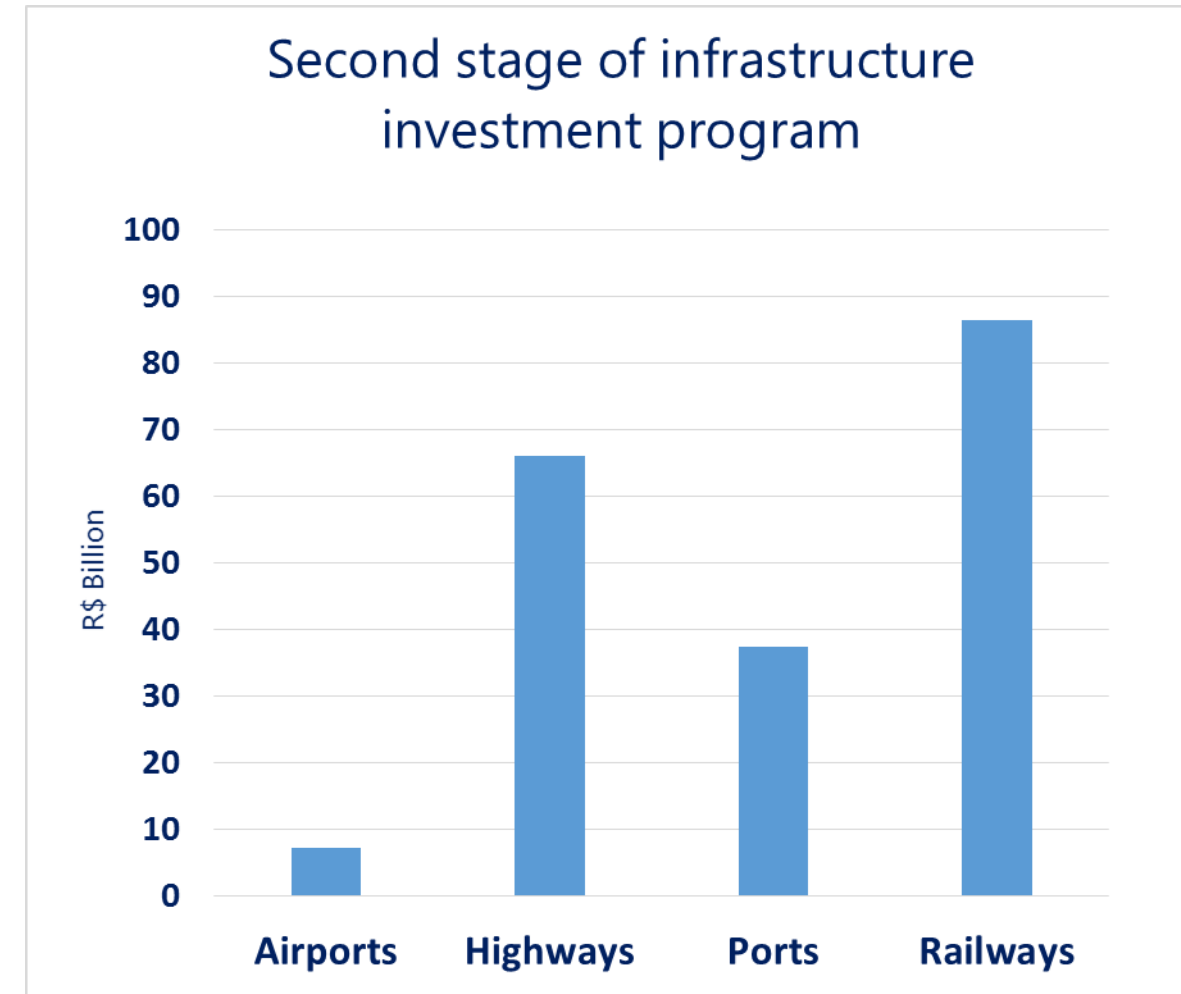
- Encompasses Federal and Local Gov't

## Improving Business Environment

- Tax reform
- Reinforce regulatory framework
- Diminishing red tape constraints
- Increasing productivity

# Logistics Investment Program (PIL)

- Brazil launched the second stage of infrastructure investment program: estimated investment of about R\$200 billion.
- Regulatory stability



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# Monetary Policy:

## Inflation Convergence and its Risks



# Central Bank continues monitoring inflation convergence (I)

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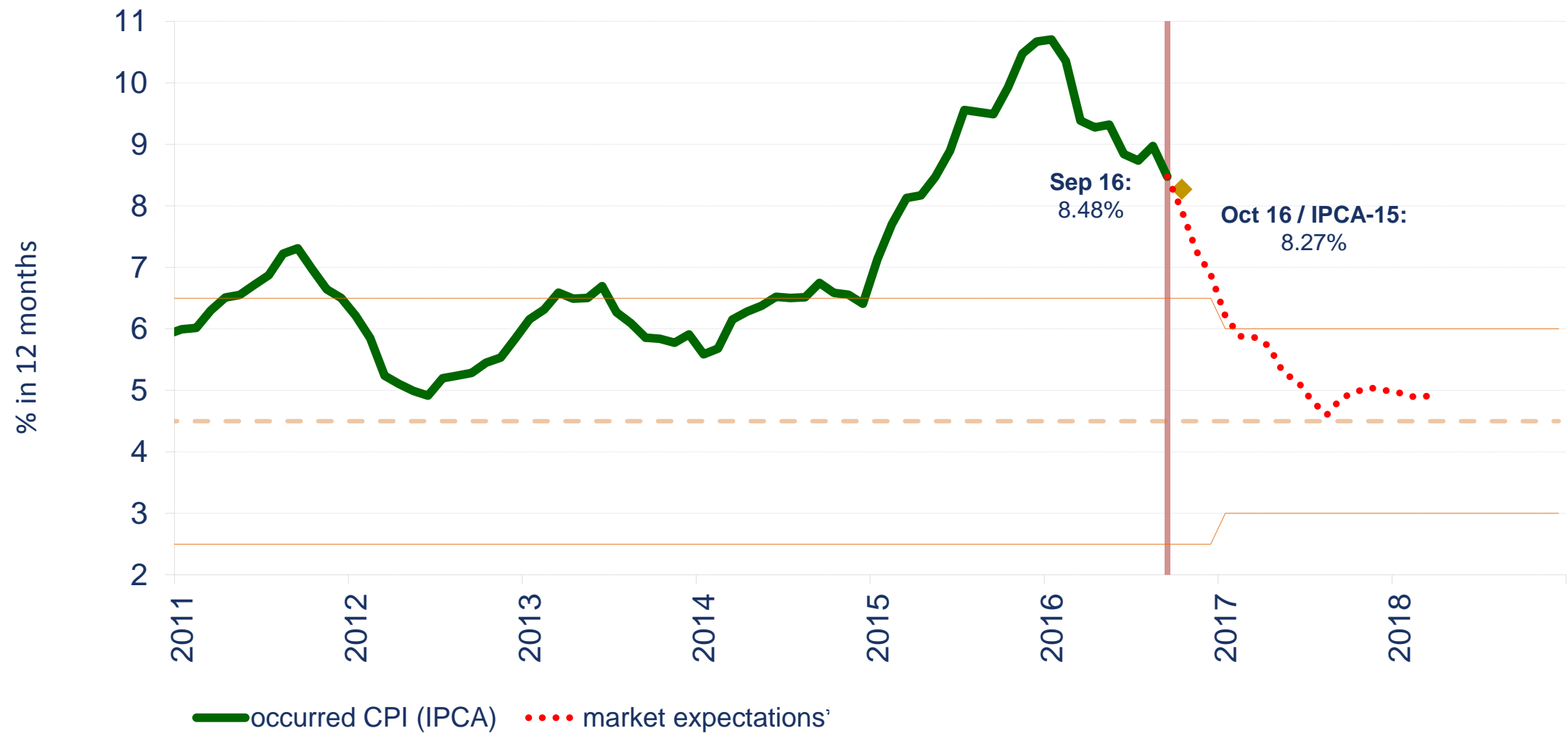
- Clear Progress in approving structural fiscal reforms and inflation expectations closer to the target for 2017.
- Food component shock is fading and its secondary effects are small.
- The progress of fiscal reforms and the evolution of inflation measures sensitiveness to monetary policy and the business cycle are key factors to assure inflation convergence at appropriate pace.
- Assessment about actual inflation and expected inflation convergence (as well as the factors above) will define pace and magnitude of potential monetary policy accommodation.

# Central Bank continues monitoring inflation convergence (II)

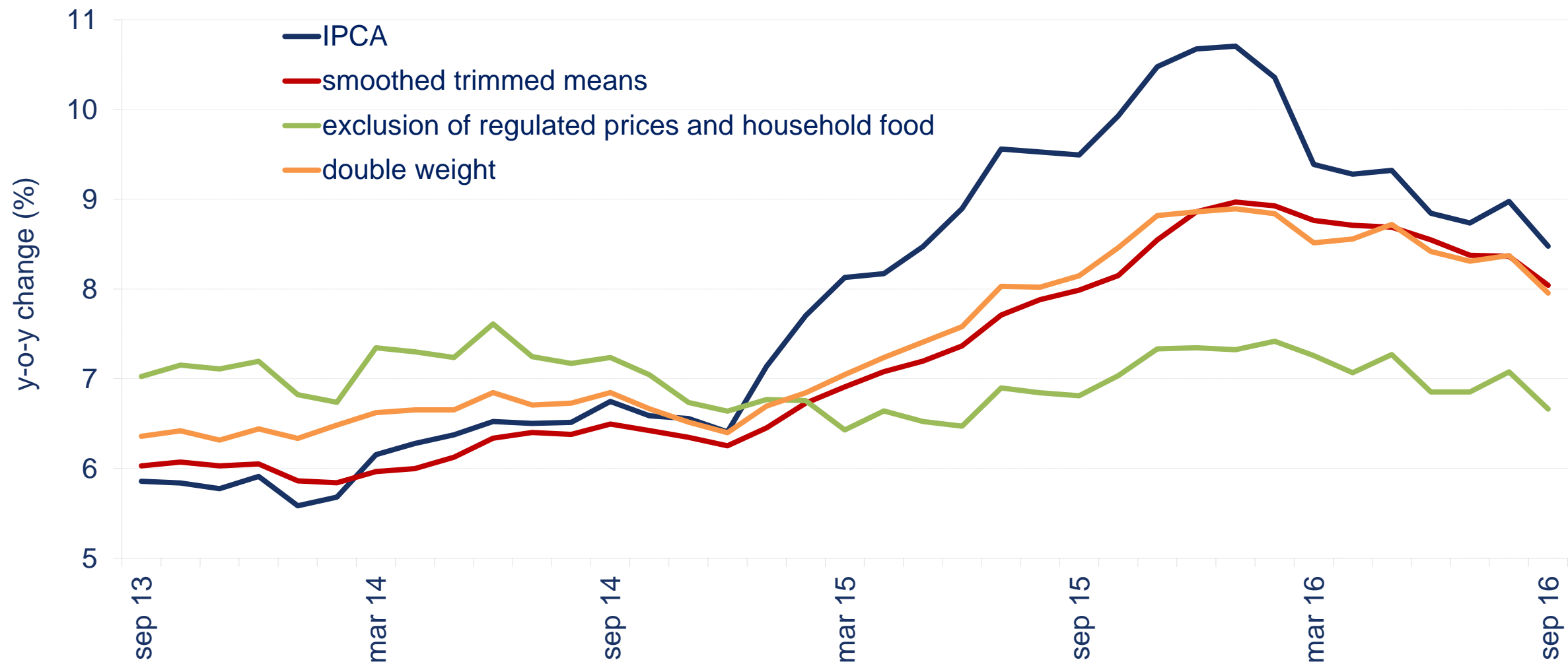
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- Inflation components sensitiveness to monetary policy and the economic cycle have been declining but there seems to be a pause recently.
- Inflation persistence may be higher depending on the sensitivity of different CPI components (particularly services and non tradable prices) to monetary policy and output gap.

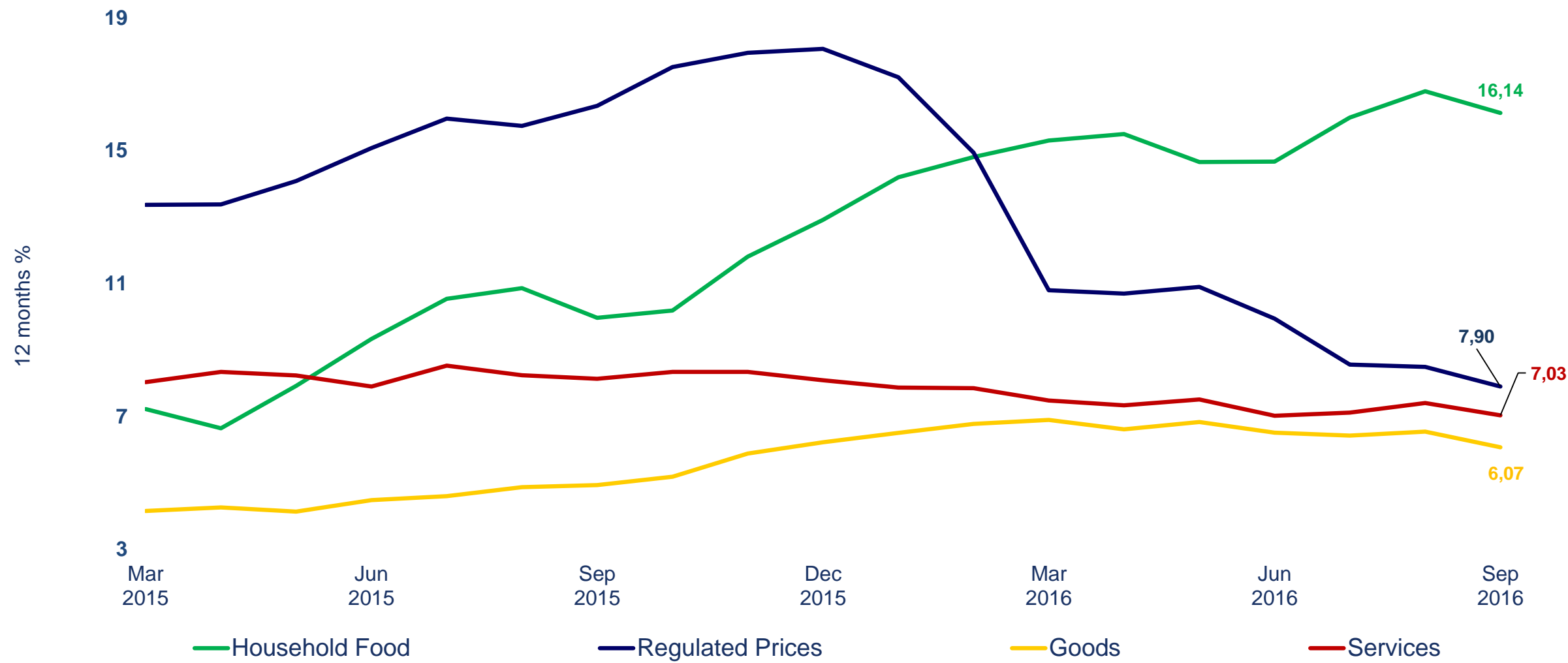
# CPI (IPCA) Market Expectations converging to the Target



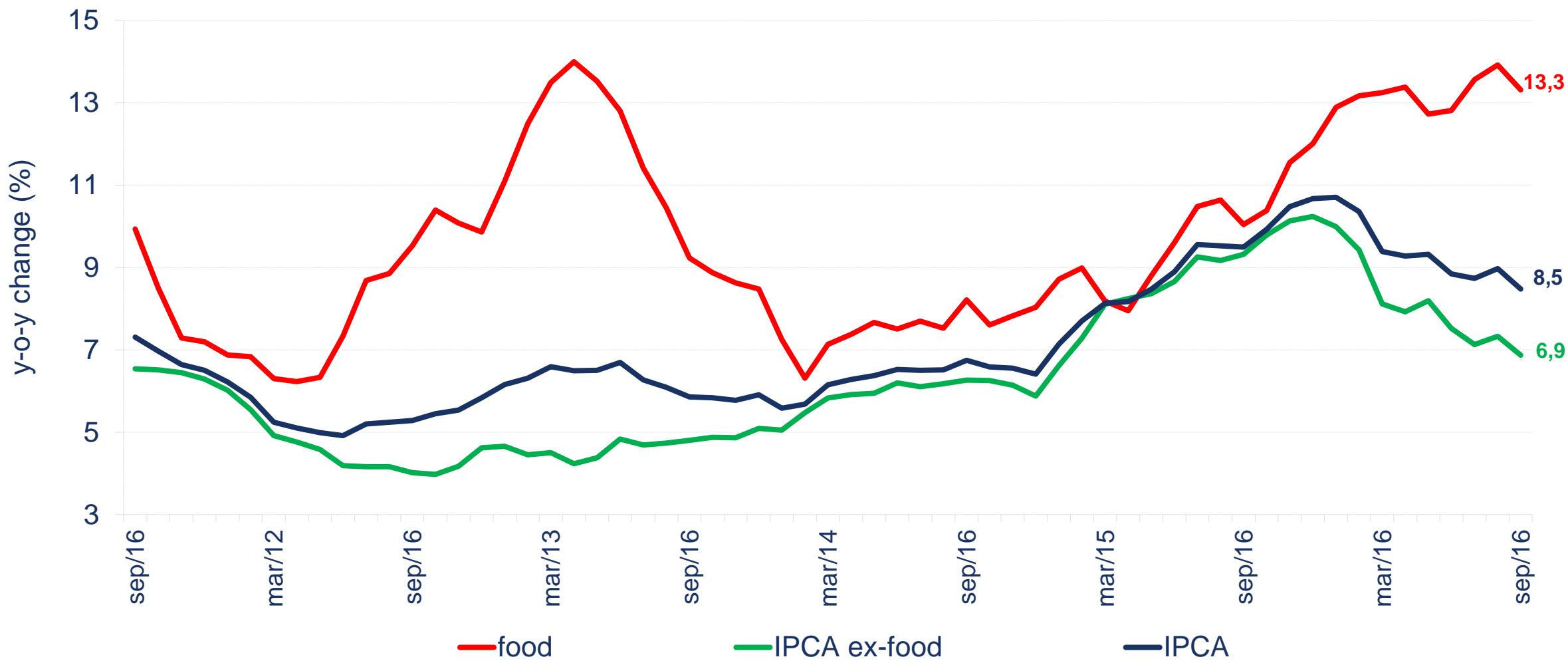
# Inflation Convergence: CPI (IPCA) Headline and Core Measures



# CPI (IPCA) Segments – Short Term Path

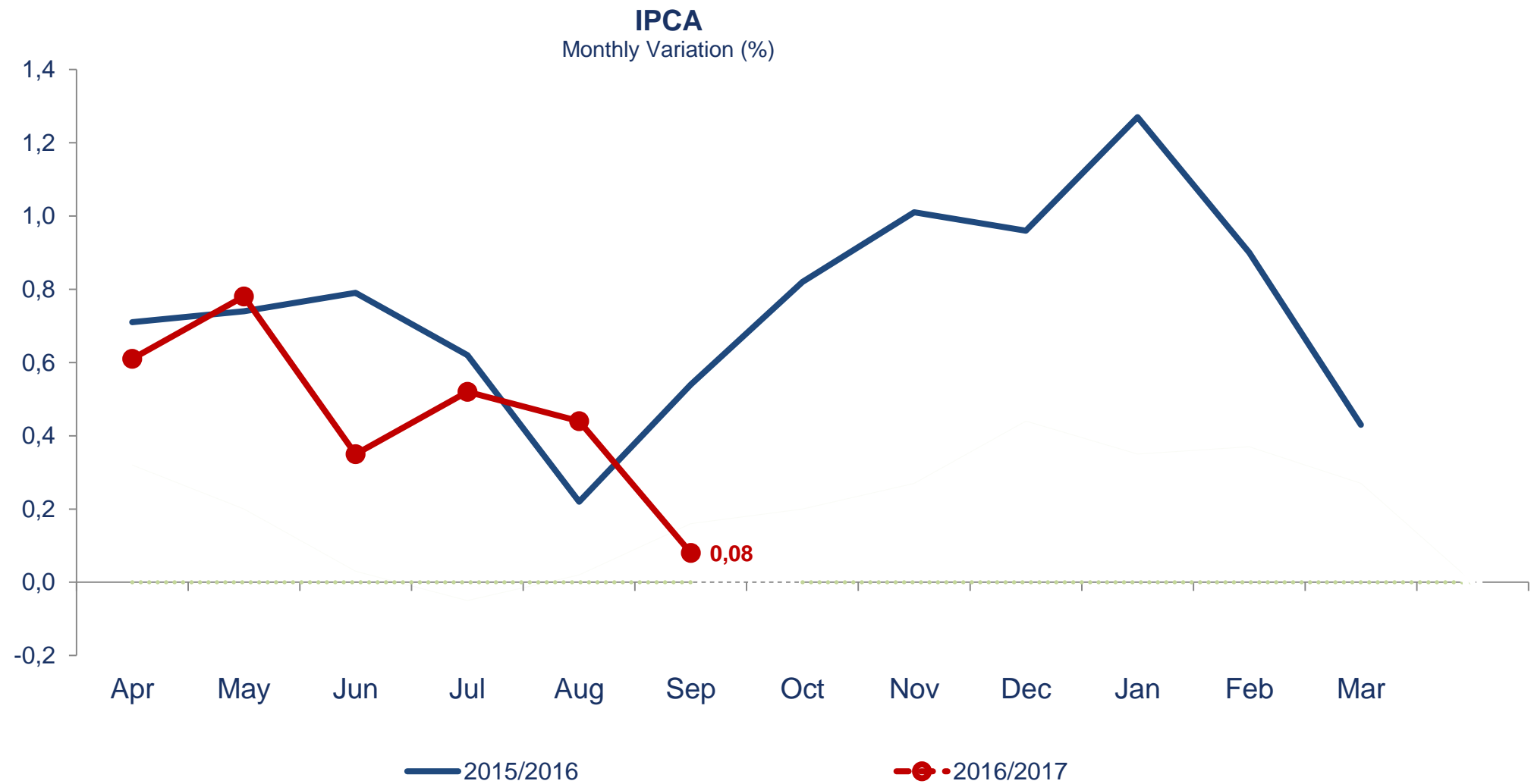


# Inflation Convergence: Headline CPI (IPCA) and Food(\*) Prices



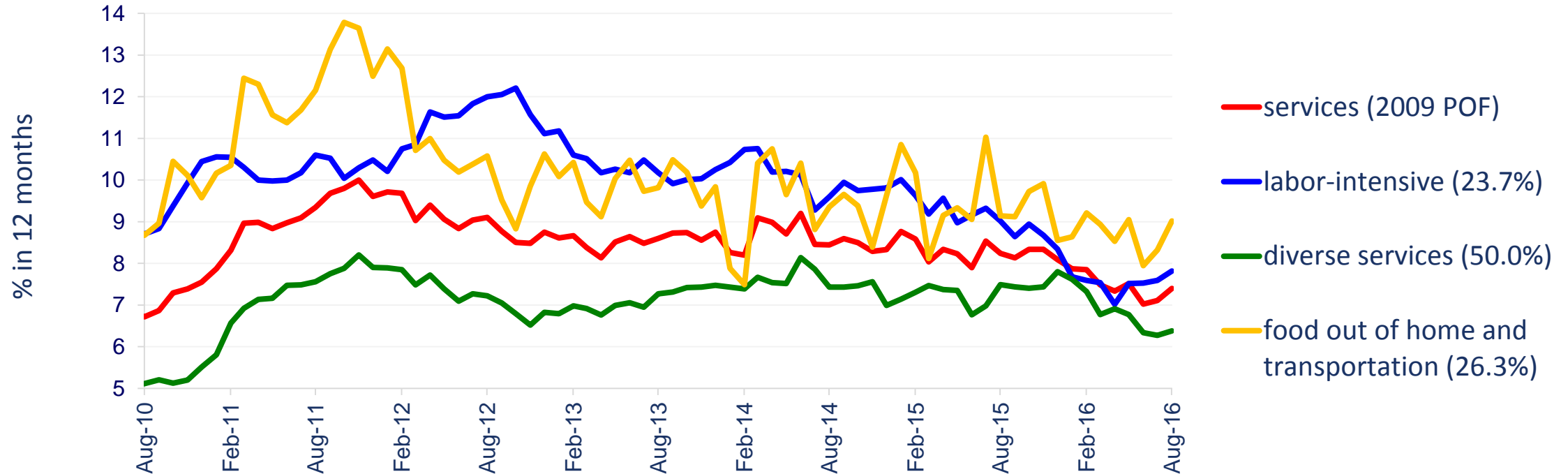
(\*): Food weight: 26.1%

# Monthly Path for CPI (IPCA): Contrasting Results 2015 vs 2016



# Assessment of Services Prices as an Inflation (IPCA) Component

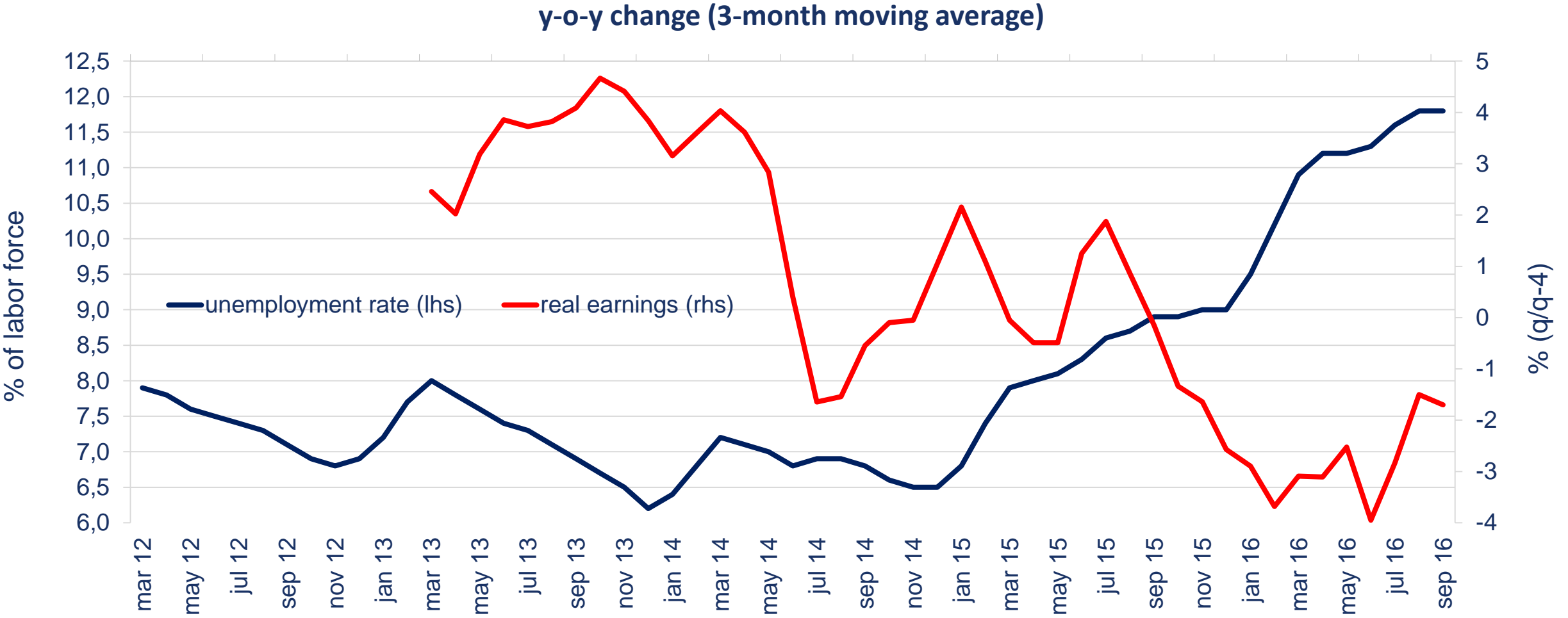
- Evaluates the disinflation process in the services sector through several available measures
- Some measures present faster disinflation than the average services prices in the IPCA



- Uncertainties whether the recent deceleration observed in some services prices represents disinflation that should disseminate

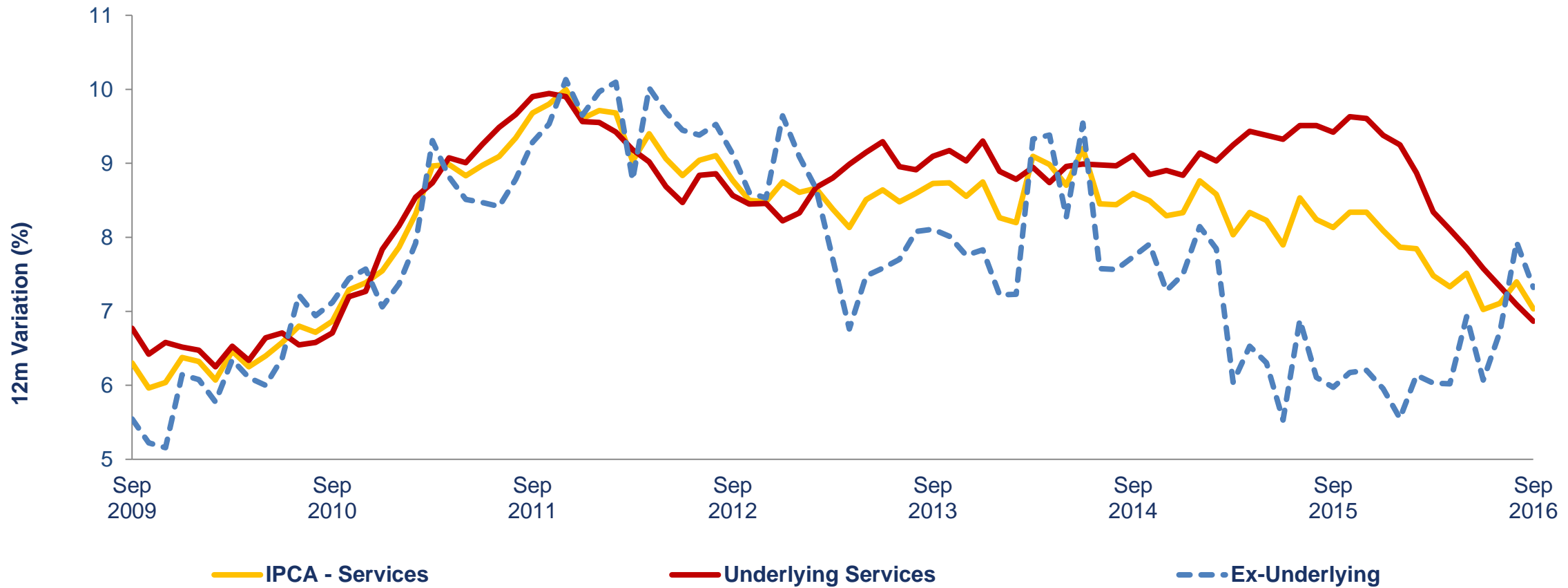


# Unemployment and Real Earnings(\*)



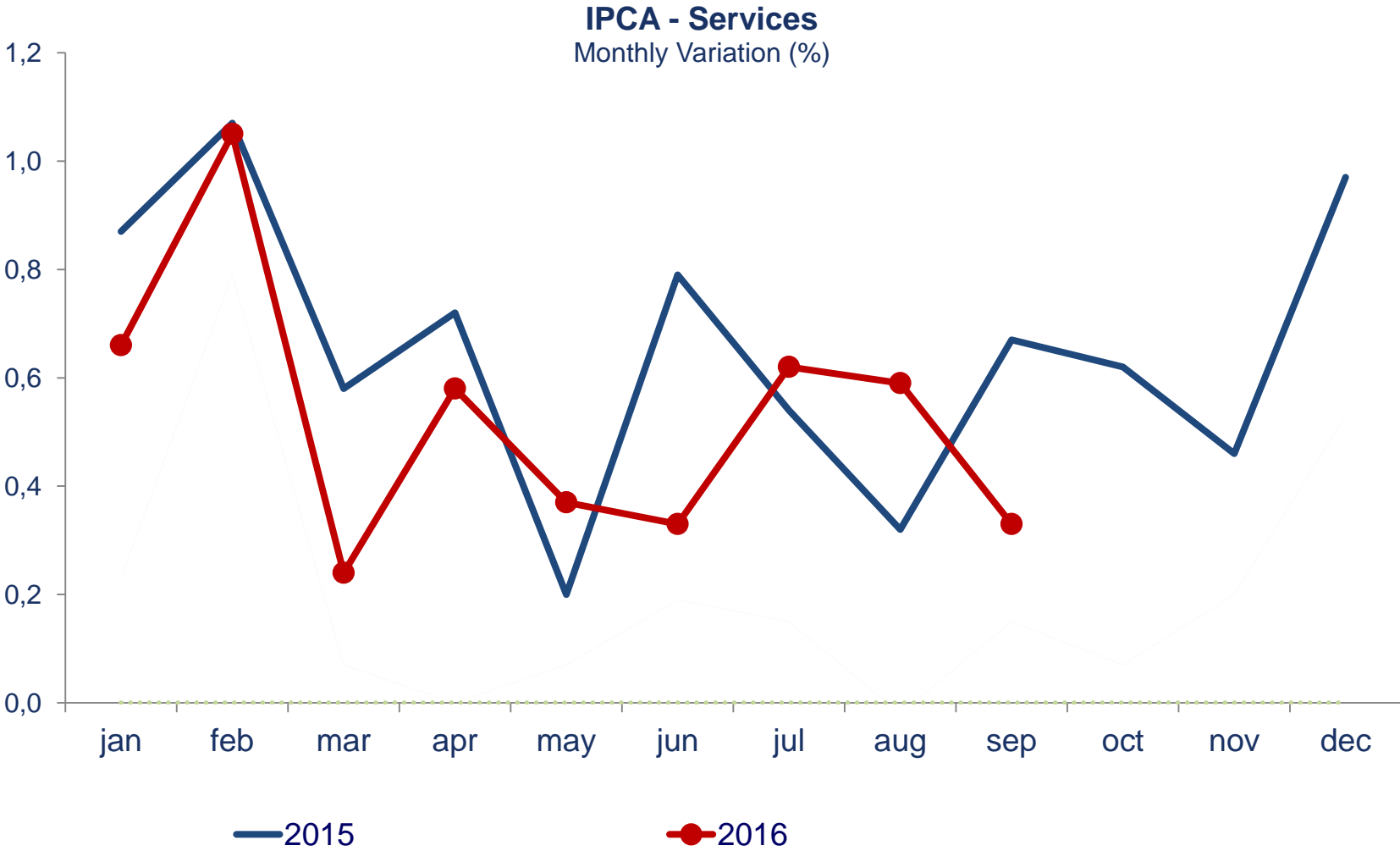
(\*): Real Earnings: last month of the quarterly moving average

# Services Prices Components: Overall, Underlying(\*) and Ex-Underlying

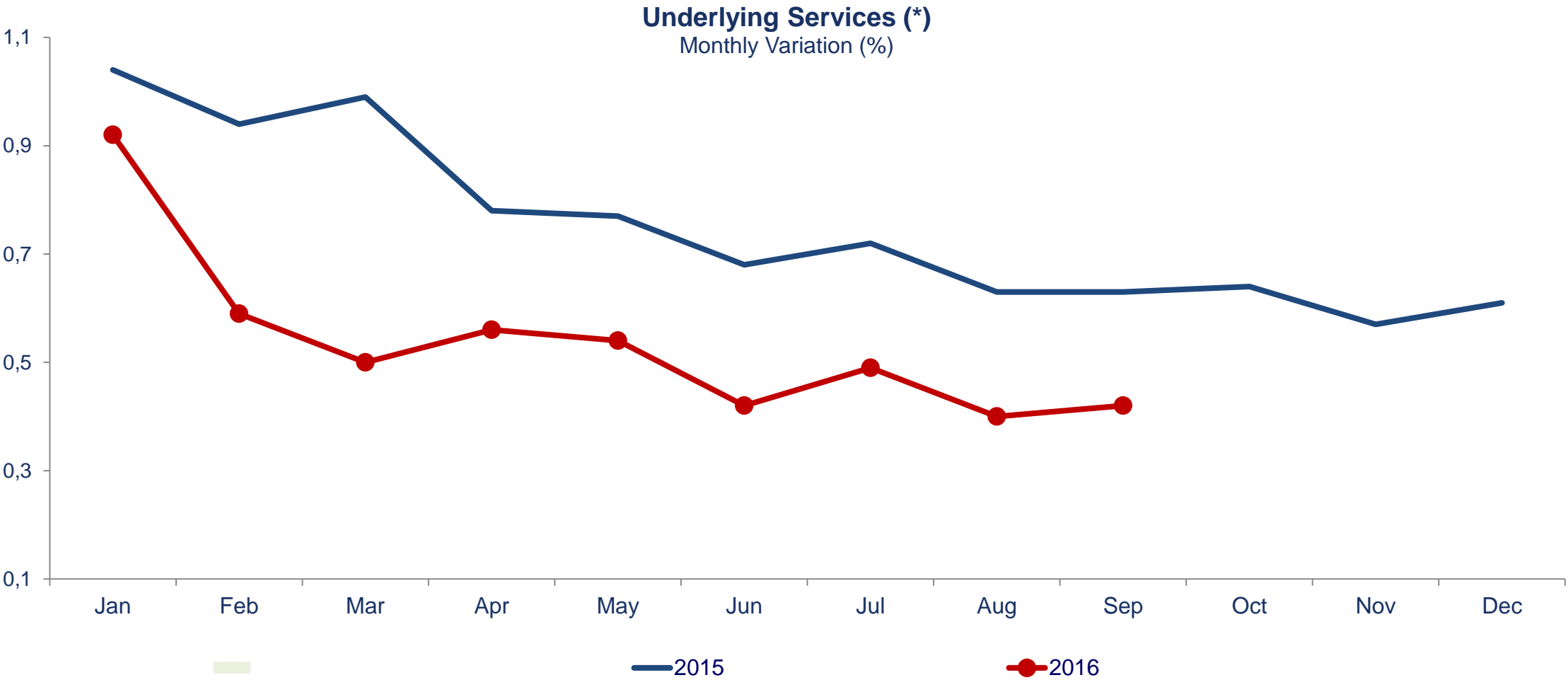


(\*): Domestic services, courses, communication and tourism

# CPI Overall Services Component: Contrasting Results 2015 vs 2016

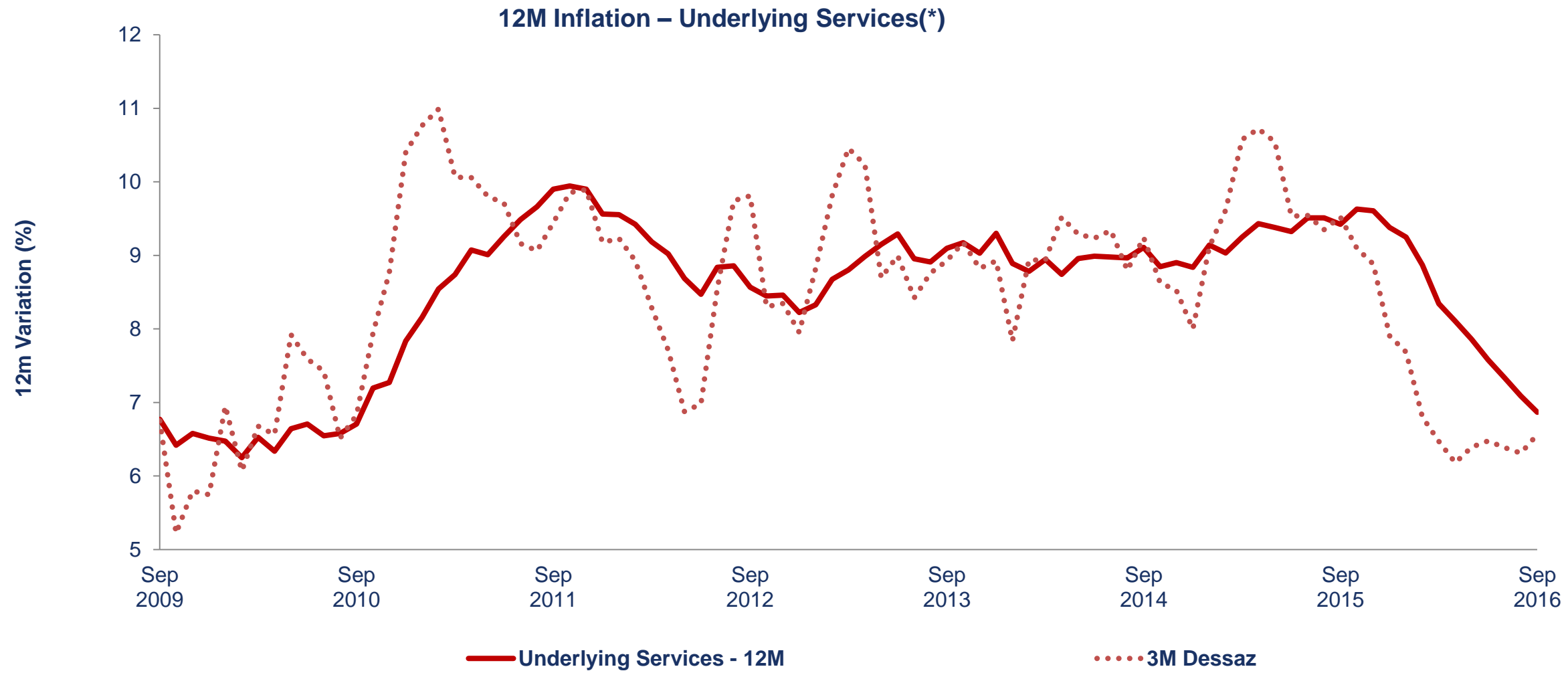


# Services Prices: Underlying Component (\*) - results 2016 vs 2015



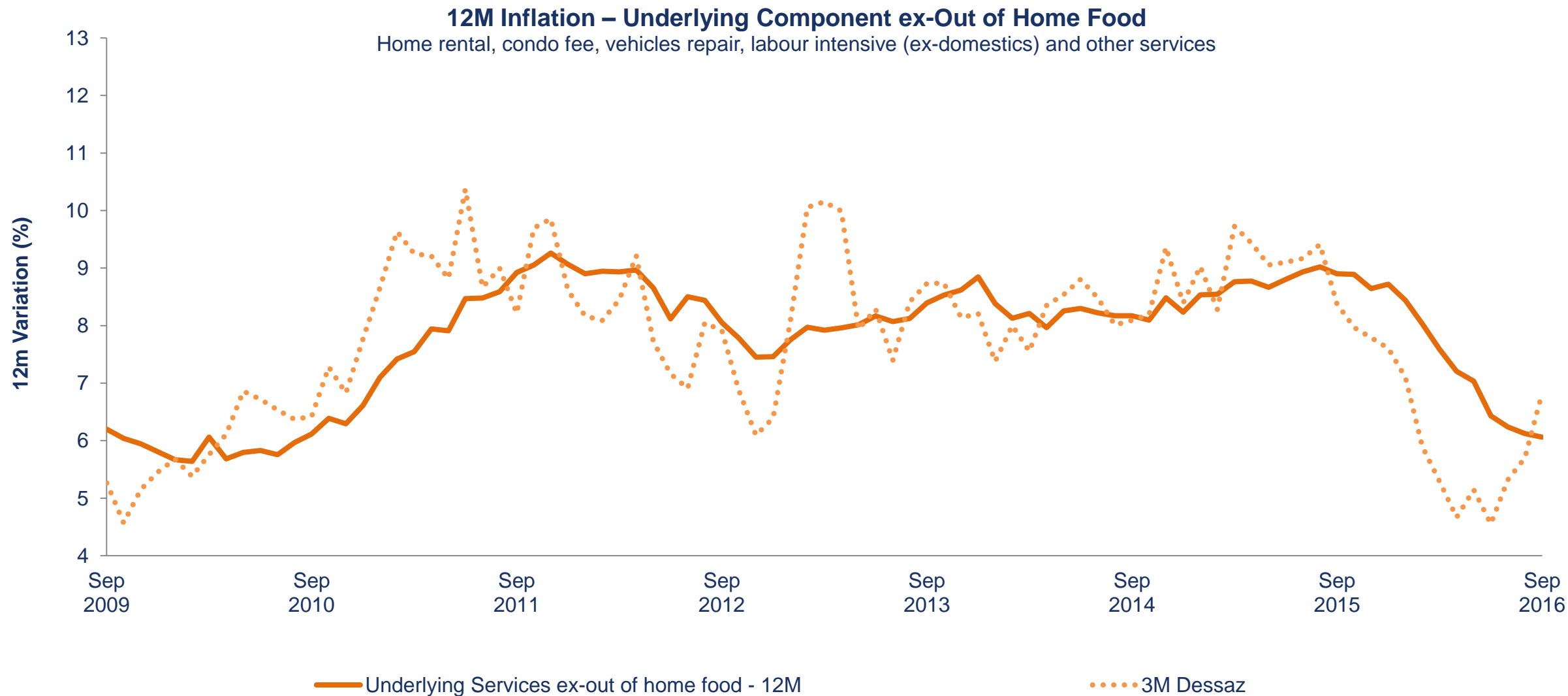
(\*): Overall services excluding domestic services, courses, communication and tourism

# Services Prices Path (CPI-IPCA): Underlying Component (moving average)

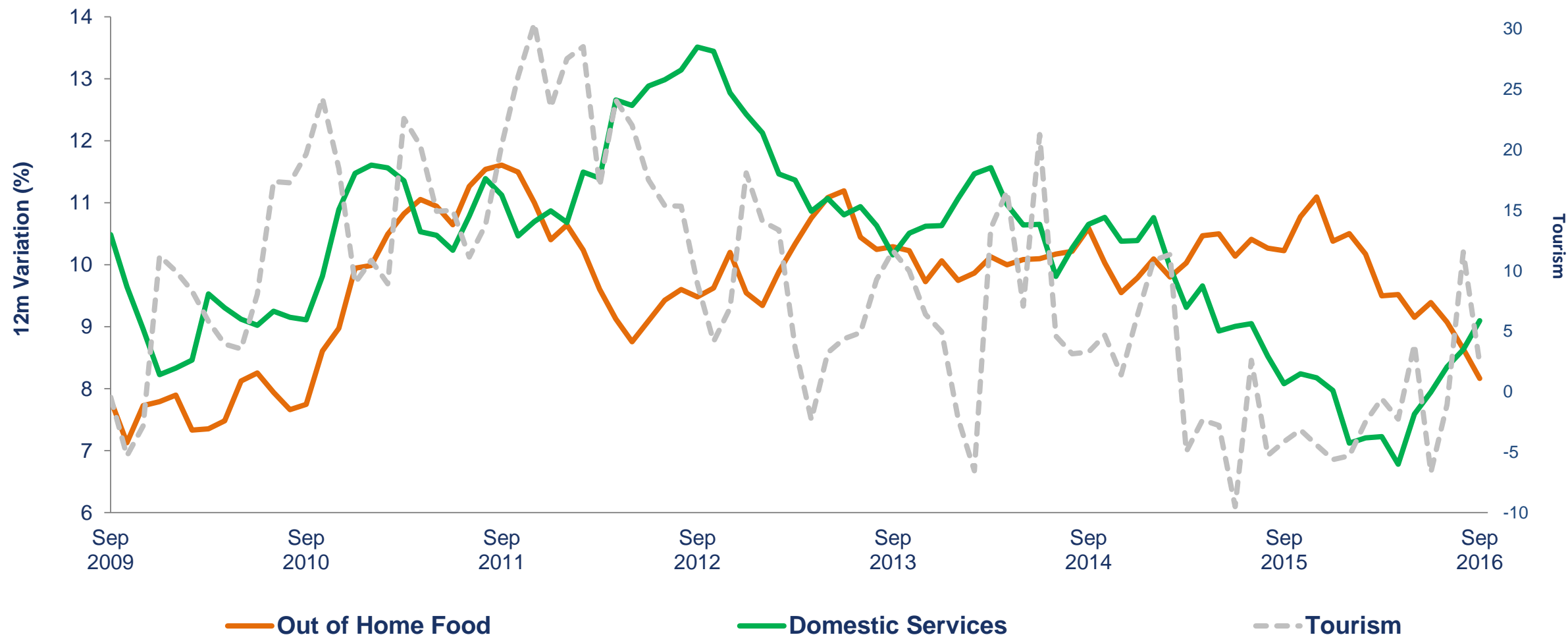


(\*): Overall services excluding domestic services, courses, communication and tourism

# Services Prices Underlying Comp ex-Out of home food – moving average



# Services Prices Decomposition (CPI-IPCA): Selected Components



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# **Resilience Factors:**

## **Financial System and External Accounts**

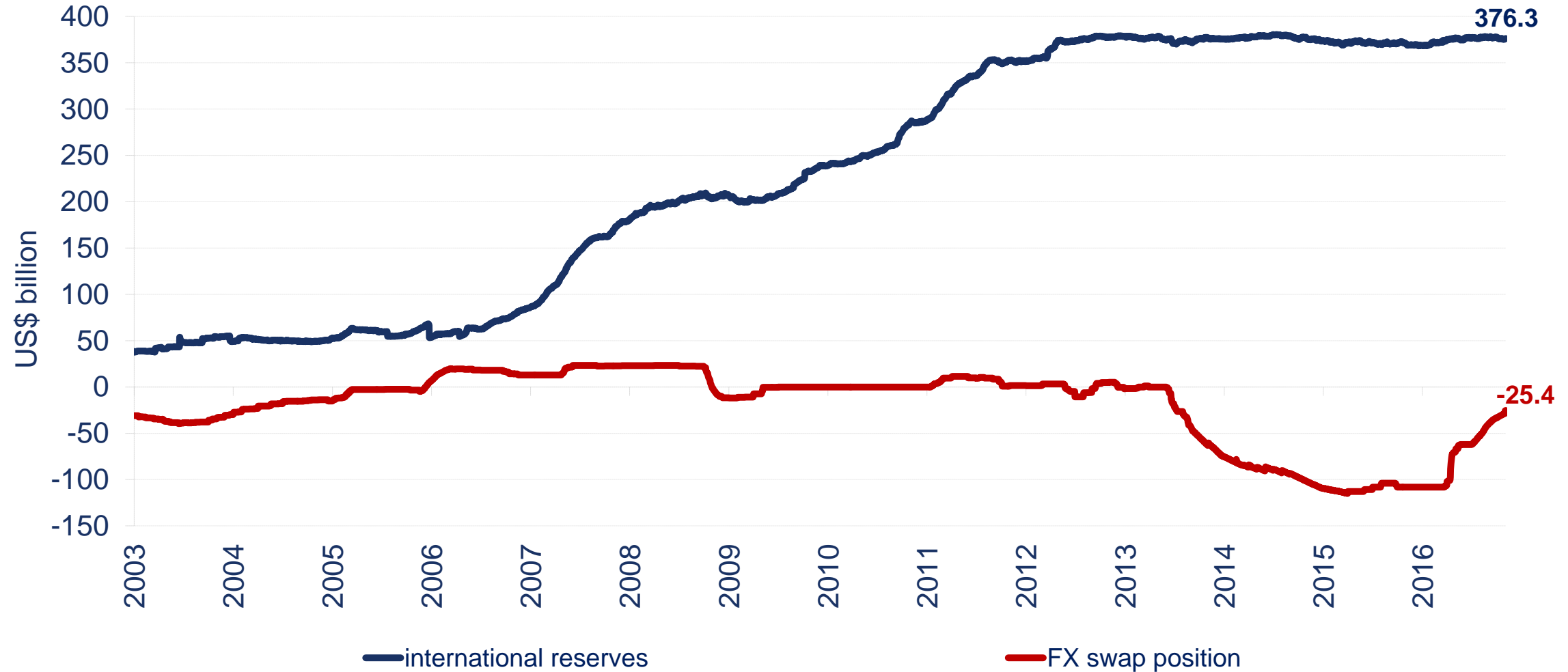


# Resilience Factors: Financial System and External Accounts

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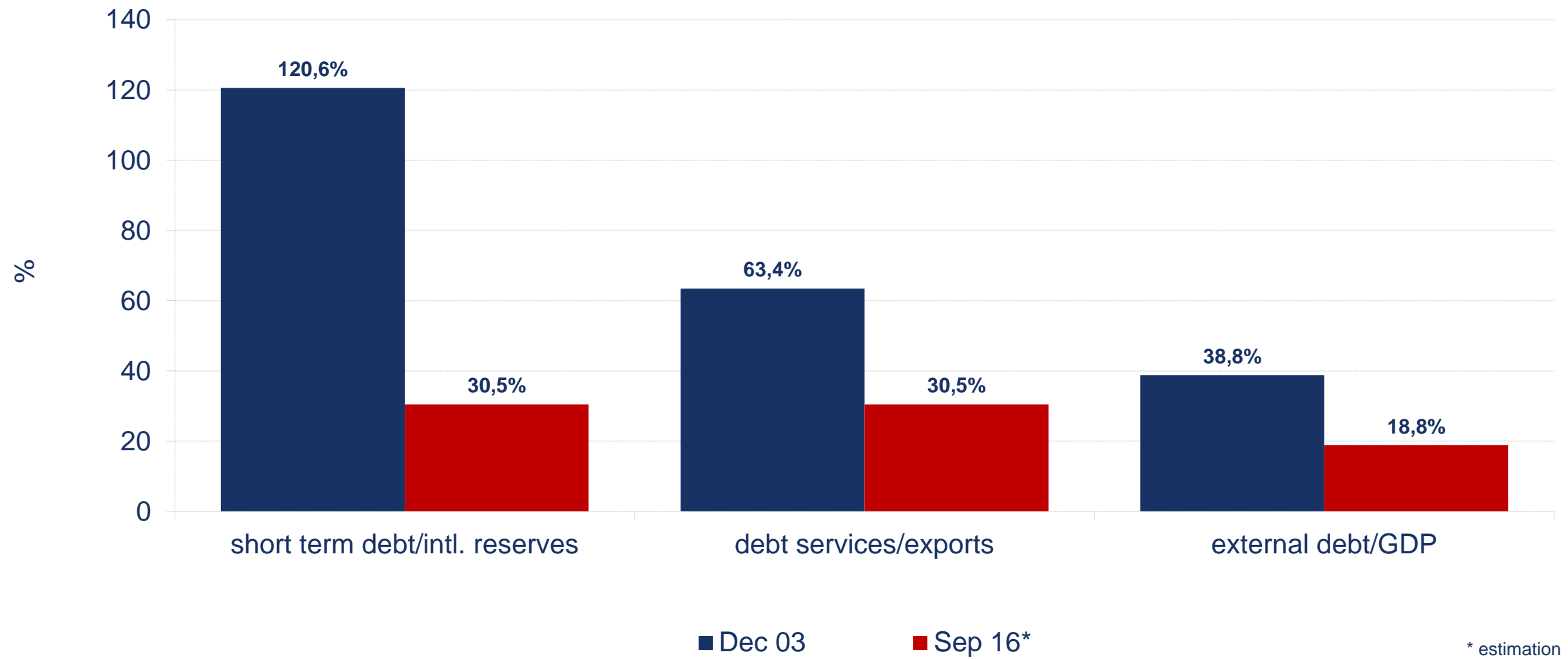
- Low exposure to forex liabilities, large domestic investor base for public debt financing and sound current account financing assure resilience to (negative) headwinds from the international economy and limit contagion from external volatility
- Financial system with solid capital structure and limited leverage, despite historically large recession.

# Reduced CB Vulnerability: FX Repos and Reserves Cushion

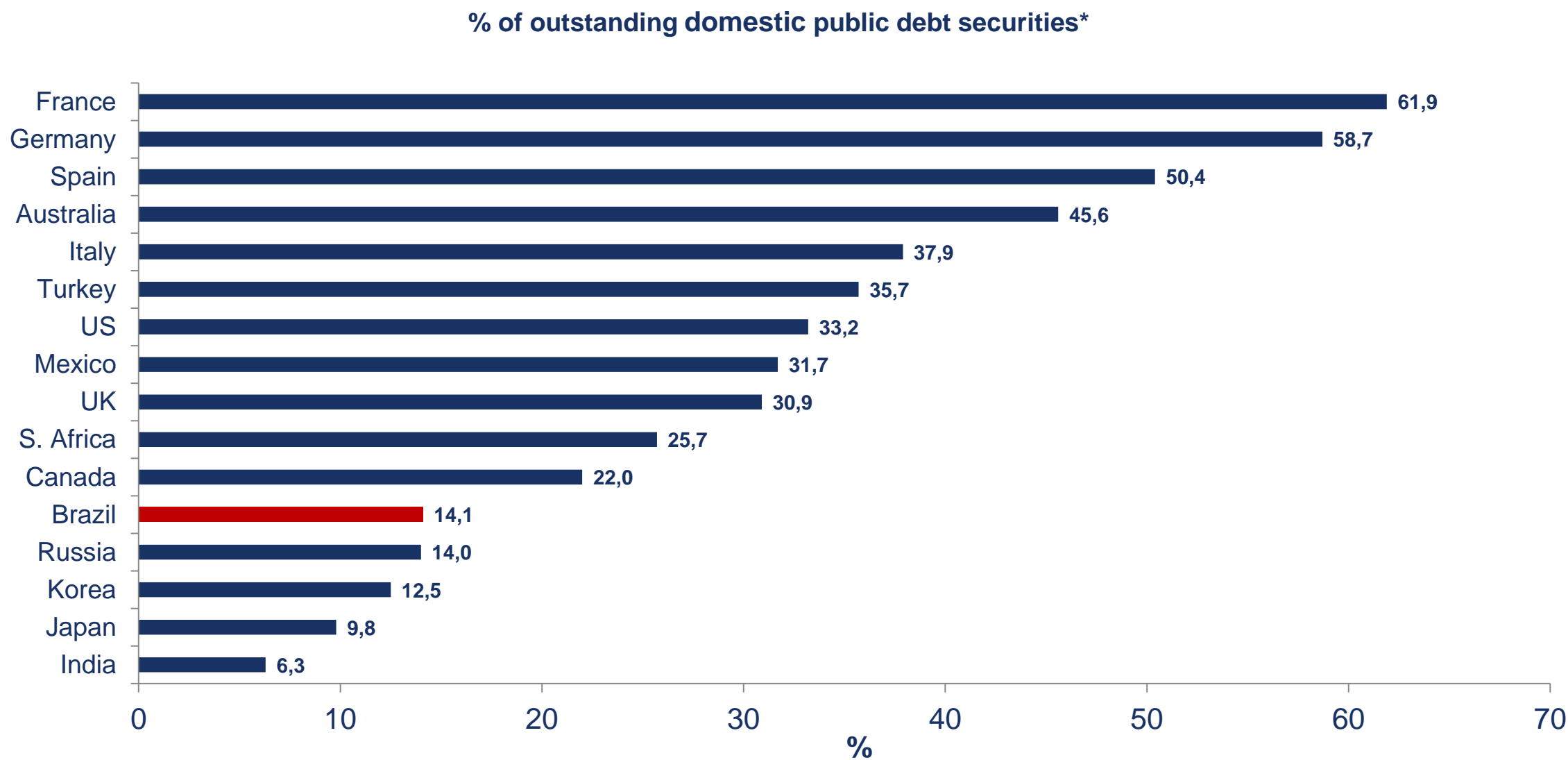


\* As of November 3<sup>rd</sup>

# External Debt Ratios

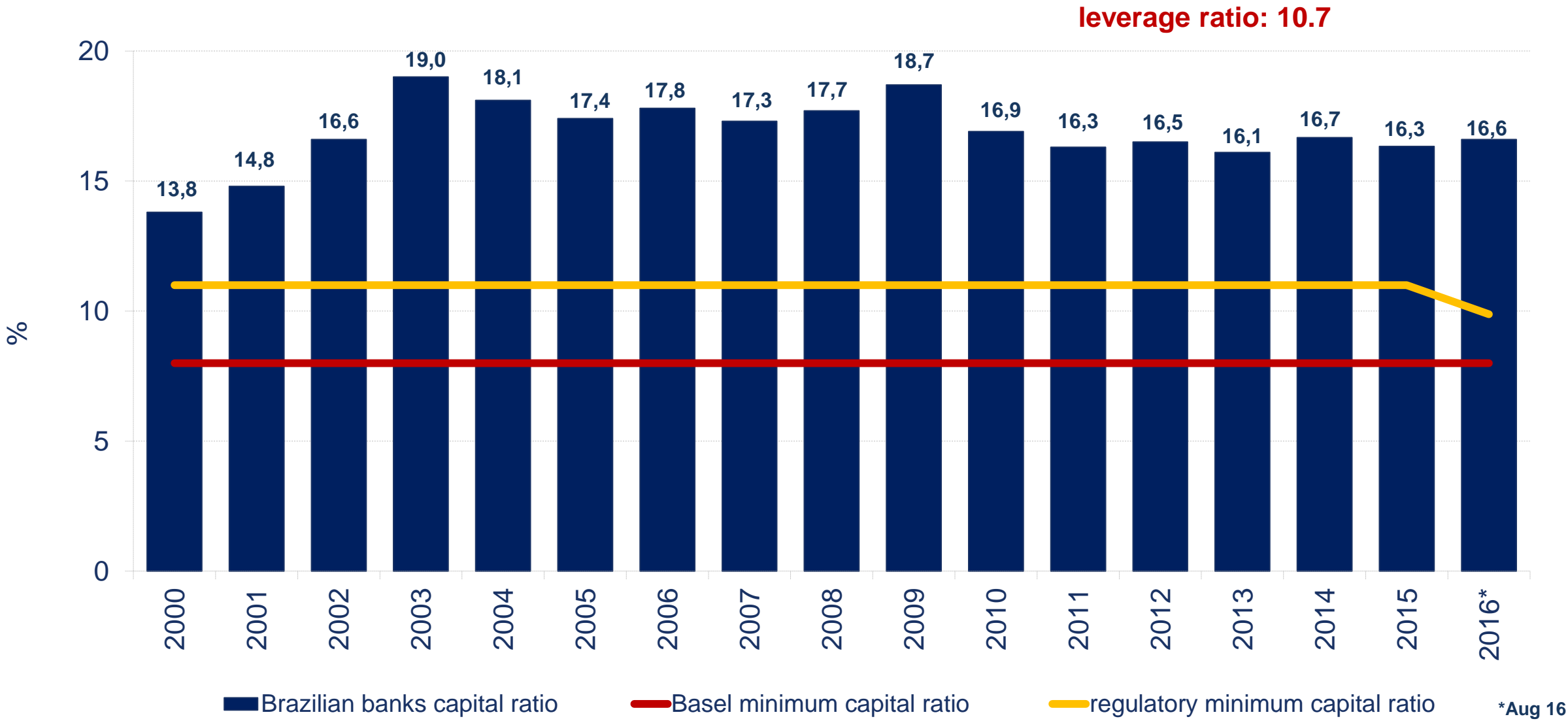


# Public Debt Held by Non-Residents – International Comparison

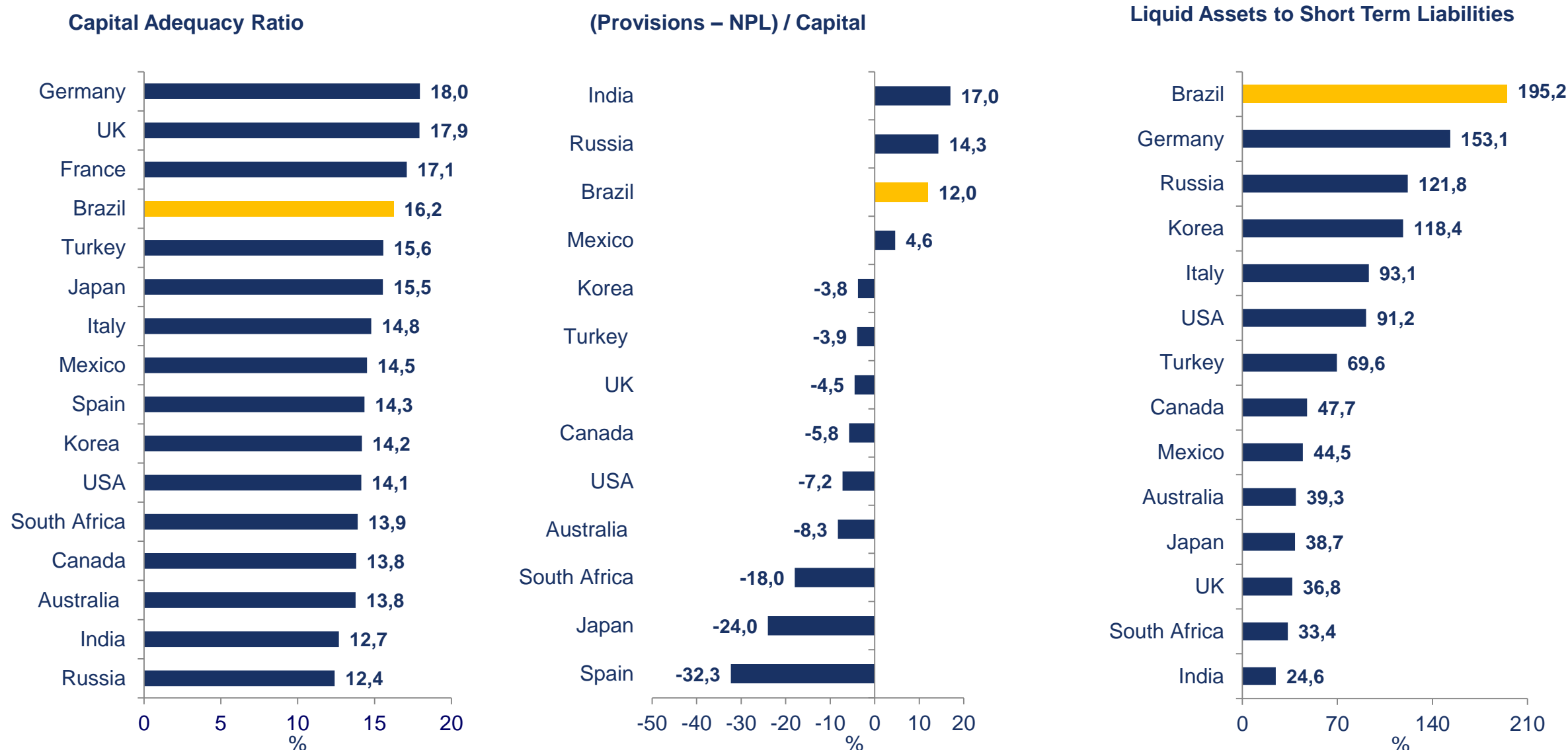


\* The latest data reported by the IMF Fiscal Monitor in Oct 16

# Brazilian Banks - Capital Adequacy Ratio

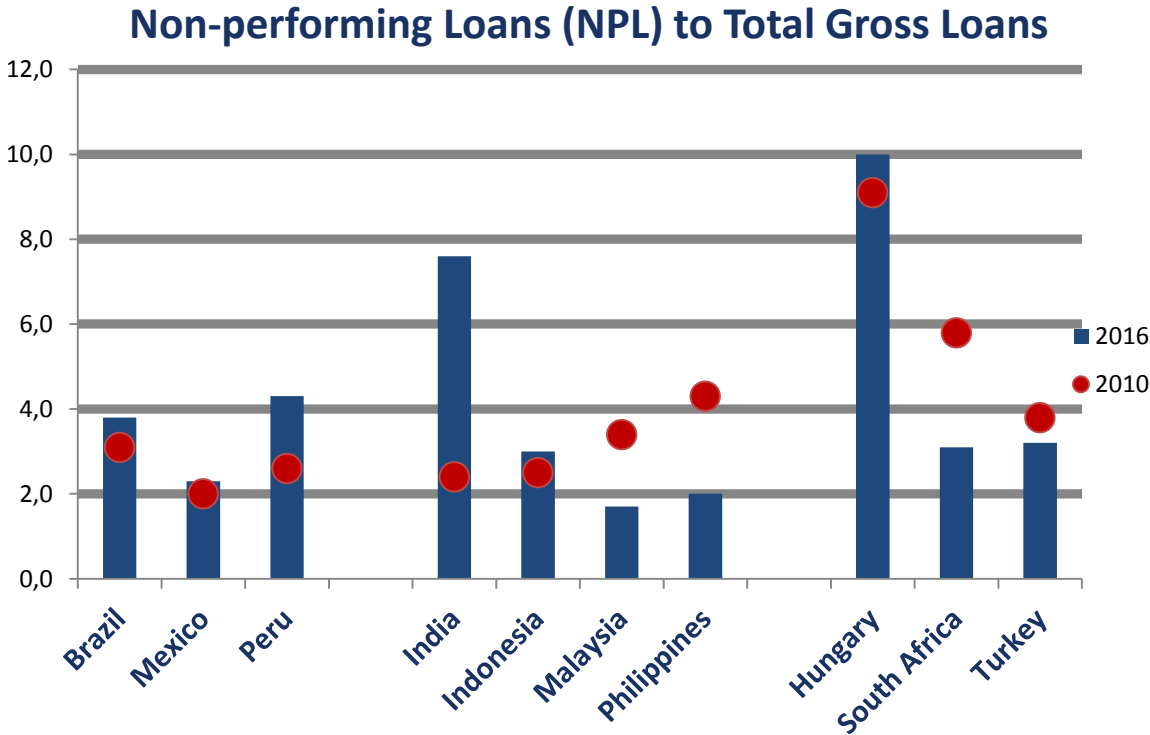
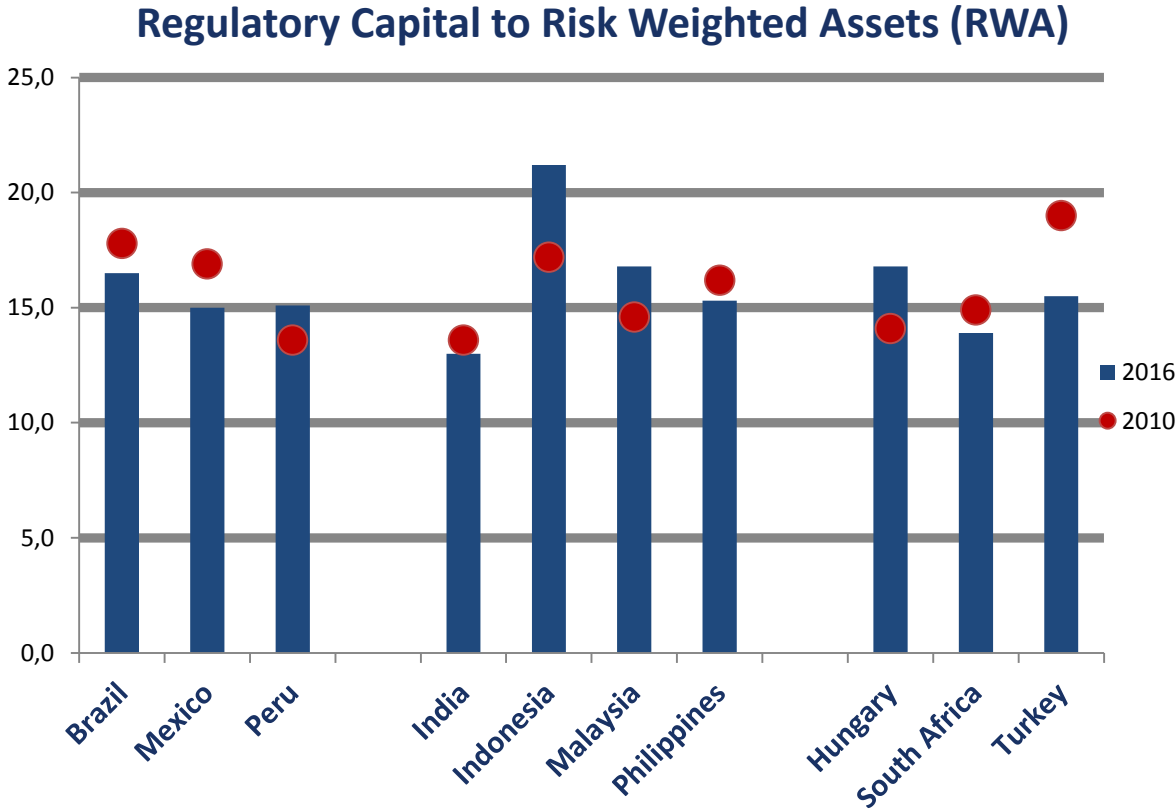


# Brazil: Comparative Financial Soundness Indicators\*



Source: IMF (FSI) \*latest available data

# EM and Brazil: Banking sector in an stronger position



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# Outlook for the Brazilian Economy:

## Conclusions



# Outlook for the Brazilian Economy: Conclusions (I)

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- Progress on implementing the new comprehensive policy agenda sustains **positive turnaround in confidence.**
- **Structural Fiscal Reform is critical** to bring fiscal equilibrium back, assuring public debt sustainability and **removing uncertainty for longer horizons**
- **Productivity and growth agenda** with a favorable business environment will **unleash private sector investment** in logistics and Infrastructure, **reinforcing the virtuous cycle**

# Outlook for the Brazilian Economy: Conclusions (II)

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- Progress in inflation convergence:
  - Depends on the sensitivity of services and non tradable prices to monetary policy and output gap
  - May be reinforced by a faster than expected fiscal reforms implementation
  - Will influence magnitude and pace of potential monetary policy accommodation
- Despite transitional risks, Brazil can show gradual but firm progress addressing domestic challenges and withstand external headwinds
- Goal is to recover sound fiscal dynamics, keep inflation low and stable and achieve sustainable growth. There is a mutual reinforcing and synergic nature on this policy agenda.



# ***Thank You!***

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**Tiago Berriel**

Deputy Governor for International Affairs  
and Corporate Risk Management

***Brazilian American Chamber of Commerce***  
New York City

*November 9<sup>th</sup> 2016*